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HOUSING: TAMING THE ELEPHANT IN THE ECONOMY

A report to the Housing and Productivity Research Consortium

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The Blind Men and the Elephant

The story of the blind men and the elephant is an ancient Indian parable of a group of blind men who are introduced to an elephant. They are asked to define their notion of the elephant through touching a particular part of the large creature.

Of course, the trunk, the tusks, the tail and the flank elicit different responses, images and metaphors. In consequence, the men all have different conceptions of the word 'elephant', based on their partial experience of what the elephant is and have difficulty communicating the idea with their blind colleagues.

Discord and disorder are likely consequences.

But, at the risk of allegorical overkill, the housing system elephant is not only a beast now poorly grasped by policymakers, it is also one that is rampaging through the economy.



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Executive Summary

Key points

- Over the last 40 years Australia's housing system outcomes have exacerbated inequalities of both income and wealth, compromised economic and financial stability, and negatively impacted on labour productivity.
- At the heart of the difficulty is a substantial capacity deficit – of skills, institutions and governance structures – to both understand the housing system, and to construct a coherent housing market strategy and the policies to deliver it.
- The absence of a coherent housing market strategy matters, not only because the housing market impacts the whole housing system, but also because it is central to the development of the national economy.
- Among Australia's leading economists and housing experts, the overwhelming majority (85% in our survey) back the contention that 'policymakers should pay greater attention to the economic productivity effects of housing market outcomes, such as costs, tenure, quality and proximity to work'.
- By a margin of almost four to one (67% versus 17%), leading economists and other surveyed housing experts share the concern that 'the absence of a coherent housing market strategy for Australia now constitutes a significant barrier to structural adjustment in the economy and to an effective post-pandemic recovery'.

But while there is wide recognition that the economy drives the housing market, there seems little recognition that outcomes in the big housing system have significant feedback effects on the economy itself. Housing matters in employment, income, consumption, wealth and debt.

The scale of the housing market in the Australian economy and the diffuse, often disconnected, spread of policy powers that address different aspects of this system make the Parable of the Blind Men and the Elephant a perfect metaphor for our current predicament.

This strong conclusion has emerged from an online survey and interviews with a panel of 87 leading Australian economists and sector experts¹ (collectively termed 'experts' from this point on) and from a major review of national and international literature² undertaken for the Housing Productivity Research Consortium. This report presents a synthesis of these findings and the conclusions and recommendations we draw from them.

Crisis? What Crisis?

By any measure, the housing market is a major sector in the Australian economy: the housing stock is now valued at an estimated \$8.1tn³— double the value of a decade ago – and almost three times the value of Australia's superannuation funds; housing construction provides 5% Australian jobs; consumer spending associated with rising house prices shape 15% of GDP; housing wealth comprises well over half of household assets; Australians, with record debt to income ratios, have \$2.1tn in outstanding home loans⁴.

But at the same time, since the mid-1990s, housing prices have consistently outstripped income growth, the national home-ownership rate has fallen by 4% and the ownership rate for under 35s has collapsed, building in structural problems for future decades.

1 MacLennan, D., et al. (2021) Housing and the Economy: Interrogating Australian Experts' Views; Sydney: UNSW City Futures Research Centre <https://cityfutures.be.unsw.edu.au/>

2 These will be published as three separate reports in July 2021.

3 <https://www.corelogic.com.au/news/australian-housing-market-surpasses-8-trillion-valuation>

4 <https://www.ibisworld.com/au/industry/mortgages/1909/>

For the economy, these trends reflect a triple crisis where housing price outcomes have exacerbated income and wealth inequalities, contributed to economic and financial instability and – often unrecognised – diminished productivity and growth.

Unfortunately, large system scale does not seem to have led to big thinking in designing policy and strategy for the national housing market and this contributes to problematic outcomes. For households, pervasive problems of affordability keep spreading up income and age ranges and the prospect of home-ownership for young Australians has been damaged by present policy approaches.

In responding to housing economics evidence, Australian housing policy actions seem to perfectly meet Einstein's test of madness: in repeating the same actions and expecting different results. Now, emerging from potentially the worst recession of the last 100 years, we already have a new housing boom rippling across the nation. Of even more concern, the RBA, almost flying in the face of advice from other central banks, has remained sanguine on rising house prices and argued they are good for growth. This view has no validity if the longer-term evolution of the economy and the housing market is the concern.

This key point from our research provides evidence that across the whole of government, and different orders of government, there now needs to be an integrated housing market strategy to deliver more Australian homes and more sustainable house price appreciation. Now, like the blind men and the elephant, policy makers grasp at different pieces of policy impacting housing, including tax policy, monetary policy, macro-prudential policy, housing, infrastructure, planning and other sector actions, but never grasp the whole system.

Policy makers, restricted by their narrow roles, never fully recognise – let alone placate – the economic elephant that is the housing market.

What Housing-Economy Links and Impacts Need To Be Recognised?

Productivity impacts

Residential property has profound impacts on wider economic productivity that are ignored in contemporary policy debates.

- Among Australia's leading economists and housing experts, the overwhelming majority (85% in our survey) back the contention that 'policymakers should pay greater attention to the economic productivity effects of housing market outcomes'.
- As many as 91% of our survey respondents agreed that 'high housing costs reduce consumption of non-housing goods'.
- Nearly three quarters (73%) agreed that 'metropolitan housing market distortions such as sub-optimal labour market matching due to high prices and rents are impairing economic growth and productivity'.

Rising residential housing markets can support positive impacts on productivity; for example, when increased housing wealth is used as collateral to borrow to fund non-housing investments. At the same time, residential investment can 'crowd out' investment in more productive activities and lead banks to prioritise lending to housing consumption and 'rent seeking' investment with no positive feedback into economic productivity. Australian evidence on the balance of these effects is missing.

High metropolitan house prices and rents push lower and middle income households further away from employment-rich locations reducing overall labour productivity by diminishing the 'thickness' and matching effectiveness of labour markets.

Unaffordable, poor quality and badly located housing has clear and well-documented impacts on human capital formation, through their repercussions on an individual's ability to develop

productive capabilities. Despite its importance to economic growth and employment, evidence on the actual productivity of the residential construction sector is lacking.

In a fairly dynamic economy like Australia's where we have embraced micro economic reform a fair bit ...[but] we've never been brave enough to touch housing markets [quotation from in-depth interviews report]⁵.

We're still building half of our housing out on the urban fringe at ever more distant locations. So what that's doing is wasting human capital, and we can't afford to waste human capital [quotation from in-depth interviews report].

5 MacLennan, D., et al. (2021) Housing and the Economy: Interrogating Australian Experts' Views; Sydney: UNSW City Futures Research Centre

Instability impacts

Over several decades Australia's housing system has become more unstable, due to housing and mortgage market changes, and now poses a greater threat to economic and financial sector stability.

- Nearly three quarters of experts (73%) in our survey believed that 'high mortgage debts and burdens (reflecting high house prices) raise instability risks for the economy'.
- 85% of these experts rejected the statement that 'short-term interest rate policies are sufficient to ensure macroeconomic stability'.

Overall household debt has risen substantially relative to GDP from 70% in 1990 to almost 185% by 2020. Some three quarters of this debt is in mortgages and 60% of debt held by Australian banks is in the form of residential mortgages, one of the highest globally and greatly exposing the banking system to potential disruption.

International evidence suggests that house prices have, since the 1960s, become highly volatile and closely correlated with the business cycle. There is clear evidence from Australia and elsewhere that high and rising house prices have substantially exaggerated 'normal'

business cycles, triggering and reinforcing wider systemic financial and economic crises.

Price changes that shift housing wealth have potentially significant transmission links back to the economy that are not captured in conventional/housing starts cyclical models, yet are key to understanding contemporary economic and financial instabilities.

Households may wish to hold more housing assets than required to meet their consumption demands. That is, investment or speculative demands. Aspiring rental investors are the most obvious example, but home-owners - especially older owners, living in homes with excess space simply because housing has a high net asset return - add substantially to this. Australian tax settings boost that speculative demand. APRA interventions, curbing access to interest-only mortgages, restrained investor lending in 2014 and in 2016 and had a beneficial, albeit temporary, effect in moderating these pressures. Investor purchases have risen sharply into 2021 as a growing share of property purchases. APRA regulations also frame 'safe mortgage lending' for owner occupiers. However, Australia's long-upward trend in the household debt to GDP ratio remains unchecked. And APRA's current reluctance to tighten regulations in the 2021 boom reflects a relatively short term view of the potential stability consequences.

Inequality impacts

Housing system outcomes of recent macro-economic policies, including QE, have exacerbated inequalities of both income and wealth.

- By a margin of five to one, economists and other experts saw 'status quo' economic policies as having exacerbated income and wealth inequality.
- Almost 9 out of 10 rejected the statement that 'claims that house price inflation has worsened income and wealth inequalities in Australia are overstated'.

Homeownership rates have dropped, halving for the under-35s since 1995, while housing wealth

has concentrated in the hands of the over 65s. Nevertheless, the home-ownership rate among over 65s is predicted to fall from around 79% today to only 65% by 2056⁶.

The growth of homeownership from the Menzies era until the mid-1990s was widely regarded as a spreading of wealth and a reduction of overall inequality. This process has effectively reversed as asset speculation in housing has driven homeowner gains much more than the traditional life cycle saving objectives.

As a result, household wealth distribution in Australia is now significantly unequal and markedly more unequal than incomes.

6 Brendan Coates and Tony Chen (2019). Fewer retirees will own their home in future, and that has big implications for policy. The Conversation, Friday 12 April.

The tax system wasn't a problem in the 1950s because we didn't have ... asset price inflation. Once [this] came into it, the kind of tax system we had became a problem and we didn't change it [quotation from in-depth interviews report].

It's going to be very hard to prosecute economic policy that continues to polarize people So a lot of the things that you need to improve productivity, you run into barriers if you have a polarizing inequitable society [quotation from in-depth interviews report].

Housing and the Economy: Taming the Elephant

Increasingly commentators, and national level policy politicians, comment that housing is a 'supply side problem' and many highlight 'planning' as the major cause of slow delivery of inadequate stocks of land and housing. Such conclusions are often based on anecdote and are somewhat incomplete. Housing price inflation is driven by excess demand. But rapid demand stimulus as well as sluggish supply can generate excess demand for housing. And even if sluggish housing supply rather than over-stimulated demand is problematic, then it is important to understand which element in the complex supply chain for homes is at fault, including the timing of land release by developers and financial constraints on development capacity – and not simply resort to blaming 'planning'. At local, metropolitan and national levels, housing supply chains need to be

much better understood. But our policy-making is bedevilled by a substantial deficit in the skills, institutions and governance structures needed to better understand Australia's housing market and strategies to make it more effective and stable.

A system that raises housing costs for all Australians, that raises instability and lowers productivity, does not serve the nation well. And as for rising housing wealth, it is not like the wealth created from effort and innovation, for that creates gains for all. Rather, it makes some Australians – the affluent and older – better off, by making younger and poorer Australians, and also future buyers, worse off.

The housing elephant is in the living rooms and Party rooms of Australia and is set for another rampage through the economy. It's time to tame it!

Key recommendations

Reversing the substantially problematic trajectory of Australia's housing system over recent decades will call for extensive tax, regulatory and other policy reforms. However, a pre-condition for any such program of work is the reshaping of relevant over-arching institutional frameworks. It is with this understanding in mind that the following measures are proposed:

- Given the fundamental nature of the issues involved, given their disparate nature across departments and levels of government, and to frame renewed government approaches, a **Royal Commission on Housing Future Australia** should be set up.
- **A Cabinet-rank post responsible for Housing Policies and Outcomes** should be re-established in the Commonwealth Government, a position that – given the highly diverse range of relevant policy instruments – should be closely linked to the Department of Prime Minister and Cabinet.
- As a crucial vehicle for inter-government co-ordination in this policy area, a **permanent Housing Committee** should be created as part of the National Cabinet structure.
- The Commonwealth Government should commit to developing a **National Housing Strategy**, including a housing market strategy.
- Expand the National Housing Finance and Investment Corporation (NHFIC) as an enduring **National Housing Agency** tasked with informing government policy-making, championing actions to enhance housing-economy outcomes, promoting affordable housing development and re-establishing the analytical capacity of the former National Housing Supply Council.
- In the immediate term, Australian governments should give consideration to **switching housing stimulus** efforts from market housing to the social rental sector with potentially lesser inflationary consequences.
- The Australian Government should **expand the formal accountabilities of the RBA** to include maintaining a more price stable and well-functioning housing market.

1. Forward Looking Housing Policies for the Economy

1.1 Making Better Housing Policies

The major aim of this report is to encourage the resetting of how economic and housing policymakers, sector lobbies and commentators think about the relationships between housing system outcomes and a number of key economic outcomes. We argue that there are policy measures and frameworks for managing an essentially market-led housing system, containing a complementary and effective non-profit sector, that might lead to a more economically competitive, stable and equitable Australia. Quite complex economic arguments are presented in non-technical fashion and the evidence to support the case for policy paradigm change is set out here in very compressed form. This report summarises contentions that are presented in much fuller detail in five associated papers, including one published earlier in 2021^{7, 8}.

1.2 Policies Losing Sight of Housing, Damaging the Economy.

Almost five years ago, in a compelling speech about reaching for more affordable housing outcomes, the then Commonwealth Treasurer, Scott Morrison, concluded that Australia could not keep doing the 'business' of housing policies the way it had done in the previous decade. But

doing the same thing, and sometimes less of it, has been what the present government, led by Mr Morrison, has done. Australian, and other, governments have aspired to economic aims of higher productivity, greater stability and poverty reduction and, within that broad framework, to reduce homelessness, construct better housing, more affordable homes and expand homeownership. But alongside these aspirations, the past 20 years have also seen rising concerns over economic and financial instability, rising inequality, economic efficiency stagnation, and deteriorating housing outcomes.

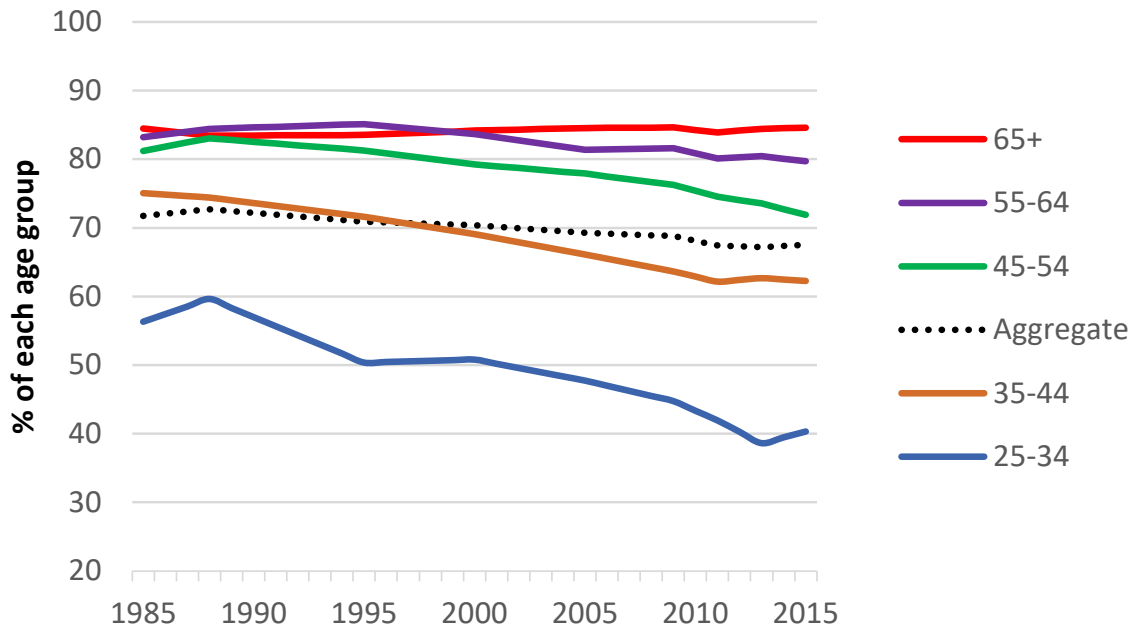
Unfortunately, it appears that Australia's policy settings, in so far as they impact housing, have patently failed to deliver the desired outcomes, with little indication these policy settings have changed in the five years since Mr Morrison's comments. The nation's twenty-first century housing system has been characterised by growing homelessness; minimal social housing investment; rising housing costs in relation to incomes for low earning households inducing relentlessly rising affordability stresses for this population cohort and growing barriers to homeownership; internationally high and rising levels of household and housing debt relative to GDP; burgeoning numbers of frustrated younger households seeking decent rental housing and often paying record high rents as many wait (for parental help) to access homeownership; home-ownership rates for young adults down by a fifth since 2000, and the overall tenure share of ownership fallen by down by 4% points over this period to its lowest level in over 40 years – see Figure 1⁹. And forward forecasts suggest significant further falls in the three decades ahead, see Figure 2.

7 MacLennan, D., Long, J., Pawson, H., Randolph, B., Aminpour, F. and Leishman, C. (2021) Australian experts views of housing and the economy: Abstract dreamings or real directions? Sydney: UNSW City Futures Research Centre https://cityfutures.be.unsw.edu.au/documents/630/Expert_view_report_06.pdf

8 These more technical and more fully referenced papers discuss our exploration of expert views, the links between housing outcomes and economic and financial instability, the effects of housing wealth in the economy and, finally, the productivity implications of housing outcomes. It is hoped that these will provide a basis for discussions involving experts and policymakers from Australia and comparator countries. The team are happy to receive comments on this, and the follow-up documents and Duncan MacLennan can be contacted at duncan.maclennan@glasgow.ac.uk

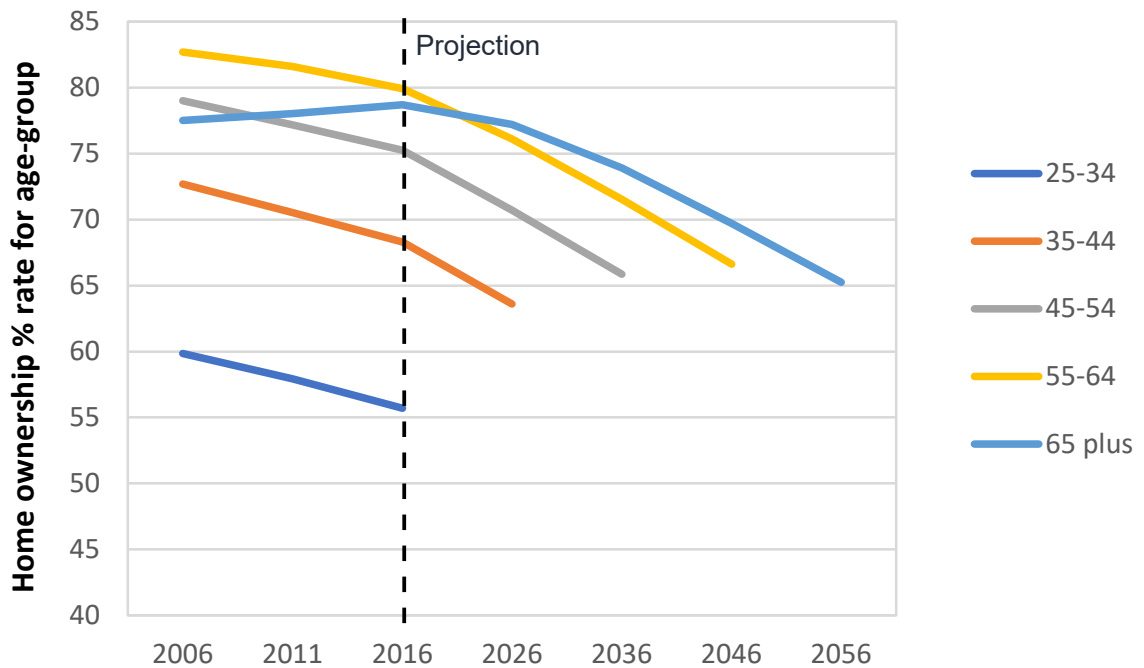
9 Although details differ, similar adverse shifts in outcomes (in relation to stated official policy objectives) have been the hallmark of housing systems in this millennium in many of the (supposedly) pro-ownership countries and Canada and the UK were used as particular reference comparators in the literature review.

Figure 1. Home-ownership rates by age cohort, 1985-2015.



Source: ABS Surveys of Income and Housing and Household Expenditure Surveys 1984 to 2015-16

Figure 2: Home-ownership rates – projections by age cohort 2016-2056



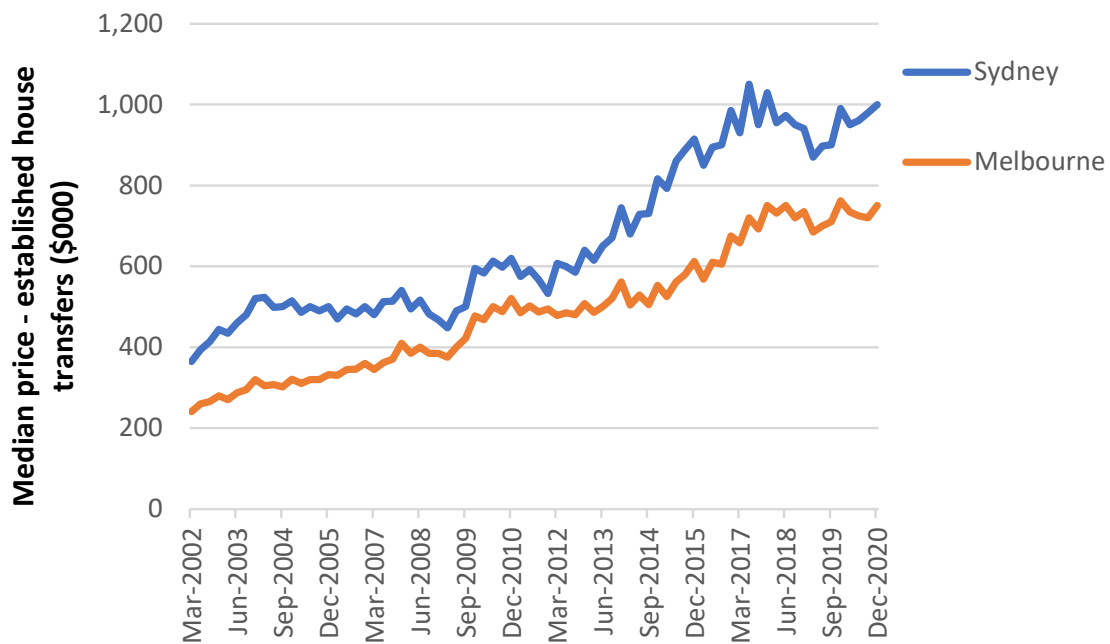
Source: Brendan Coates, Grattan Institute (2020) <https://nationalseniors.com.au/news/latest/unaffordable-housing-is-the-biggest-threat-to-a-comfortable-retirement>

Note: home ownership rates calculated on different basis from Figure 1.

Our literature review for this project emphasises that these issues have been accumulating for decades, although by and large officially unnoticed or ignored. The identified problems largely reflect high and rising real housing prices, see Figure 3 for price changes in Melbourne and Sydney for 2002-2020, relative to the growth and distribution of incomes. For longer than the last decade there have been markedly high

increases in prices and rents through a period when, in contrast, there has been excess labour supply and low wage rate increases, usually less than 2% per annum¹⁰. Critically, evidence is presented below that current housing outcomes reinforce inequality, economic instability and low productivity growth in Australia, yet remain unaddressed by coherent policies to shape a more effective housing system.

Figure 3: Median house prices, Sydney and Melbourne



Source: ABS Cat 6416.0 Residential Property Prices, Eight Capital Cities, Tables 4-5

We do not discount the conventional merit good arguments for enhanced housing programs that would improve wellbeing for low-income households by reducing costs and improving quality. There are informed moral arguments for social justice and redistribution, with more occasional arguments to address market functioning failures. But these contentions are not the focus of this report. Put simply, the case presented here is that, given the goals of higher productivity and expanding homeownership espoused by all Australian governments over the last quarter century, this is a story of sustained national failure. Housing outcomes have not only persistently fallen short of official aspirations, but they have also had negative feedback effects on the long-term functioning of the economy.

There is policy failure as well as market failure, as governments neglect to acknowledge or act to reduce the economic harm that adverse housing outcomes impose.

This review of research literature and exploration of expert views among colleagues working on housing, economy and finance issues in Australia, concludes that unsatisfactory housing outcomes contribute to poor national performance on promoting economic stability, growing productivity and limiting inequality. Granted, it is widely recognised by governments that demographic and economic change drive housing market outcomes. However, taking a longer-term and system-wide perspective,

¹⁰ Davies, K. (2021) Navigating by the Stars. Coolabah Capital.

such housing outcomes today shape economic performance tomorrow, and indeed decades ahead. These feedback effects, with a few exceptions in relation to construction multiplier effects, are often unrecognised and seldom seen at the forefront of policy decisions at Commonwealth and state/territory scales. For example, the research team has previously demonstrated that the location and type of housing investments have significant effects on labour productivity in the Sydney metropolitan economy¹¹. Yet, in contrast to other policy spheres (such as transport infrastructure investment decisions, for example), the housing channel to productivity effects continues to be ignored in official policymaking.

Performance of the housing system, one of the key integrative systems in the economy and society, is now a very large, often rampaging, elephant in the government's room. 'Business as usual' housing policy responses are well exemplified by the metaphor of the blind man and the elephant. Different, siloed policy sectors (social welfare, social security, health, environment, construction, infrastructure) make small policy tugs at separate tusks, or the tail or the trunk and the big system is neither fully understood, nor recognised, by the central agencies of treasury/finance ministries and Prime Minister's and Premiers' Departments.

Over the last four decades shifts in social, expenditure and economic policies, at all levels of government, have fragmented the housing system perspective and lost sight of why and how the housing elephant matters in national, regional and metropolitan economies. At the same time, monetary policy stances (previously focused on narrowly defined inflation targets and now somewhat singularly focussed on keeping Australian unemployment rates below 5%) and macro-prudential regulation policies (sometimes defined with little knowledge or modelling of major housing markets) have cut across, in uncoordinated ways, sectoral housing policies and fiscal policies that shape housing choices.

11 MacLennan, D., Randolph, B. and Crommelin, L. (2019) 'Strengthening Economic Cases for Housing, Report for the Community Housing Industry Association. City Futures Research Centre, UNSW Sydney.

A relevant question to both governments and oppositions is whether they can credibly claim that their suite of sectoral, monetary and fiscal policies has been well-designed to secure the housing outcomes that will fashion a more competitive, productive, fair, and advancing Australia? Standing back from short term political/electoral goals, can the expert perspectives and research evidence unpacked below be simply dismissed as misleading and misinformed?

1.3 Building Back Better as the Catalyst for Long-Needed Rethinking

The case for making housing policies differently in Australia has been growing for decades. The pressing imperative to act now, and the policy context for doing so, is driven by the need to build back better from COVID-19. That context is difficult but also full of opportunities for fundamental policy re-appraisal and reform.

At the time of writing the nation has endured more than a year of damaging personal, social and economic losses imposed by the pandemic. However, by April 2021, Australia's economic recovery was relatively advanced, and as vaccination programs unfold similar sentiments have been expressed across most OECD economies. The April 2021 meetings of the International Monetary Fund, that were quickly followed by upwardly revised OECD growth forecasts, emphasised a forward look for the advanced economies recognising that market processes, economic activity, trade and growth were beginning to recover from the 2020 shock. It is expected that this process will continue, boosted by significant stimulus packages, with 2019 levels of output re-achieved by end 2021 or during 2022. Such ongoing recovery expectations are widely expressed by the Commonwealth Government. At the same time the acceleration of the pandemic in less prosperous countries, not least India, will limit global recovery over a more prolonged period.

In their commentary on Australia's continuing economic recovery in macro-economic aggregates such as unemployment, inflation and growth, analysts also advise much caution

in pronouncing on the sectoral and geographical patterns of recovery and lingering damage. The key, widespread economic policy assumptions are that following removal of 'special COVID-19' protection measures in relation to jobs, incomes and businesses in March 2021, there will be high but then quickly reducing unemployment (especially for younger, female, and unskilled workers) without inflation.

Permissive monetary policies and the willingness of governments to stimulate aggregate demand in the economy, via debt-funded investment, will be as important in the ongoing recovery as in forestalling unprecedented depression through the 'great market stop' of the last 15 months. Indeed, in contrast to broadly comparable countries, the Commonwealth Budget announcement in April 2021 noted an underspend of \$21billion for 2020-21, the peak year of COVID costs, but also intimated, despite strong forecast economic recovery, increased government spending of successive amounts close to \$25bn for each of the next three fiscal years¹². There has been, since 2019, a globally strengthened policy commitment to low interest rates to encourage borrowing and investment and, additionally, substantial rates of quantitative easing to facilitate private spending growth, but also to facilitate public borrowing to raise publicly financed infrastructure investment (compensating for private sector demand deficiencies).

Alongside major adjustments in macroeconomic policy (especially in monetary policy) and in their support for businesses and household incomes in 2020, governments also implemented substantial emergency housing and homelessness initiatives. In many respects the Australia's national and state/territory governments deployed policy tools and resources generously and effectively to mitigate pandemic-generated housing security and homelessness risks in 2020¹³. The mix

of income supports, and measures to protect against rent and mortgage arrears prevented much disorder and distress. Indeed, in the initial phase of the pandemic low-income households generally saw significantly increased incomes as a result of the emergency measures. Rental market pressures, and rents, declined modestly in some downtown capital city locations, while households with mortgages benefitted from reduced interest rates.

House prices and rents across most Australian markets have bounced back sharply since the last quarter of 2020, imposing renewed stress on low-income renters and aspirant first homeowners. It now seems that the COVID-19 pandemic has temporarily impacted Australia's housing difficulties rather than changed their fundamental long-term character.

Internationally and in Australia some governments have combined economic stimulation through infrastructure investment with the promotion of social housing supply. The Canadian government, for instance, added a further \$2billion for rental housing provision in its April 2021 Federal Budget. Similar non-profit stimulus has occurred in the UK Government's measures for England (also launched in early April), though this has been outweighed by wider housing market stimulus through suspended stamp duty charges and enhanced grant support for first homebuyers. The Australian Government has significantly boosted first home buyer support but has declined to target stimulus to either market or non-market rental housing. In contrast, the Victorian Government has pledged major (by Australian standards) expansion of non-market rental provision.

In common with their counterparts in key comparator countries, Australian governments have taken housing issues seriously through the 2020 emergency, especially at the state/territory level. Policy lobbies have also effectively highlighted how past housing policies (and inaction) contributed to national vulnerability to the pandemic. Societal risks were heightened not only by large homeless populations liable to infection, but also by the extent of cramped living conditions, inadequate broadband connectivity

12 BDO (2021) 2021 Federal Budget Report. Canberra.

13 Pawson, H., Martin, C., Sisson, A., Thompson, S., Fitzpatrick, S. and Marsh, A. (2021) COVID-19: Rental housing and homelessness impacts – an initial analysis; ACOSS/UNSW Poverty and Inequality Partnership Report No. 7, Sydney <https://bit.ly/3p2er65>

and remoteness from work locations (for poorer households in all tenures) that compromised scope for adaptation to COVID-19 conditions.

As citizens and governments look forward to global recovery, housing policy experts and lobbies have become concerned about two related sets of issues. First, what distress and disorder will arise, especially in rental markets and for low income homeowners, as COVID-emergency measures are removed? Secondly, how can housing systems be placed on a better footing for the long term?

1.4 Back to Business as Usual?

There must be a concern that, as economies recover lost ground, housing policymakers, and indeed many of those who lobby for housing programs have reverted to their pre- COVID norms and rhetoric, focusing on specific narrow policy measures and short-term goals and debates. Writing in early 2021, the lack of bigger picture framing of housing policies and a renewed reluctance to use the housing market 'elephant' to pull real system reform was already all too apparent.

Rising real house prices (often solely viewed as indicating a thriving economy - as opposed to a manifestation of speculative behaviour, inappropriate monetary policies and/or supply system failure) – are the major, adverse, recursive link from housing outcomes to the wider economy. Albeit originating around Q3 2020 amidst deep economic recession, Australia experienced a continuing (and broadening) house price boom. Record median house prices were being recorded across most metropolitan and regional markets by April 2021.

Property sector commentators have, through 2020, highlighted shifts in favour of many regional locations and away from inner cities, as well as towards houses and away from apartments. This has been seen as reflecting changing preferences for lower density living among relatively affluent and middle-income households, facilitated by new-found locational freedoms on working from home, or resulting from accelerated early retirement. By early 2021

the relative performance of core metropolitan areas also manifested price rises and stabilising rents. And all of this has occurred alongside minimal immigration which has cut population growth by well over half.

As in Canada and the UK, Australia's real house prices rose by around 10% in the year to April 2021 and increases for the coming year are widely predicted at 10-14% (although some experts take a very different view and highlight potential sharp bubble deflation). Many have expressed surprise at this emerging price boom. However, low mortgage rates, allied to the reality that COVID-19 has had concentrated economic damage, with for instance many middle- and upper-income professional households incurring few job or income losses, highlights strong incentives to invest in housing. Indeed, with high expected house price increases and low interest rates, homeownership - when measured by the user cost of housing capital - has become particularly affordable.

It is pertinent to ask if this incipient and potentially unstable housing market boom is what the Australian Government means by 'building back better'? Home-ownership stimulus packages implemented by both the Commonwealth and state/territory governments have undoubtedly boosted construction sector employment. Roughly 10% subsidies to owner purchasers have contributed to a 10% rise in prices paid (including by non-recipients of subsidy).

In making these observations, we are voicing no anti-ownership sentiment. But policies inducing rising house prices seem an odd long run strategy for reversing falling ownership rates and achieving stable and productive growth. These wider economic consequences (see below) are still to be addressed but already these inflationary housing system outcomes may be edging monetary authorities towards raising interest rates that will damage wider recovery efforts in the economy. For instance, the Bank of Canada (in its Monetary Report of April 2021¹⁴) indicated an intention to taper its quantitative easing program and, in contrast

14 Bank of Canada (2021, April). Monetary Report. Ottawa.

to earlier reflections, it now envisages the possibility of raising rates in 2022. When will the RBA follow?

In these circumstances, there is an urgent need for a coherent system-wide strategy for shaping Australian housing markets where monetary policy, prudential regulation and housing infrastructure investment strategies address long run policy weaknesses and avoid compromising wider 'building back better' aspirations. In housing, governments really need to drop the 'BBB' metaphor and grasp the reality of housing outcomes that support economic change for the long term. It is a sign of the weakness of policy thinking that public and political debate about rising house prices is primarily about how large and sustained they will be, rather than how they will shape long-term adverse economic outcomes.

1.5 Changing Perspectives

Critics might respond that this report is whistling against the wind. However, winds of change are already evident in emerging post-pandemic economic policy reflections. These involve both recognition of changing political economies and different understandings and roles within key economic institutions of government, including central banks. The Commonwealth Government is committed to reviving homeownership growth, but it is clear from decades of experience that, in the longer term, bursts of first-homebuyer grant injection achieve precisely the opposite. They also impose collateral damage on most other housing consumers, as well as on long-run economic performance.

In Australia, just as in comparator countries, both governments and opposition parties remain stuck in a view of what drives ownership growth, and how to promote it. They take, in the main, a narrow and short-term view of the political gains from their promotion policies and seem to fail to recognise the problems created and the potential new political economies consolidating around these difficulties. For example, there will soon be significant parts of Australian metropolitan areas that will have a majority of renter voters. Indeed, there are

state government electoral constituencies where this is already true. There are substantial shares of potential owners rationed out, with well under half of under 35s having achieved homeownership, and growing groups of older households in difficulty within the sector. Has politics got a real grip on the patterns emerging in Australian housing systems? And, if politicians finally grasp the elephant, will policy bureaucracies change their approach as a convincing new synthesis emerges?

The power of the Washington Consensus in economic policy-making has greatly diminished, not least in Washington, over the last decade. Looking across Australia and comparator countries, the forward fiscal and monetary policy contexts for economies, and how they are being discussed by the IMF and the OECD, are markedly changed from 2019 – not only due to the COVID-19 pandemic but through the accumulation of dysfunctional economic, social and environmental outcomes.

These are changing times in the ways that Central banks and some national/Federal Treasuries/Finance Ministries are considering not only wider macro-economic goals (including unemployment, income inequality, social inclusion and environmental sustainability), in addition to controlling inflation. They are also broadening their conceptual frameworks and range of policy tools, especially monetary policy. There is a changing emphasis in goals and a retuning of how to manage market-led economies. Recent actions, including at the RBA, stand in sharp contrast to the conventional policy wisdoms that have prevailed through the four decades prior to 2019. COVID-19 may, thus, prove to have been a catalyst for policy paradigm change that failed to emerge after the Global Financial Crisis of 2008. The broad evidence presented below makes the case that in the top level rethinking of how to manage the economy, and deal with the existential crises of sustainable development, and reduce inequalities there must be a new view on housing in the economy.

So, what is the evidence base for a change in housing-economy policy understandings?

2. Evidence and Experts

The remainder of this paper brings together a review of key literature on housing effects on the economy as conducted by Maclennan, Long and Leishman¹⁵. Manuscript structure was informed by a heuristic model of recursive housing-economy interactions as set out below¹⁶. It builds on conventional economic perspectives that emphasise how economic factors drive the housing system, producing multiple outcomes that include economic feedback effects transcending conventional income and employment and related multiplier effects. Also highlighted in the review are additional feedback effects of housing prices and rents on wealth, residual incomes, economic and financial stability and, importantly, productivity. These feedback effects are often unrecognised or missing links in the design of housing policies.

15 The research methods used were straightforward. Members of the team had already been involved in different systematic reviews (Sutton et.al, 2019) of housing wealth and its consequences (Soaita, Gibb and Maclennan) and on and integration of previous reviews on housing and productivity (Maclennan, 2008; Maclennan et al, 2018; Maclennan et al 2021). These earlier reviews were updated by seeking evidence on recursive effects through instability, inequality and productivity, and adding contemporary references in relation to Australia. Studies reviewed included materials from the 'gray' literature of government and central reviews, as well as reports from financial institutions and others with a 'vested interest' in particular outcomes. Academic references were searched from books and journals in the field of housing and urban studies, planning, management, finance, real estate and economics.

16 When framing relationships between housing and the economy our research concluded that it is essential to see 'housing' as both a set of activities, including planning, financing, building and selling homes, and as a complex set of outcomes including dwelling sizes and styles, their connectivity and location, neighbourhood setting as well as costs and price. Housing is spatially fixed capital investment and has to be seen as essential economic as well as social infrastructure. Too often research and policy thinking stops by assessing the ways on which population and economics growth drives housing demand and with supply responses shapes outcomes such as prices, new supply, location and tenure choices as well as affordability and homelessness challenges. These processes are important but in this review the additional emphasis is on how these housing outcomes then, recursively, impacts subsequent key economic processes and outcomes.

2.1 Expert Views

The literature review was supplemented by our original fieldwork which probed the views of Australian experts on current housing-economy interactions. Cross-referring our literature review and housing system expert fieldwork also provides a check on the extent to which expert views were grounded in published evidence. For at any Friday dinner party for six in Surry Hills at least nine different views on the Sydney housing market may be gleaned. Our fieldwork here involved an online survey of 87 of Australia's leading economists and other government, industry and academic stakeholders with specialist knowledge of housing markets and housing provision (October 2020). More extensive insights were revealed through follow-up interviews with 20 survey respondents (November/December 2020). Fieldwork methodology is more fully detailed in the two freestanding reports on these linked studies published separately as part of the current series¹⁷.

There were some notable differences between the survey responses of economists (47) and others (40), and within the economists there were different shades of opinion, particularly on certain topics – particularly the housing market influence of land-use planning. These variations are explored in the full research reports of the survey and the follow-up in depth interviews (see footnote). Equally, however, the survey report highlights many perspectives on housing: economy connections where there was a strong consensus among participating experts – economists and non-economists alike. These included:

- The recognition that central banks are latterly paying increased attention to issues such as sustainability and inclusion, supplementing their inflation targeting roles

17 'Australian experts views of housing and the economy: Abstract dreamings or real directions?'; 'Housing and the Economy: Interrogating Australian experts' views'.

- A generally critical view of the efficacy of Australian tax policies in relation to the housing sector
- A belief that the recent pattern of housing system outcomes has exacerbated inequalities of both income and wealth
- An understanding that housing market outcomes compromise economic and financial stability
- A view that housing outcomes have a negative effect on labour productivity in Australia, particularly distorting labour markets
- A recognition that housing supply responses may be restrained by land-use planning restrictions, notwithstanding that the development of zoned land is also influenced by other housing supply chain constraints including in relation to construction labour shortages, materials shortages and an undersupply of necessary infrastructure
- A strong view that the Commonwealth Government should have included a significant social housing investment program as part of its effort to stimulate national economic recovery

These unambiguous results highlight that, as these issues were being viewed in late 2020, a strong majority of Australian economists and other housing experts were deeply concerned by the Commonwealth Government's unwillingness to address housing system impacts on the economy and to more actively and effectively invest in and manage overall housing market outcomes. For example:

- By a margin of almost four to one (67% versus 17%), expert respondents agreed that 'the absence of a coherent housing market strategy for Australia now constitutes a significant barrier to structural adjustment in the economy and to an effective post-pandemic recovery'.

Their observation on the need to expand investment in affordable rental housing (a phrase used here as an umbrella term including social housing) is of immediate importance:

- By a margin of eight to one, respondents disagreed with the proposition that omission of a social housing stimulus program in the 2020 budget was well-judged. Moreover, 57% (51% of economists) disagreed strongly

However, of much wider, and longer-term, significance for Australian housing and economic policies are the expressed beliefs of the majority that current Australian housing policy approaches (including associated tax settings) increase risks of economic and financial instability, reinforce inequalities in income and wealth and constitute a major drag on productivity growth in the Australian economy. For example:

- Nearly three quarters of participating experts (73%) believed that 'high mortgage debts and burdens (reflecting high house prices) raise instability risks for the economy as a whole'.
- By a margin of five to one, economists and other experts saw status quo economic policies as having exacerbated income and wealth inequality; yet by a margin of two to one, they doubted that countering inequality is genuinely a current official policy priority.
- 85% of respondents (79% of economists) agreed with the proposition that 'policymakers should pay greater attention to the economic productivity effects of housing market outcomes, such as costs, tenure, quality and proximity to work'.

There is a worrying gap in Australia, as COVID-recovery becomes feasible, between 'expert opinion' and apparent official thinking on how best to think and act for housing in the economy. And it is 'expert' opinion that is backed by the published (and mainly peer reviewed) evidence reviewed in this report.

2.2 Findings on Feedbacks: Overall

The literature review affirmed our working hypothesis that housing outcomes today impact tomorrow the major goals of economic and financial stability, income and wealth equality and future growth and productivity. Stability and inequality are additionally recognised as limits on productivity and the research confirms that housing outcomes have significant feedback effects on the stability, equality and productivity goals of modern economies.

As reported below, the more detailed conclusions from the literature review strongly support the contention that, in addition to merit good cases for housing policy investments, there are now compelling reasons to take the economic consequences of housing outcomes more seriously. To a much greater extent than in recent decades, these outcomes need to be factored into economic, fiscal, monetary and financial policy. In this there is a need to recognise that at both national and state/territory levels the crucial influence of housing outcomes on productivity and competitiveness has been traditionally unrecognised or ignored. To date the key 'thought centres' for shaping Australian economic policy have not engaged with such arguments and there is little appreciation that a coherent housing policy could generate both fairer outcomes and faster productivity growth.

Our review confirmed the introductory proposition that macroeconomic policy in the OECD is increasingly concerned with system outcomes beyond the traditional goals of output, employment and inflation targeting¹⁸. The goals addressed in macroeconomic policy actions are now changing and diversifying in many central banks, finance departments and treasuries. In some countries institutions, experts and policymakers have been loath to depart from the technical and value judgements embedded in the policy paradigms prevailing since the 1970s.

¹⁸ Lonergan, E and Blyth, M (2020) *Angrynomics*. Agenda Press. Newcastle-upon-Tyne:

Carney, M (2021) *Values, Building A Better World for All*. Penguin/Random House.

Other authoritative experts stress the need for change as times, and economic systems, have altered¹⁹. A key 'technical change' required in policymaking, at national and sub-national levels, is to address the missing economic understandings of housing system effects in policy making. Australia would appear to lag behind the UK, Canada and New Zealand in addressing such gaps in housing and economic policy thinking.

2.3 Framing the Evidence

Economies are complex, partly understood systems. Different 'schools' of thought regarding how they might be conceptualised exist and compete. At the macroeconomic scale, 'monetarist' emphases in macroeconomic policy gained great currency in combatting inflation in the 1970s and 80s and notions of tight control of the money supply, reliance on deregulated and competitive markets and aversion to high public debt and taxation rates were central elements in the so-called Washington Consensus that displaced older Keynesian ideas in the thinking of economics ministries and central banks. Keynesians paid less attention to controlling monetary aggregates and emphasised the importance of fiscal and budgetary policies in dealing with demand deficiencies in the economy to maintain near full employment and stimulate growth.

Keynes famously said, on commenting on giving economic advice, 'when circumstances change, I change my mind'. In reality, despite sharply different theoretical rhetoric, managers of macro policies have drawn on both schools of thought as growth and stability challenges change. Keynesian economics are always more attractive at the onset of, and in the wake of,

¹⁹ Economist (2020) The COVID-19 pandemic is forcing a rethink in macroeconomics. <https://www.economist.com/briefing/2020/07/25/the-covid-19-pandemic-is-forcing-a-rethink-in-macroeconomics>

IMF. (2021) *World Economic Outlook: Managing Divergent Recoveries*. Washington, DC, April.

Furman, J. and Summers, L. (2020) A reconsideration of fiscal policy in the era of low interest rates. Unpublished manuscript, Harvard University and Peterson Institute for International Economics.

major economic downturns. The monetarist perspectives of Milton Friedman tend to be found more appealing when inflation and boom times arrive. Now, in building back better from COVID-19, there is a major moment for more Keynesian perspectives, at least as inflation is quieted. As the Economist highlighted in mid-2020, macro-economic and monetary policymakers are working towards different syntheses relevant to our time. We want a coherent framing of the housing sector within models and policy making.

Within these macro perspectives, it is generally recognised by housing researchers that residential property markets form a complex system and Figure 4 provides a simplified outline. Demand and needs are driven by factors in the Aggregate Economy such as incomes, employment and interest rates²⁰. Supply responses are also complex and involve, in the short term, turnover as well as new supply flows. These two 'sides' of the market are indicated in the stylised heuristic model in Figure 3. In this analysis we retain the complex nature of housing that involves size, quality, location and asset roles as there are significant economy feedbacks from each of these different aspects of housing choices. Home is, for many, the centre of their economic as well as their social lives.

The interaction of complex demands and relatively inelastic supplies means that the key outcomes of the interaction of housing demand and supply at any point of time will spark a series of market adjustments when supply and demand do not reconcile at prevailing market prices. The first key adjustment, or feedback channel, is the focus of traditional analyses of feedback effects from the housing market to the wider economy, has been price change induced (output) supply increases that raise investment in the housing sector. These are labelled as Route 1 in Figure 4 and they reflect how rising house prices induce increased employment and incomes in

the housing sector and wider multiplier effects in the economy - at least when the system is not near full employment. Increased market activity of course generates increased turnover and sales rates for existing stock, and more recent work has recognised that this also has demand effects in the aggregate wider economy - for removalists, home improvers, and new white and household goods, for instance.

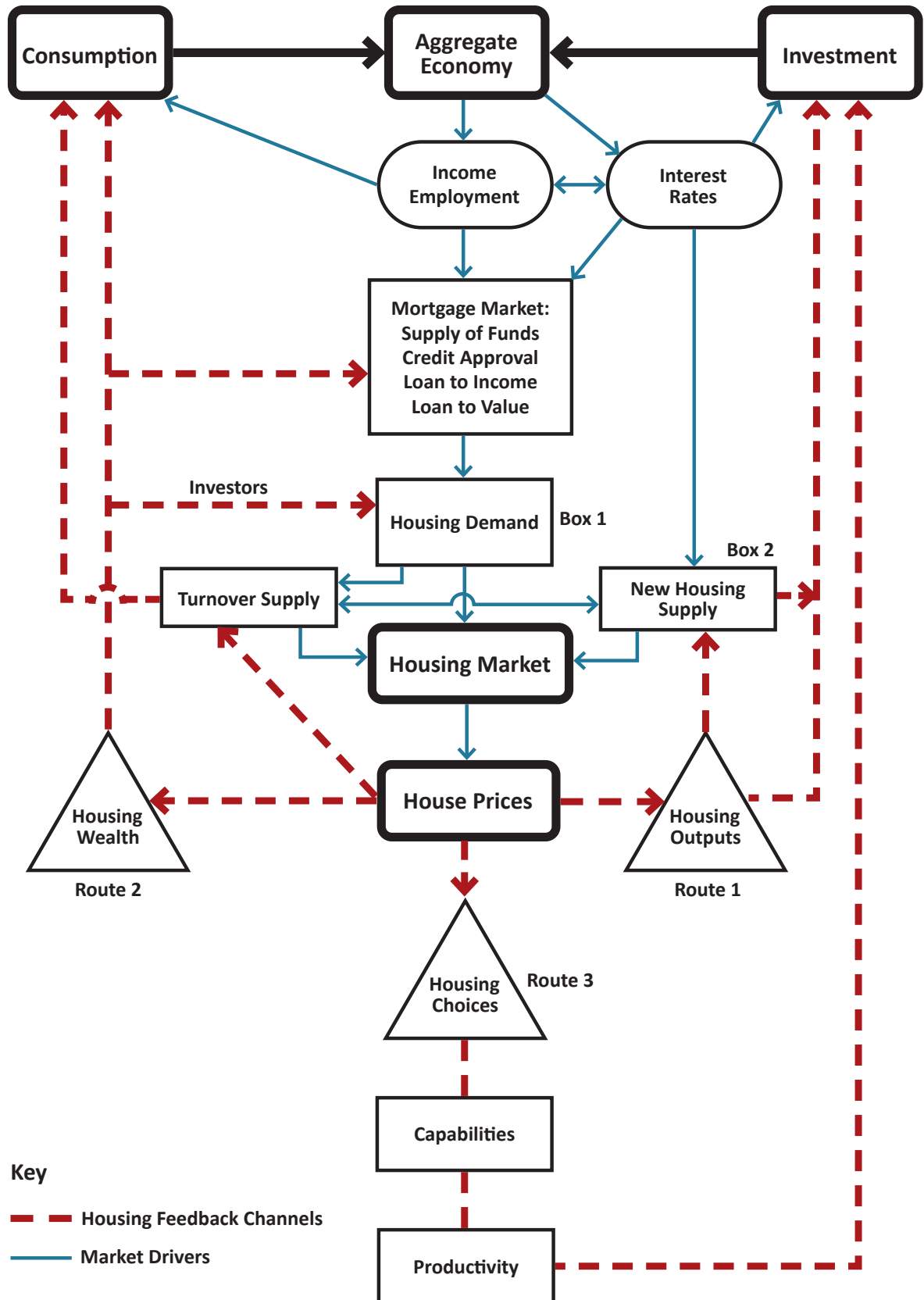
The market is also referred to as the 'price' system. Supply/demand imbalances induce price changes (increases with excess demand) that signal consumers to trim back demands and producers to raise supply until supply and demand reach a balance at some now 'equilibrium' price and output level. Price changes are then a key Feedback Link via Route 1 (see Figure 4).

Casual commentators tell us the housing market is just Economics 101 (Oh, if only!). Serious mainstream microeconomists in the neoclassical tradition of perfect markets with perfectly rational and completely informed buyers, sellers and producers construct reductionist mathematical models of quite complex housing market outcomes. They are interesting and important if one puts interest in mathematical modelling of the economy as a research priority. If the priority is to develop applied economics frameworks that do not assume away key operational features of markets then a different, more empirical approach may be required.

Our approach is clear. Equilibrium is not a feature of Australian housing markets in the twenty-first century. Prices often do not stabilise markets and price changes have complex sets of connections back to the wider economy. There are links from price changes that do not flow immediately back into market equilibration. Price rises can induce demand increases in the next market iteration, if households do not wish to be left behind by rising prices (Feedback Link 5) or sustained price increases in a market may attract new external investor demands (Feedback Link 6). Rising housing prices and rents may reduce incomes after housing costs and diminish aggregate savings or consumption (Feedback Link 7). Rising prices ahead of incomes may lead to increased loan to income

20 The Figure simplifies the system and key demographic influences that drive demands and needs, such as ageing, migration and household formation, as well as important supply chain consideration including construction costs, development finance, skilled labour supply, materials prices, planning and infrastructure systems, are excluded.

Figure 4: Stylised housing system connections and feedbacks



ratios and individual and national mortgage debt to income ratios and risks (Feedback Link 8). And, of course, rising house prices increase the wealth of existing owners with links back to consumption and investment in the economy. These are complex adjustments that operate through price/wealth effects, indicated as Route 2 in the Figure 4.

There is a third, key feedback route from housing outcomes to the economy. Because houses are a complex commodity, when house prices rise, households may wish to adapt by altering different elements of their chosen housing bundle. Higher prices and rents may change tenure choices, and that has an important feedback on patterns of household wealth and savings. Higher prices may induce poorer households to smaller and lower quality dwellings. That may, in turn, affect household health and learning capabilities that damage the formation and utilisation of human capital. High central city housing costs may induce households to move away from concentrations of employment, weakening the agglomeration gains of more effective matching in thick labour markets and have impacts on the productivity of labour and capital. There may be more and different feedbacks in different housing market settings and as carbon effects become increasingly priced into the search for zero carbon economic activities, housing quality and location may be significant in shaping new (redefined) productivity locations. The feedback of housing outcomes on inequality, instability and productivity needs to be a central concern in housing and economic policy making. But this is rarely the case.

It is these dis-equilibrating feedback effects from high and rising housing costs and prices to the economy that suggest neither Economics 101 nor complex general spatial equilibrium models are going to help much in framing key recursive connections between housing and the economy. The sections below emphasise what housing economic policy needs to know.

2.4 Findings on Route 1 Feedbacks: Sector Scale, Employment and Multipliers

2.4.1 Sector Scale

Traditional (Keynesian) economic perspectives on the importance of housing in the economy assess the extent to which spending on ‘housing/property’ adds to aggregate demand, with much interest in consequent multiplier effects. The overall weight of housing in the economy can be estimated in different ways, but all the measures confirm the importance of the sector and its growing significance in this millennium. The most expansively defined property sector-economy estimate for the Australian economy saw the Property Council argue that the property sector constituted the largest, and rising, share of the Australian economy and employment, contributing close to a quarter of GDP in 2006 and rising to 30% by 2016²¹. Broadly, two-thirds of that activity was estimated as attributable to the residential sector. A definition focusing only on direct property sector contributions indicated a share of around 13% of GDP.

A more recent study, for 2020, suggested that the share of GVA contributed by construction alone was closer to 7.6% and Renting, Hiring and Real estate added another 3.2%. NHFIC (2020) updated estimates of residential construction scale (strictly defined) and reported that it was one of the largest industrial sectors in the Australian economy producing 5% of GDP and generating 134,000 direct jobs for 2019-20. It is unfortunate that, given the scale of cross-sector effects pointed-up by the Property Council’s special study in 2017, government does not publish a recurrent run of more meaningful housing sector data that allows fast access to assessing the weight of housing-economy connections – not just nationally, but regions, metropolitan areas and jurisdictions. This should be basic economic policy information given the ‘weighty’ scale of the sector (even with minimalist definitions).

21 Property Council of Australia (2017) Economic Significance of the Property Industry to the Australian Economy; Sydney: APC <https://tinyurl.com/uf3tytdn>

The housing sector's scale and its direct impacts on the labour market have also generated a traditional policy concern with the jobs induced by housing spending. This connection is best summarised in 'multiplier' estimates. A recent NHFIC report concluded that the residential construction industry has Australia's second largest (of all 114 industries that make up the economy) sectoral economic multiplier, estimated at 2.9. That is, \$1 million of residential building construction output supports around \$2.9 million of industry output and consumption across the broader economy thus supporting nine additional jobs across the economy²². Multiplier effects are less useful policy tools where initial tax revenues raised to fund investment displace other economic activity, or where investment in housing largely creates inflation rather than new output. But the residential construction multiplier is a significant economic factor when the economy faces aggregate demand deficiencies. It is also important to recognise that multiplier effects in stimulus investment packages may depend on regional and sectoral patterns of investment. There is little sign that recent stimulus spending by the Commonwealth Government has paid much attention to such issues.

2.4.2 Turnover Feedbacks

Feedbacks from housing activity to the economy, in the short term, also arise from turnover of the second-hand housing stock and the Reserve Bank has also highlighted how Australian housing turnover has fluctuated since the 1990s²³. Housing turnover, and the associated non-housing spending appear to coincide with, and reinforce, broader cycles in growth rates (housing turnover effects on household spending are pro-cyclical and reinforce upswings and downswings).

22 NHFIC (2020) Building jobs: How residential construction drives the economy <https://www.nhfic.gov.au/media/1298/building-jobs-how-residential-construction-drives-the-economy-final4.pdf>

23 Debelle (2019) 'Housing and the Economy' Address at the CFA Societies Australia Investment Conference Sydney – 17 October; RBA <https://www.rba.gov.au/speeches/2019/pdf/sp-dg-2019-10-17.pdf>

2.5 Feedback Findings: Housing and Economic Cycles and Instability

2.5.1 Housing market cycles

Housing policy advocates often limit their economic cases for housing to multiplier effects to forestall recession. These are not to be neglected in policymaking. But longer-term feedback impacts on cycles and instabilities, growth and productivity are likely to have prolonged and more fundamental effects on the Australian economy.

Official statistics demonstrate that both the overall property and housing sectors have grown faster than GDP over the last decade (to 2020). Since the start of the 1970s new housing starts in Australia have 10 completed well-defined cycles, and the system is presently in an 11th. The peak to trough duration has typically been 4-5 years unless disrupted by significant shocks, such as the East Asian Financial crisis, the GFC and now COVID-19. Despite the rapid growth in Australia's population the peak quarterly output of the sector rose relatively slowly (per annum 38-40,000 units in the 1980s, 45-47,000 in the 1990s, around 60,000 units by 2010, and that total was reached again in 2018, and by quarter 3 2020 output had fallen to just over 40,000 units). Key literature findings from a range of studies include that residential investment leads the business cycle (though the leading role of residential investment over the business cycle in Australia is less pronounced, and more variable, than for the U.S. and Canada (when housing starts are used to proxy investment, housing construction leads GDP)), but when the housing impetus is measured as residential investment then it is coincidental with cycles and as GDP starts to fall completions fall too.

2.5.2 House Price Changes as Feedback Link: More Vicious Cycles?

House price and rent changes are key measures of housing market activity and signals that stimulate supply responses (whether, or not, in equilibrating fashion) and, with supply

lags involved, may shape cyclical patterns in removing supply-demand imbalances. Research evidence across the OECD suggests that house prices have, since the 1960s, become highly volatile and closely correlated with the business cycle. Rents are more stable than house prices, with a lower correlation with the business cycle (and Australian rents have lagged house price increases since 2015 and there appears to be further divergence into 2021).

Rising real house prices continue to be officially celebrated as a sign of growing economic success and national wealth, and by homeowners as a measure of their own success and (incorrectly) efforts. At the same time, they may reflect imbalanced monetary and infrastructure policies and housing and land market failures, particularly in metropolitan areas. Price changes that shift housing wealth, as indicated in Figure 4 above have potentially significant transmission links back to the economy that are not captured in conventional/housing starts cyclical models, and are key to understanding contemporary economic, and financial, instabilities.

It is important to understand the economics of why Australia has built, and bought, its way into this economically unstable scenario and to comprehend why attendant volatility risks are little discussed in housing policy formation (though assume greater consideration in monetary policies). Prior to the 1970s real house prices remained flat and, intermittently, marginally rose and fell, in almost all the major OECD economies, including Australia. In earlier decades policy choices to grow homeownership were progressed in eras of stable house prices. Homeownership encouraged households to save and accumulate assets through regular mortgage payments. That process provided lifelong housing for owners but also redistributed their consumption possibilities across their life cycle, thus helping maintain living standards in retirement. From 1907 onwards in Australia (when housing rather than pension plans became the vehicle for old age saving), in the USA in the New Deal 1935 Housing Act, and in the UK after WW II, home-ownership

was seen as a vehicle for saving based on effort and not as a sector for passive or active asset speculation unrelated either to housing consumption requirements or effort.

Homeownership and asset accumulation through work, effort and savings began to disappear in the 1970s, with effort and saving displaced to the deposit formation stage, and then further displaced by flows of family wealth to form deposits. Since then, only the decade 1988-1998 showed limited real house price growth. In this millennium inflation-adjusted price growth has been faster and the evolution of the price pattern has displayed more frequent burst and dips in inflation rates.

Much evidence reviewed suggests that when homeowners move from being essentially savers to passive speculators (taking the capital gains that come their way) they can then readily shift to become active speculators as households and investors, sensitive to housing price shifts and driven by their asset price expectations. Such active speculators include not only more affluent households who buy multiple properties to hold and rent out but also older households (empty nesters and single survivors) who continue to live in large family homes that offer a flow of housing consumption services well beyond their demand for such services, but that meet their asset demands better than available alternatives. Housing price booms, busts and bubbles, and all their associated instabilities (Schiller) have become part of the housing-to-economy transmission processes. House price increases through the speculative demand channel may stimulate more and not less demand for housing, thus exacerbating upswings.

The evidence for Australia, and particularly the major metropolitan areas, has been that significant speculative demands for housing have characterised markets out of equilibrium over much of the last two decades²⁴. The significance of domestic buy to let/investor landlords, though diminished as a share of all home purchasers

24 MacLennan. D and Miao. J (2019) Housing in the Metropolitan Economy, pp 119–133, in MacLennan. D., Pawson. H., Gibb. K. and Hulchanski. D. Shaping Futures. University of Glasgow (mimeo).

since 2017, is well established in Australia²⁵. Strong, positive price signals also become beacons for investment to internationally mobile 'housing' capital. The significance of overseas (especially Chinese) buyers in Australian housing markets in this millennium, until the reforms of the Turnbull government in 2017, is well established²⁶. However, Australia's major housing speculators are not overseas investors, nor domestic 'investors' (though both impart significant procyclical reinforcement to house price booms), but the majority of Australian homeowners. Moreover, the gainer-loser pattern in the speculative process is well defined and constitutes shifts in net wealth from younger to older generations that is substantial, continuing, and not – as some economists believe – economically neutral.²⁷ Today's battlers are really battling yesterday's battlers.

2.5.3 Pervasive House Price Inflation and Missing Policy Measures

Given the effort devoted to suppressing wage inflation after the mid-1970's, it is many ways remarkable, given the scale of the sector and the persistence of house price rises, that Australian governments have been reluctant to address the causes and consequences of house price inflation. In part it is because they have carried into the more febrile housing markets of the last thirty years the policy mindset of earlier decades: homeownership would grow steadily with incomes, it encouraged steady saving, growing the sector spread wealth and it was a 'fiscally' low-cost housing solution for all times and ages. And of course, the assumed realpolitik that owners constituted the majority of voters.

None of the above assumptions remain certain nor well-founded. Speculative gains far outweigh the accumulation of steady savings; housing wealth growth no longer reduces

aggregate wealth inequality (see below); the non-taxation of housing capital gains is a substantial tax-expenditure to the Treasury; intra-family wealth transfer is becoming as important as income in shaping who can enter the sector and at what age; growing proportions of the over-60s continue to repay mortgage debt. And, of course, the stability, wealth and productivity effects of house price increases reported below have not constituted positive feedback outcomes for the overall economy. And are not high prices and housing costs at the core of Australia's housing difficulties?

One can readily recognise the benefits of homeownership as historically understood and yet argue for more policy concern to stabilise house prices in the longer term. Has housing policy effectively transformed Australia from an effort and entrepreneurship economy to an increasingly rentier-based economy? With housing wealth the dominant asset of more than half the population, and the bulk of that wealth unearned capital gains, the question is not just relevant but important. Do the Australian Federal Treasury and the RBA have a well-researched view not only on what drives house prices, but also the long run implications of house price increases for Australia. If not, why not? And if they do, the housing sector deserves to know what it is.

2.5.4 Rethinking Connections and Interactions

Over the last decade central banks, the OECD and the IMF, have become much more concerned about housing prices, and especially their implications for economic and financial instability. The literature review identified a number of significantly changed 'feedback' channels:

- a) Changes in financial sector (de-)regulation and the development of wholesale capital market funding of homeowner mortgages or new forms of equity withdrawal have removed or relaxed some endogenous limits to housing market growth and instabilities. Albeit interrupted by COVID-19, the globalisation of flows of human capital, ideas and housing capital in deregulated

25 Pawson, H. & Martin, C. (2020) Rental property investment in disadvantaged areas: the means and motivations of Western Sydney's new landlords; *Housing Studies* – online first, DOI: 10.1080/02673037.2019.1709806

26 RBA (2016) Financial Stability Review, October: and, Foreign Investment Review Board (2019) <https://firb.gov.au/sites/firb.gov.au/files/2020-05/FIRB-AR-2018-19.pdf>

27 Buiter (2010) Housing wealth isn't wealth; *Economics-the Open Access Open-Assessment E-Journal*, 4.

economies has substantively changed the operational dynamics of housing markets (particularly major metropolitan areas) since the 1990s. Mortgage market ‘circuits’ have become more closely integrated into domestic capital markets and, in turn, national capital markets have become more globally integrated. These integrations extend beyond capital market flows. The IMF has identified growing synchronicity of house price trends in ‘global cities’, including Sydney and Melbourne, in this millennium and with these major centres partially unlinking their market trends from the national systems within which they are set²⁸. This raises major questions about the appropriateness of ‘national’ policies, and especially macro-prudential policies, for coping with metropolitan house price booms.

- b) Transmission channels for house price effects have changed. Rising real house prices make economies less stable, as speculative investment demands for housing are somewhat more volatile than households’ demands for space and accessibility.
- c) Rising stocks of housing wealth impact aggregate demand and consumption in pro-cyclical ways. The literature review found strong evidence that rising housing prices that create rising stocks of housing wealth then unleash effects on household consumption and investment behaviour. The evidence suggests that they will reinforce upswing ‘feel good’ factors and spending, but, equally, will prolong downswing recessionary ‘hangovers’ when lost and negative equity dampens housing demand. This ‘feel good’ factor and its electoral dividend is, of course, seductive to politicians. If, further, financial sector innovation and reforms allow households to ‘withdraw’ housing equity, as happened after the 1990s, the potential for rising house prices to fuel increased household

expenditures and exaggerate housing boom effects arises. Reviewed research literature demonstrates how housing price/wealth outcomes are both driven by, and then recursively drive, the economy with then a tight linkage of housing prices and the business cycle.

- d) Prices rising ahead of incomes create more marginal buyers and more households with rising mortgage stress. Research across many countries over the last decade demonstrates strong statistical links between the different phases of business and financial (credit, housing, and equity) cycles: recessions associated with financial disruptions, notably house and equity price busts, tend to be longer and deeper than other recessions. Conversely, while recoveries following asset price busts tend to be weaker, recoveries associated with rapid growth in credit and house prices are often stronger. This emphasises the significant role of house price growth and asset price busts prior to recessions in determining both the duration and the depth of recessions. The importance of house prices and credit in triggering financial crises is also well established in many (though not all) instances. Econometric analyses of bubble-like behaviour in housing and credit markets suggest that they have positive and statistically significant effects on the probability of significant financial sector instability. The probability of a financial/economic crisis increases markedly when bubble-like behaviour in house prices coincides with high household debt leverage.

There is clear evidence from Australia, and similar OECD economies, that high and rising house prices, and their wealth consequences, have had substantial effects in both exaggerating ‘normal business cycles and in triggering and reinforcing wider systemic financial and economic crises. Policymaking has been, arguably, slow to react to those modern macro-economic realities.

28 IMF (2018) Global Financial Stability Report, April. Washington.

2.5.5 New Concerns and Prudential Financial Regulation

Published literature confirms that destabilising house price/housing wealth effects have grown in magnitude over time, they are procyclical and they increase instabilities and the challenges for fiscal and monetary policy. Our study failed to unearth any published estimate of the extent to which increased interest rates, induced by seeking to control rising house prices, have damaged investment in business and human capital. However, in this millennium international agencies such as the OECD, BIS and the IMF, along with national central/reserve banks, have paid increasing attention to housing prices and business cycles, as much to understand systemic risks of major crises, as to nuance more recurrent anti-cyclical policy.

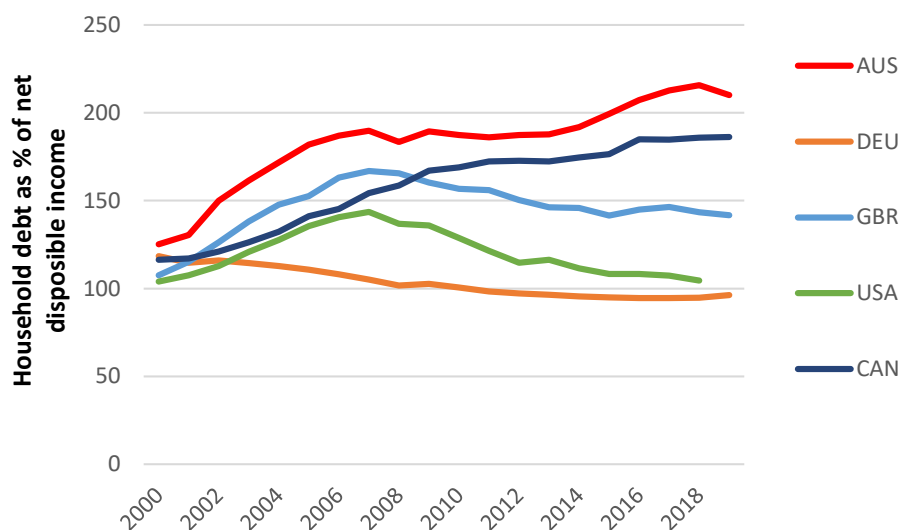
Work at BIS, and the IMF, recognises that housing market downturns play key roles in around one recession out of two. In consequence, they argue that housing systems need to have a resilience to potential external as well as cyclical shocks and that requires ‘prudential regulation’ measures. Such measures have created some consequences that have been unanticipated or have run counter to other ‘housing policies’ supported by fiscal and expenditure programs of other parts of governments (most notably first-

home owner grants). House price changes are much influenced by the operation of national, and global, capital markets, the regulation and structure of national housing credit institutions, and the monetary policies that impact them. Some experts take a rather different long run view from the ‘it’s a supply side problem’ commentators (including the RBA)²⁹. They conclude that, as in other countries, loose monetary conditions in Australia have shaped mortgage and house price booms and the consequent macro-financial vulnerabilities, reflected in high household debt and low housing affordability, that have become a major concern after housing booms.

In the half century since 1970, household mortgage borrowing in Australia has come to dominate bank credit, absorbing two-thirds of increased credit in that period. A growing proportion of such loans have been deemed risky because of high loan to value and loan to income ratios. The accumulation of housing debt, with its associated macroeconomic and financial sector risks, across the OECD is well documented. On this score, Australia now appears to have particularly high measures of household debt to GDP ratios, see Figure 5.

29 Jorda, O. et al (2016) The great mortgaging: housing finance, crises and business cycles; Economic Policy pp. 107–152

Figure 5: Household debt to GDP ratio – Australia and selected comparator countries



Source: OECD household debt statistics <https://data.oecd.org/hha/household-debt.htm>

Mortgage credit has been the fastest growing component of rising debt to GDP ratios in Australia and statistics suggest a potentially significant housing-mortgage market vulnerability to economic shocks. After stabilising at around 120% of income in the mid-2000s, the household mortgage debt ratio has since risen through 140% in 2018 to closer to 150% by 2020. Overall household debt has risen substantially relative to income from 70% in 1990 to close to 190% by 2020. However, since the GFC, these ratios have not risen for households at median income and at the twenty-fifth income percentile.

The poorer half of Australia has been less able to access increased credit over the last decade (as housing wealth has concentrated in upper income groups) and this may well reflect that they are increasingly rationed out of homeownership and access to cheap credit. This is a fundamentally important observation in relation to both inter- and intra-generational equity in Australia. Homeownership is no longer acting as the asset builder for younger, poorer households and – especially as it contracts in overall representation – no longer performing as a wealth spreader in Australia.

Similar concerns are relevant to the banking sector and the financial system. The Australian financial system is heavily weighted towards housing lending. The banking system is highly concentrated and since all of the banks have very similar balance sheet structures, a problem for one is likely to be a problem for all. Further, with mortgage debt accounting for 60% of all lending, Australia leads the international economies in the extent to which such debt is provided by the banking system. By international standards, Australian banks, and in consequence the financial system, are particularly exposed to any threats to repayment difficulties and credit quality in the stock of mortgages.

The RBA's latest Financial Stability Review (2020), in the early period of COVID-19 impact, established that through 2021 many households will find their finances under strain due to efforts to contain the virus. This is consistent with the

Bank's earlier analysis³⁰ that some households will be able to draw on significant financial buffers, including large mortgage prepayments, but the majority, and especially the most highly indebted households have only small buffers and so are more vulnerable to lost income. The 2020 FSR notes that, regardless of age, income or employment status, households with small buffers report experience of financial stress. Arrears and vacancies may rise when government assistance ends, and this may impact property price/mortgage stability for landlords in due course. Homeowners were reporting significantly increased payment stress through 2018 and recent industry data from Digital Finance Analytics (March 2021) indicate that up to a third of owners with a mortgage have been experiencing some level of mortgage stress. Similarly, although most 2020 mortgage deferrals had ended by that time, rising numbers of households were experiencing serious arrears problems (more than 90 days). DFA perceived a serious danger of default for 3-5% of mortgage holders at that time.

These observations suggest there is a substantial macroprudential management problem that has been allowed to evolve over the last two decades. The failure to contain housing prices has built bank-led mortgage provision that now has some difficult foundations to repair. The likely prospect of prolonged low interest rates to 2030 provides some comfort (as long as quantitative easing does not lead to stronger fears of rising inflation requiring rising bond yields). The RBA concluded that, by 2019, stress tests for likely ranges of income and interest rate changes suggested that banks were sufficiently well-capitalised to handle any foreseeable rise in loan delinquencies. That is, any substantial downturn in the housing market would have implications for the economy rather than the stability of the financial system.

There can be little doubt that short term fiscal and regulatory interventions after 2017 have reduced speculative pressures from the investor sector and improved the safety of the stock of

30 Lowe, P. (2017) Household debt, housing prices and resilience. *Economic Analysis and Policy*, 55, pp.124-131.

mortgages. But were these temporary measures, a short-term palliative, and have they contributed to a better designed financial system that will enhance housing stability? Did they need to be aligned to broader monetary policy measures, housing supply and infrastructure strategies to shape an integrated housing market strategy for the nation? The marked upward shift in house prices after mid-2019 raises some important questions in that regard but the system test is still to come. It is not how the sector has coped through the first year of COVID-19 (with such large-scale income supports and homeowner stimulus), but how it will progress from mid-2021 onwards after the removal of market supports.

RBA reliance on non-traditional QE policies will stimulate access to lower cost funds for housing by all investment sectors. Large asset (bond) purchases by central banks (quantitative easing) manipulate the bond market primarily, pushing

prices up and yields down. This drives credit towards the inter-bank market and increases the supply of capital and mortgages, thus pushing down the effective mortgage interest rate. However, even if QE raises the stock of money in the economy direct government action may still be required to lead housing investment stimulus for rental housing provision for poorer renters and indeed potential homeowners with little equity and modest incomes. Without such action an unbalanced housing market boom for those with higher incomes and existing (housing) assets may unfold, leaving weaker market sectors further behind and fashioning a split within the homeowner sector as well as between owning and renting. There appears to have been little thought given to ensuring how QE ultimately raises investment demands in the housing sector and this may become a critical issue in Australia in 2021-22.

Quantitative easing didn't have the real [economy] ... stimulus that they assumed, but it certainly did [inflate] asset prices ... And of course, the higher income earners have better access to those asset classes and so [QE] has increased inequality [Academic A4] – quotation from in-depth interviews report.

This lengthy discussion of feedback effects from housing outcomes on economic and financial stability in Australia illustrates and evidences some of the ways that rising house prices can potentially damage economic stability and how long-neglected policy action to recognise the elephant' has been. More active prudential financial regulation as deployed on occasions over the past decade has averted some difficulties, but almost invariably when other government policy settings, in fiscal, spending and monetary policies unleash or reinforce property price rises. To illustrate the paradox, it will be interesting to observe if APRA introduces, by mid-2021, tighter macroprudential regulations on first home buyer mortgages as house prices soar, stimulated by homebuyer grant programs, so that only the already rich will enjoy the benefits of official grant largesse.

2.6 Feedback Effects: Housing Wealth and the Economy

In the previous section it was noted that since the 1970s rising real rising housing wealth, largely driven by rising house prices, has become an important feedback from current housing market outcomes into consumption and had reinforced the amplitude and duration of economic cycles. Rising housing prices and rents have other important effects on the economy through household wealth and income channels.

2.6.1 Residual Incomes

Until the 1970s, housing costs rents and prices in Australia moved broadly in line with incomes and the cost of living, the pattern experienced in most other advanced economies. But over the last four decades more rapidly rising rents and prices, increasing faster than incomes, have

been more characteristic of Australian economic growth. The inherently inelastic demands for basic housing characteristics have meant that typically rents for lower income groups have often risen fastest. As a consequence, rent to income ratios for poorer renters have risen most which has resulted in reduced 'residual' incomes (i.e. that part of income left after housing costs have been deducted) for these households. At the same time, however, property price escalation

has bestowed the greatest unearned capital gains on those in the most expensive housing, especially in the metropolitan regions. These processes are in the inherent nature of the growth process and as a result have reinforced income inequalities. And the effect is increasing over time. *Quite evidently, housing policies are not achieving their redistributive aims and they are failing further as time passes.*

It's great for me in the [equities] business, but ... I think it's to the detriment of long-term growth and fairness in society [Consultant C1] – quotation from in-depth interviews report.

2.6.2 Housing Wealth Patterns

Until the 1970s the accumulation of household wealth in homeownership led to well defined patterns of net housing asset ownership, with households paying down mortgages earlier in their life-cycle and holding debt free housing assets by retirement ages. Typically, overall household wealth patterns saw rising net assets from 25-30 years onwards until 60-65 and retirement ages. In contrast to the present, typically after age 65 overall wealth fell, and was consumed as households aged further. Housing inheritances were much smaller than now and were received at earlier ages. Through that initial post-war period, equality measures for overall wealth across economies were positively correlated with higher shares of home-ownership. In Australia, for instance, the growth of homeownership from the Menzies era until the mid-1990s was widely regarded as a spreading of wealth and reduction of overall inequality wealth inequality.

The scales and roles of housing wealth in the economy have changed significantly since that time. Household net wealth in Australia has grown faster than household incomes. Growth rates in household assets have been even higher than for increased debt (and both have outstripped income growth), such that the value of household assets has grown from around six times household disposable annual income in

the early 1990s to around 11 times in 2019 (with Australia now in the top five wealthiest countries in the OECD).

Housing has been an important element of the growth in both assets and liabilities. Indeed, as for the OECD, where net asset holdings are twice as concentrated as incomes, household wealth distribution in Australia is now significantly unequal and markedly more unequal than incomes. Housing wealth shifts have played important roles in shifting overall patterns inequitably. By 2016 ownership of the household's main home comprised 40% of all wealth and a further 12% of wealth held in real estate comprised a significant total of investor/landlord wealth in housing³¹. The inequalities in housing wealth in Australia are sufficiently marked and growing that, as argued by the Grattan Institute, the key inequality issue in Australia is not income disparities (neither particularly high nor increasing) but housing cost and wealth inequalities (both high and rising)³².

31 ACOSS (2020) Inequality in Australia. ACOSS Sydney.

OECD (2019) Income, wealth and earnings Inequality in Australia. Sila. U and Dugain. V. Economics Department Working Papers No 1538 OECD Paris.

Ferraro. S (2019) Inequality is growing but it is also changing as Australia's super rich evolve. The Conversation. July 15th.

32 Coates, B. and Chivers, C (2019) Rising inequality in Australia isn't about incomes: it's almost all about housing; The Conversation, 19 Sept <https://theconversation.com/rising-inequality-in-australia-isnt-about-incomes-its-almost-all-about-housing-119872>

[Rising house prices are] essentially a [wealth] transfer from people who don't own houses to people who do [Academic A5] – quotation from in-depth interviews report.

Who gains? The people who gain are those multiple property owners [Consultant C6] – quotation from in-depth interviews report.

2.6.3 Reinforcing Inequalities, Reducing Social Mobilities.

As real house prices have increased ahead of incomes in Australia since the 1990s much has changed. Asset speculation in housing has driven homeowner gains much more than the traditional life cycle saving objectives. Consequently, the wealth-spreading effect of homeownership growth has diminished as homeownership rates have dropped, halving for the under-35s since 1995, while housing wealth has concentrated in the hands of the over 65s (70%). Increasingly, wealth transfers from parents/grandparents to first home buyers have become essential for many younger buyers so that home-ownership is now more strongly predicated on parental property wealth and the increasing importance of intergenerational transfer between generations at times of house purchase. These patterns imply a likely reduction in social mobility. Housing market outcomes make the aspirational struggles of Australia's battlers increasingly challenging, and little assisted by mainstream tax and monetary policies (that favour existing owners and households as investors).

In remaking housing policies, and shaping a fairer and potentially faster growth Australia, the now adverse distributional effects of housing capital gains lie at the heart of both the measured economic cases for change and the difficult political economy of change when two-thirds of the population are homeowners. By and large, metropolitan owners have gained more than regional populations. Owners have benefited more than renters and the margins between owning and renting have become a broadening terrain of household misery and stress: more younger households are queuing unhappily for longer, and at higher rents in landlord-owned properties, and more marginal owners are concerned about inability to maintain ownership and progress within it. This growing renter aspirants/owner precariat's share of the population, and particularly under 40s is just now emerging as a significant discontented block (possibly up to one in seven of all households) within the Australian housing system. In the process, the unequal distributions of winners and losers by city/region, owner/renter and young/old are reshaping social stratifications in Australia.

[I]n a fairly dynamic economy like Australia's where we have embraced micro economic reform a fair bit ... we've never been brave enough to touch housing markets. So, you know, the tax privileged nature of housing ... The whole question of access to home-ownership, as distinct from access to decent housing, we haven't gone there [Consultant C2] – quotation from in-depth interviews report.

The tax system wasn't a problem in the 1950s because we didn't have ... asset price inflation. Once [this] came into it the kind of tax system we had become a problem and we didn't change it [Academic A6] – quotation from in-depth interviews report.

2.6.4 Housing Wealth, Pensions and Old Age

Saving for old age via housing (and other assets) has been a key element in Australian retirement plans since the early 1900s and is the basis of current asset-based welfare arguments. It remains so, and homeownership and the acquisition of investment properties has become even more important in this millennium (with equity rich ‘investors’ purchasing properties for retirement incomes, to be paid mainly by younger households rationed out of owning). However, the resulting falling rates of homeownership among younger cohorts are likely to decrease the ability of those households to use housing equity to support consumption and care as they age. Recent policy measures during COVID have tried to rebalance asset ownership towards first home buyers but investor interest has re-emerged in the first half of 2021.

Moreover, many household relationships do not remain stable and the (equity) withdrawal of housing wealth to address financial shocks stemming from ‘uninsurable’ events such as

relationship breakdown is well established. However, taken together, the existing research suggests that while net housing wealth may provide a positive safety-net in the short-term in case of divorce/dissolution, it may have long lasting adverse effects on the housing wealth held by divorcees as well as on that of their children in the future.

A growing number of studies highlight how housing wealth can help households cushion adverse events, secure better housing outcomes for children and grandchildren and be associated with potentially better levels of mental and physical health into older age. Having housing wealth is beneficial to households but most of it arises from ‘passive’ speculation. However earned, housing wealth is increasingly unequally distributed in Australia and the well-intentioned role for building homeownership assets in spreading wealth has been overtaken by patterns of economic development and housing policy failure to become a key speculative asset and reinforcer of wealth inequality. And in doing so, it also contributes to reduced productivity.

It's going to be very hard to prosecute economic policy that continues to polarize people So a lot of the things that you need to improve productivity, you run into barriers if you have a polarizing inequitable society [Consultant C2] – quotation from in-depth interviews report.

2.7 Feedback Effects: Productivity: All? Or Nothing at All?

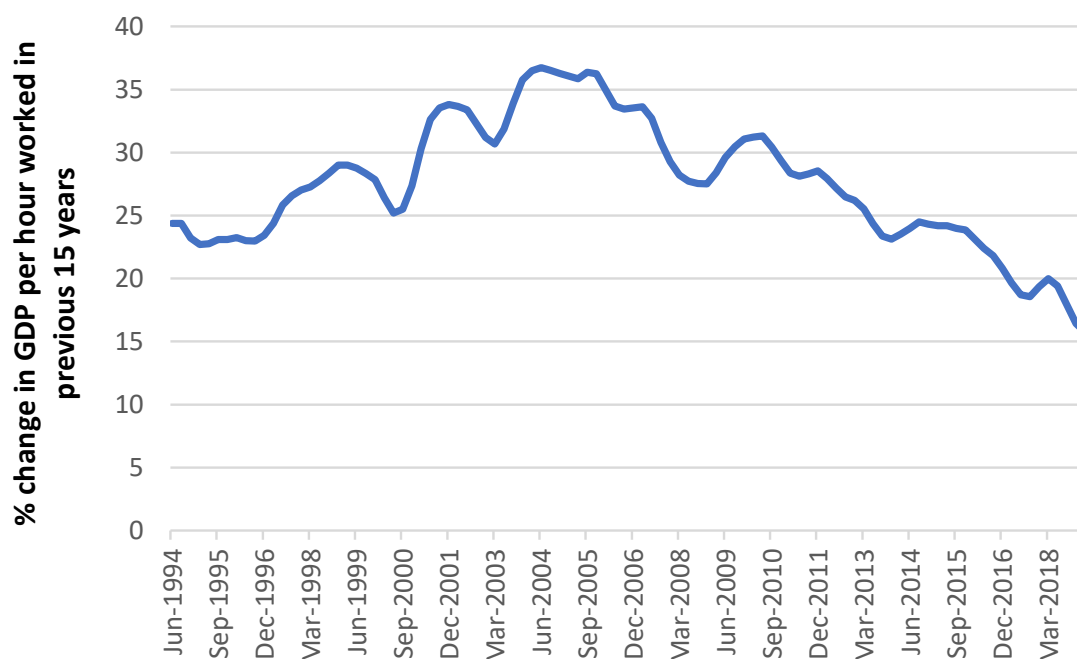
2.7.1 Productivity Effects

Productivity is a measure of how effectively (compared to past times or other places) the resources used in an economy produce desired outcomes. Typically measures relate inputs of capital and labour (human capital) to measured, valued outputs, particularly GDP. The essential idea of effectiveness of resource use can be deployed in different conceptions

of costs and benefits of actions. For example, ‘natural’ capital can additionally be considered as an input and wider measures of outputs, such as indicators of wellbeing, can be utilised. But overall, Paul Krugman’s famous remark is still apposite, that *‘Productivity isn’t everything but, in the long run, it is almost everything. A country’s ability to improve its standard of living over time depends almost entirely on its ability to raise output per worker’*³³.

33 Krugman, P. (1994) *The Age of Diminished Expectations*. MIT Press Boston.

Figure 6: Productivity Growth, Australia, 1994-2019



Source: ABS Cat 5206.0 Australian National Accounts: National Income, Expenditure and Product, Table 1.

Relatively poor, and diminishing in the last decade, falling productivity growth is a major concern for Australian economic policy, see Figure 6. However, an evidenced understanding of how the activities and outcomes of the large-scale housing sector in the economy contributes to productivity has been long ignored as an issue in housing policy making at national and metropolitan-regional scales³⁴. Recent studies in Australia have begun to explore³⁵ and review³⁶ some of the productivity effects arising from housing activities and outcomes but

there is not yet a rich base of data and research to build on. Because neither governments nor lobby groups have attempted to systematically evidence housing quality and price impacts on household capabilities and budgets or on investment decisions and the wider structure of the economy. Despite the longevity of housing policies, research evidence is piecemeal.

Conventional ‘macroeconomic’ estimates of the output elasticities (productivity effects) associated with infrastructure (usually public) investment³⁷ are now disregarded due to inadequacies in data and technique. In recent years, as sustained increases in metropolitan housing costs appear to have driven some households and firms away from high housing cost/high productivity locations to lower housing cost/lower productivity locations, researchers have applied conventional production function analysis (in the general spatial equilibrium framework) to US data³⁸. This work reveals that high house prices have created new economic

34 MacLennan, D., Ong, R. and Wood, G. (2015) Making connections: housing, productivity and economic development. AHURI Final Report, (251), 1-122.

35 MacLennan, D., Randolph, B., Crommelin, L., Witte, E., Klestov, P., Scealy, B., & Brown, S. (2019). Strengthening economic cases for housing policies. City Futures Research Centre. UNSW.

MacLennan, D., and Long, J. (2020) Extending economic cases for housing policies: Rents, ownership and assets. City Futures Research Centre, UNSW Built Environment. <https://cityfutures.be.unsw.edu.au/research/projects/extending-economic-cases-housing-policies-rents-ownership-and-assets/>

36 MacLennan, D., and Long, J. (2020) Extending economic cases for housing policies: Rents, ownership and assets. City Futures Research Centre, UNSW Built Environment. <https://cityfutures.be.unsw.edu.au/research/projects/extending-economic-cases-housing-policies-rents-ownership-and-assets/>

37 Aschauer, D.A. (1989) Is public expenditure productive?. *Journal of monetary economics*, 23(2), pp.177-200.

38 Hsieh, C. T., and Moretti, E. (2019) Housing constraints and spatial misallocation. *American Economic Journal: Macroeconomics*, 11(2), pp.1-39.

geographies of production that have reduced US productivity and GDP by 10%. Despite reservations about methodological framing and technique and, particularly the attribution of causality (planning is always assumed as the prime cause of high house prices in GSE oriented studies), that result poses a major question that Australian, UK and Canadian decision takers should be addressing.

The productivity effects framework developed by our previous work³⁹ avoids a macro, production function, equilibrium-oriented approach. Instead, it links the housing 'characteristics' approach

39 MacLennan, D. et al. (2015) op.cit.

well established in housing economics⁴⁰, the 'capabilities framework' developed by Sen and Nussbaum and 'economic growth drivers' framings developed by economic geographers, such as Storper⁴¹. Integrating these three approaches establishes a framework for piecing together evidence on the range of feedback effects operating through Route 3 in Figure 1, above. Figure 7, below, further outlines the approach (used in this study and in related work).

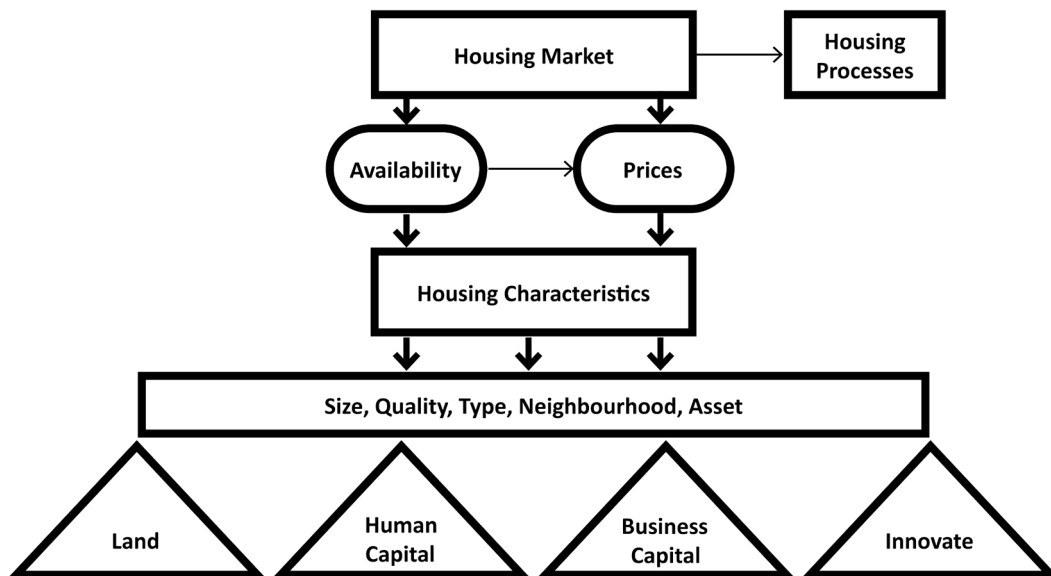
40 MacLennan, D. (2012) *Housing Economics: A Failed Experiment?* Sage Housing Handbook. Eds Clark. W.A.V., Gibb. K.D and Clapham. D.

41 Sen. A.K. (2001) *Development as Freedom*. Oxford University Press. Oxford.

Nusbaum. N. (2011) *Creating Capabilities-The Human Development Approach*. Harvard University Press.

Storper. M. (2014) *The Keys to the City*. Princeton University Press.

Figure 7: Housing characteristics – productivity connections



The logic chain is simple, even if empirical estimations are complex. Housing market interactions of consumers and suppliers drive outcomes, particularly changes in rents and prices, and market related activities (sales, turnover, new construction etc). Two different sets of questions arise. First, are induced activities, such as sales and construction high or low productivity sectors? Second, how do changing rents and prices, reflecting the nature of housing as a complex commodity, impact the attributes of dwellings chosen? Higher prices and rents may induce smaller house purchase,

or lower quality housing, or housing more remote from workplaces (and other sites that households use in the housing market), or they lead to households renting rather than owning their homes. All these effects can be observed in Australian housing markets for middle- and lower-income households in this millennium. And they may all impact economic productivity.

The characteristics of homes can impact capabilities to learn and work (as has been so emphatically demonstrated through the COVID-19 lockdown) and accumulate. Small, low amenity

housing impairs child learning and development; poor quality homes are associated with poor health outcomes that impair schooling, work and income; pushing lower and middle income households further away from employment locations reduces labour productivity, not primarily by raising commuting times but by diminishing the ‘thickness’ and matching effectiveness of labour markets; attenuating homeownership impacts household accumulation of assets and housing price and wealth changes significantly impact investment capabilities.

These capabilities impact the ‘growth drivers’ in an economy. There are housing attribute impacts on the formation and use of ‘human capital’. For example, housing outcomes influence the use of household capital and savings in ways that can impact ‘business capital’ and recent work has highlighted, for small and new businesses, that housing and neighbourhood attributes may influence innovation, growth and ‘small’ entrepreneurship⁴². However, which governments, Federal, State and Local, can say that these economic development aspects of housing are carefully nurtured in national and local economic development strategies? The research evidence (in relation to both Australia⁴³ and UK⁴⁴) is that such conversations rarely occur between those who govern economic development, housing and planning silos at all levels of government. If, for Krugman, productivity is almost ‘All’ governments have often treated the productivity effects of housing as ‘Nothing at All’.

The evidence review on which this Synthesis Report draws, provides a strong prima facie case that ignoring these housing outcome-economy recursive effects impairs productivity and especially in areas that are growing most rapidly.

2.7.2 Construction

As the construction industry contributes a large share to the whole economy, poor productivity

growth in this industry acts as a drag on the whole economy’s productivity performance. A recent survey reported that, contrasted with overall productivity growth of 2.8% for the world economy and 3.6% in manufacturing, global labour-productivity growth in construction has averaged only 1% per year over the past two decades, albeit with large regional differences⁴⁵. If construction sector productivity were to catch up with that of the rest of the economy, the sector’s value added would rise by an estimated \$1.6 trillion, adding about 2% to the global economy a year.

Studies in the US also raise concerns about slow productivity growth. Researchers attribute part of the increase in real housing prices in America before 2006 to slow technological progress in the housing construction sector⁴⁶. Similarly, a later study highlighted that sluggish productivity in construction could account almost entirely for the long-run trajectory in US and OECD housing prices over the 1970s-2000s⁴⁷. Rather than highlighting planning constraints and rising land costs, this study concluded that rising prices stem from the rising costs of inputs induced by growth in other, more productive, economic sectors. Over time, it was argued, housing production has become relatively less efficient and more costly because the prices of factors of production are decided by other most productive sectors. Other studies for the US, Canada, Europe and Japan, New Zealand all report relatively low productivity in the construction sector⁴⁸. Similar studies conclude

45 McKinsey Global Institute. (2017) Reinventing Construction: A Route to Higher Productivity.

46 Iacoviello. M., and Neri, S. (2010) Housing market spillovers: evidence from an estimated DSGE model. *American Economic Journal: Macroeconomics*, 2(2), 125-64.

47 Galesi. A. (2014) Can the productivity slowdown in construction explain US house prices?. manuscript. Madrid: CEMFI.

48 Rojas. E. M., and Aramvareekul, P. (2003) Is construction labor productivity really declining?. *Journal of construction engineering and management*, 129(1), 41-46.

Harrison, P. (2007) Can measurement error explain the weakness of productivity growth in the Canadian construction industry? (No. 2007-01). Centre for the Study of Living Standards. *International Productivity Monitor*, 14 (Spring), 53–70.

Abdel-Wahab, M., and Vogl, B. (2011) Trends of productivity growth in the construction industry across Europe, US and Japan. *Construction Management and Economics*, 29(6), 635-644.

42 Reuschke. D. (2016) The Importance of Housing for Self-Employment. *Economic Geography*, 92 (4). 378-400.

43 MacLennan. D. et. al. (2015) op.cit.

44 MacLennan. D., Miao. J., Christie. L and Long. J et al. (2021) Raising Productivity and Housing the Economy. In, *Productivity and the Pandemic: Challenges and Insights from Covid-19*, McCann P. and Vorley. T. eds. Edward Elgar.

that Australian construction industry productivity has grown slowly and remained relatively stagnant between 1985 and 2010⁴⁹.

But in contrast, it has been reported that labour productivity in the construction sector in Australia has increased steadily, except for the periods from 1998 to 2000 and 2002 to 2006⁵⁰. Existing studies have mostly relied on macroeconomic data (aggregated at the industry-level) to establish and verify the lower than average labour productivity of the construction sector. On the other hand, studies using microeconomic data (disaggregated at the firm-level), suggest a different trend. In relation to New Zealand's construction sector it has been found that labour productivity and total factor productivity (TFP) construction sector had been rising, and not deteriorating, since 2001⁵¹. What is clear from this brief review is that evidence on housing sector productivity is not consistent. Given the scale of the sector and its significant use in stimulus activities it is imperative that Commonwealth and State governments become much more certain of the productivity performance and prospects of residential construction.

2.7.3 Housing Prices, Business and the Allocation of Capital

In a market economy, the allocation and reallocation of labour and capital to producers that can use it most effectively, as induced by market price signals, is an important determinant of aggregate TFP. Housing price changes exert significant effects on the real economy and productivity. Rising housing prices impact resource allocation through the collateral channel when increased household

housing wealth is used to borrow to fund non-housing investments. Supernormal profits from real estate may also attract enterprises to purchase land and as its value increases along with house prices, businesses with more collateral value are less financially constrained and thus may be able to obtain more finance for investment in less productive activities rather than force them to pursue more productive and innovative projects. In contrast, the investment (or 'crowding out') channel may divert a flow of investment funds into housing purchase away from more productive or innovative activities such as small business start-ups, business growth and human capital formation.

Some studies suggest that the collateral channel can have significant, positive effects on investment in business. Recent research also supports the existence of the collateral channel, as housing price growth and firm investment exhibited a positive relationship more marked for capital expenditure (including real estate investments of firms) than R&D spending⁵². This also matters more in housing market downturns (when more firms are likely to be credit constrained) than booms. The collateral effect is more important in countries that rely on bank financing, collateralised lending, and with higher mortgage loan-to-value ratios.

In contrast, some studies report that rising house prices crowd out non-residential investment through capital redistribution. 2014 research, for example, found that high returns on real estate investment lead entrepreneurs to cut down their investment in management and innovation⁵³ and more recent work found that rapidly rising house prices tend to attract excess capital⁵⁴. More widely, an historical analysis of sixteen advanced economies from 1870 to 2015 found that housing returns were similar

49 ABS (2013) Australian Bureau of Statistics. (2013) Estimates of Industry Multifactor Productivity, 2012-13. Cat. No. 5260.0.55.002. Canberra.

Chancellor, W. (2015) Drivers of productivity: a case study of the Australian construction industry. *Construction Economics and Building*, 15(3), 85-97.: Productivity Commission. (2014) Public Infrastructure, Inquiry Report Volume 1, No. 71, Canberra.

50 Campbell, S., and Withers, H. (2017) Australian productivity trends and the effect of structural change. *Economic Round-up*, 1.

51 Jaffe, A. B., Le, T., and Chappell, N. (2016) Productivity distribution and drivers of productivity growth in the construction industry. Available at SSRN 2778910.

52 Suh, H., and Yang, J. Y. (2020) Housing Cycle and Firm Investment: International Firm-level Evidence. Available at SSRN 3612520.

53 Miao, J., and Wang, P. (2014) Sectoral bubbles, misallocation, and endogenous growth. *Journal of Mathematical Economics*, 53, pp.153-163.

54 Rong, Z., Wang, W., and Gong, Q. (2016) Housing price appreciation, investment opportunity, and firm innovation: Evidence from China. *Journal of Housing Economics*, 33, pp.34-58.

to, though slightly higher than, equity returns, but with much less volatility⁵⁵. The higher rate of returns and lower volatility could induce even the most productive companies to invest and diversify into real estate markets, thus limiting investment in other higher-productivity activities. More recent empirical work in China has suggested similar significant effects⁵⁶.

The overall crowding-out effect (also called the investment effect) is more obviously seen in relation to the behaviour of banks. For example, commercial loans can be crowded out by banks responding to profitable opportunities in mortgage lending. The significance is that the former is likely to be associated with gains to economic output and productivity, whereas the latter largely leads to inflation in asset prices, which has no positive feedback to productivity.

The studies underpinning the above observations suggest that collateral channel effects from housing have small impacts on capital reallocation and research and development expenditure in well-established firms. However, it has significance in new firm formation and growth. There is research evidence of a positive correlation between housing prices and entrepreneurship, verifying the existence of a housing collateral channel by exploring how the use of business debt by new entrepreneurs varies with home equity⁵⁷. The same study found that a \$100,000 increase in home equity was associated with business debt being about \$5,000 higher. It also concluded that rising housing prices were more significant for small companies starting a business as they were more likely to be financially constrained. Rising housing prices increased the potential borrowing capacity of credit-constrained entrepreneurs, allowing

them to finance more entrepreneurial activity by using their housing equity.

Research on the crowding-out channel suggests that capital expenditures are significantly influenced by housing market outcomes and shapes which firms, sectors, regions and cities attract capital investment. Others have claimed that housing booms in advanced economies have led to significant capital misallocation across sectors and firms⁵⁸.

The effects of rising housing prices on productivity through capital reallocation depends on two basic aspects: one is whether, and the extent to which, rising housing prices or increase in housing wealth relax financial constraints for firms; the other is in what kind of sectors is the draining effect of rising housing prices most felt? These observations are central to why enterprise economies must have much more regard to sustained, systemic rises in house prices and their impacts upon business. But where is the evidence and active policy discussion on this issue in Australia? Our review suggested it is largely absent.

2.7.4 Housing Outcomes (Physical Quality, Location and Tenure) and The Formation and Use of Human Capital

Early 'merit good' concerns for housing included the notion that housing opportunities for all income groups and tenures were believed important in developing the capabilities of individuals, households and, indeed, communities. It was noted above that this core policy advocacy case still needs to be strengthened by demonstrating that better quality and more affordable homes and neighbourhoods in fact foster higher levels of human capital with significant wellbeing and productivity effects. Some researchers have drawn together the scattered studies of housing outcome effects on health and education outcomes and the formation of human capital,

55 Jordà, Ò., Knoll, K., Kuvshinov, D., Schularick, M., and Taylor, A. M. (2019). The rate of return on everything, 1870–2015. *The Quarterly Journal of Economics*, 134(3), 1225-1298.

56 Shi, Y. (2017). Real estate booms and endogenous productivity growth. *Job Market Paper*. Massachusetts Institute of Technology, July, 9.

57 Connolly, E., La Cava, G., and Read, M. (2015) Housing prices and entrepreneurship: Evidence for the housing collateral channel in Australia. In *Small Business Conditions and Finance*, Proceedings of a Conference, Reserve Bank of Australia, Sydney (pp. 115-144).

58 Fougère, D., Lecat, R., and Ray, S. (2019) Real estate prices and corporate investment: theory and evidence of heterogeneous effects across firms. *Journal of Money, Credit and Banking*, 51(6), pp.1503-1546.

Cette, G., Corde, S., and Lecat, R. (2017) Stagnation of productivity in France: a legacy of the crisis or a structural slowdown?. *Economie et Statistique*, 494(1), pp.11-36.

particularly for children from low-income households and young people. However, as confirmed by this literature review, there has been very limited official and academic attention to these questions. This means that hypotheses on the effects of housing on the formation and use of human capital often lack rigorous empirical confirmation⁵⁹. Indeed, it is challenging to identify which attributes of housing can be reasonably expected to affect the formation and use of human capital and by which mechanisms, especially in the absence of a large evidence base of intervention studies⁶⁰.

That said, there is *prima facie* evidence from our own work that physical housing outcomes (e.g. overcrowding and space for study) will influence the wellbeing of households and their ability to develop productive capabilities⁶¹. The association between poor housing conditions and poor childhood development and school performance is increasingly well-documented, supported by a diverse and growing body of academic evidence. The aspects of the home that have been empirically identified by the existing literature to influence children's development include: cleanliness, housing disrepair and safety; crowding; housing affordability; homeownership; frequent residential moves and homelessness. Neighbourhoods shape access to public and private services, social standing, social interactions and social capital as well as a context for children to learn and develop⁶².

Location matters too. Households accessing affordable housing closer to jobs, education and services, compared to a situation with poor access to affordable housing and low proximity to jobs, raise their incomes and productivity.

59 Meen, J., and Nygaard, A. (2010) Housing and regional economic disparities. Department for Communities and Local Government, Economics paper 5. ISBN: 9781409812074: MacLennan et al. (2018) *op.cit.*

60 Dunn, J. R. (2020) Housing and Healthy Child Development: Known and Potential Impacts of Interventions. Annual review of public health, 41, pp.381-396.

61 MacLennan, D. et al. (2018) *op.cit.*

62 Dockery, A. M., Ong, R., Colquhoun, S., Li, J., and Kendall, G. (2013) Housing and children's development and wellbeing: evidence from Australian data. AHURI Final Report No.201. Melbourne, Australian Housing and Urban Research Institute Limited.

There is evidence that workers are more likely to invest in human capital when they have access to plentiful opportunities within local job markets⁶³. A wider discussion of how housing location choices by households impact agglomeration economies, and how house prices may also induce firm relocations, is included in the main report on which this summary is based.

Findings from the large body of studies on housing and educational performance include the observations that children of homeowners receive better grades and have higher rates of high school graduation. But few studies have disentangled the entwined aspects of selection effects of parental income, housing tenure and neighbourhood effects. In consequence, despite a century of active housing policies, we have little strong evidence developed to support the *prima facie* beliefs that high rent burdens and poor housing impact human capital formation.

For adults, homeownership could bring positive benefits to individual subjective well-being. Several mechanisms by which homeownership might exert such effects: on life satisfaction, on self-esteem through a sense of status, and on sense of control via the experience of freedom at home.

As this brief review makes clear, the patchy nature of evidence on housing and productivity, the missing questions about the economic effects of rising house prices in public debate and the absence national and local policy conversations on the topic seems to leave our housing policy elephant in the government room undisturbed. The key question remains: is the Australian Government, like its predecessors, content to drive an economic system based on taking the rewards from scarcities (a rentier economy where some Australians only gain at the loss of others) rather than innovation and effort (an enterprise economy, where growth and trade make mutual gains and enhance Australia's international competitiveness). But what policy initiatives might begin to change understanding and outcomes?

63 Rotemberg, J. J., and Saloner, G. (2000) Competition and human capital accumulation: a theory of interregional specialization and trade. *Regional Science and Urban Economics*, 30(4), pp.373-404.

3. Conclusions, Policy Processes and Priorities

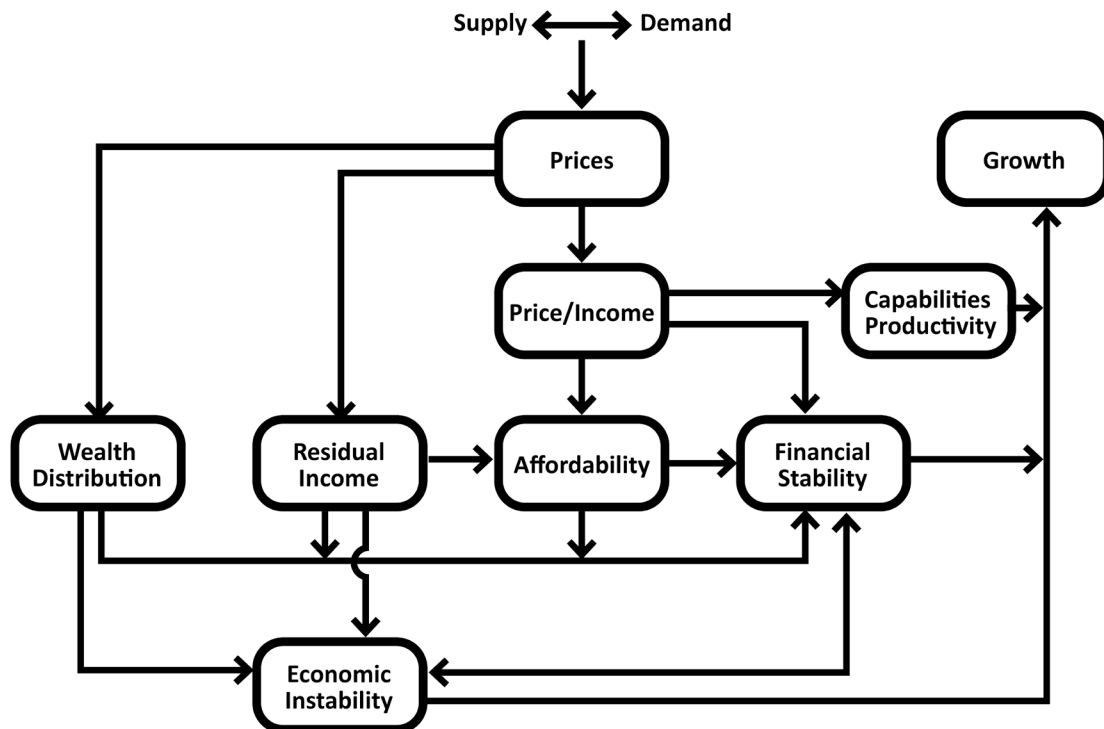
3.1 Homes for Australia, Today and Tomorrow

Policy research reports typically focus on a well-defined question that can draw on a stockpile of existing national evidence to underpin specific, costed proposals for policy action. Recommendations are usually directed at a limited number of governments and their agencies. They make proposals for immediate and specific government actions. This project is different. It has reviewed available literature, drawing on national and international understandings, but that process also revealed

a fragmented, limited availability of applied economics and social research on the economic consequences of Australian housing systems and the policies that shape them.

Our synthesis reveals that there are major issues in Australian economic performance that are closely connected through the outcomes of the housing system, as summarised in Figure 8. The contribution of this report is to highlight these connections and our main conclusions concern the governance of these housing system issues. We do also highlight, below, two immediate policy actions for the Australian Government and two more for States and metropolitan entities.

Figure 8: Connected effects and Housing policy problems



Our main conclusions are about better understanding and governing housing effects on the economy and they are not just directed at government but at 'politics' more widely. Our call for a longer term, better linked understanding of what housing means for the economy applies to the press too. It is not uncommon to scan a major newspaper and read, in successive pages, of the

tragedy of rising rates of local homelessness and the triumph of faster rising house prices. Could these issues be related? And in the business sector there needs to be a clearer debate about how rising land and property values impact the investment and wage costs of businesses that trade globally and really require well- functioning, dense labour and housing markets. Australia

may be burying much of the gain from three decades of impressive metropolitan growth in the sands of rising property values and driving talent and successful firms away from the most productive locations for the future to the lower cost localities of today.

We look to all these national influencers to develop a more coherent understanding of how the present housing system not only fails to provide adequate and affordable homes for a growing and substantial share of Australians but impairs national economic performance on major measures of economic success. We do not expect a consensus to emerge from this work, but we do hope for a sustained, informed national conversation that leads to fairer outcomes and faster growth.

3.2 Addressing Adverse Outcomes

There are stark conclusions from our reviews of literature and expert opinions. In this millennium, housing outcomes in Australia have made the distributions of wealth and incomes (after housing costs) more unequal. The debt exposure and potential instability of the housing market has increased significantly as the global economy heads into a period of significant uncertainty. There is growing prima facie evidence that housing outcomes may have previously unrecognised negative effects on productivity undermining contemporary growth processes. Put starkly, current and affluent Australians become wealthier because they capture, from other younger Australians, and enjoy the gains from housing scarcity rather than primarily prospering on the basis of effort and innovation that leads to gains from trade and for all. Is this really the basis on which to build an economy, and homes for younger and next generation Australians?

This question, arguably, could have been posed at any time in the last thirty years. It is now more urgent than ever because the most obvious consequence of the early economic recovery from COVID-19 has been the next unjust, unstable and unproductive property boom. And

why should politics listen? Our review suggests that there is potentially a new political economy emerging that may seek a different approach to affordable housing. The bigger cities are edging back to 50% renters, there is a significant dissatisfied margin of younger households who will become owners (if at all) a decade later than their parents and indeed only if these parents provide substantial equity tranches for market entry. There is a rising share of existing owners stressed by the experience, with more returning to renting.

The homeownership sector has changed, in ways that seem to be poorly recognised, since the 1970s. But neither promoting nor reducing the ownership share will solve the key issues. They largely stem from the sustained policy neglect to ameliorate and stabilise rising housing prices. How did a nation much concerned with beating wage inflation and targeting the overall inflation rate (quite successfully) fail to assess and deal with the economic damage arising from sustained real house price increases?

3.3 Changing Housing Policy Processes and Priorities

At the heart of difficulty is a substantial capacity deficit, of skills, institutions and governance structure to construct a coherent housing strategy, and policy, for Australia. Housing policy has traditionally been focussed on the provision of housing stock and support for poorer households. It had a policy agenda dominated by notions of needs, merit goods and redistribution. That approach has been eroded in Australia for three decades, public housing has stagnated, non-profit provision has been stalled whilst Housing Ministers have disappeared from Cabinets, been reduced to minor shares of portfolios.

At the same time, as markets shares of provision have increased governments have not developed the capacities to understand and manage housing markets and their economic consequences. There are few economists within Federal and State governments familiar with the housing sector from any education

in housing and urban economics, and this contrasts with officials with backgrounds in labour economics and monetary economics and indeed this may reflect the minority interest of Australian economics in housing system issues. Where Economic Analysis and Policy selected, in 2020, it's 50 most significant papers for the Fiftieth Anniversary edition, not one of these examined housing sector issues. Arguably, only the Reserve Bank keeps a strong interest in one aspect of the housing system but does so with models that assume away key features of the housing system, especially at metropolitan levels.

In consequence interest in and arguments for housing policy support are poorly developed and fragmented across different sectoral silos within Commonwealth Governments, and indeed State Governments too. That fragmentation needs to change and a Cabinet post for Housing Policies and Outcomes, and a close interest from the Prime Minister's Office is required. In 2020 the Prime Minister proposed sub-committees of National Cabinet would be formed and include state/territory premiers to tackle key national issues. Such a sub-committee for housing should be formed, now.

This report has highlighted that housing systems are large scale and complex in the economy. Effective outcomes require not only collaboration within an order of government, but across all of them. In Australia, just as in comparator federations, the proper roles of national government include addressing issues that manifest at a local level but have nationwide spillovers and wider than state effects. They also have policy autonomies and fiscal bases

unavailable to state and municipalities. Some system difficulties and policy inadequacies/ absences reflect Commonwealth Government choices – for instance in monetary and fiscal policies or immigration policy. Others arise at state level – including inadequate social housing delivery strategies and poor strategic planning and delivery of land use change, infrastructure and other services. Similar remarks can be made regarding local government. Our research reconfirmed the evidence that at these sub-national levels housing, planning and economic development officers seldom converse about how housing hinders or facilitates economic growth. Conversations across sectors and levels would be an essential start to change.

Given the shattered housing policy governance structures that prevail in Australia there is a case that the Commonwealth needs to establish a clear national housing strategy, including a housing market strategy. To shape and deliver that strategy, a national housing agency under Commonwealth Treasury is required to establish an enduring specialist policy capability to advise the Commonwealth Govt, and act as a champion for achieving effective housing-economy outcomes and promoting affordable housing. It should also re-create the analytical capacity of the National Housing Supply Council. A national strategy process could stop the self-serving 'blame-game' where monetary policy officials lay the responsibility for house price inflation and the door of state and local planning departments, and Commonwealth Ministers ignoring the fiscal funding system download responsibility for funding affordable housing provision to state/territory governments. None of that rhetoric matches the problem.

There are no serious supply constraints through the planning system in our country ... the constraint rests with the holders of those developable sites [Consultant C2] – quotation from in-depth interviews report.

To help set the longer vision for Australian housing outcomes and policies, and frame renewed government approaches we also believe that a

Royal Commission on Housing Future Australia, that would embrace all the major issues identified in this report, be established.

3.4 Starting Now

In the meantime, there are short-term actions that might constrain the present boom. For the Commonwealth Government, as recovery continues and first homeowner grants stimulate as much house price inflation as long-run net additional owners, there may be merit in switching stimulus efforts to the affordable rental sector with potentially lesser inflationary consequences. At the macro level, there may be immediate benefit in expanding the formal accountabilities of the RBA to include maintaining a more price stable and well-functioning housing market. At the state/metropolitan level, there should be an immediate requirement to investigate the housing supply chain within metropolitan and rural areas and to identify the range of relevant blockages to faster and fuller supply responses to price pressures.

We need less theory and more evidence informing Premiers and Prime Ministers on what really holds up housing delivery. And at these more local scales there should be a prompt Premier-led review of how better cross-action links between housing, planning, infrastructure (transport) and economic development can shape better economic performance of the housing system.

Key recommendations

As we noted above, reversing the substantially problematic trajectory of Australia's housing system over recent decades will call for extensive tax, regulatory and other policy reforms. However, a pre-condition for any such program of work is the reshaping of relevant over-arching institutional frameworks. It is with this understanding in mind that the measures proposed above have been framed.

To summarise the discussion in this final section, the following key recommendations are proposed to help open the eyes of the blind men to focus on how best to tame the housing elephant in the economy:

- Given the fundamental nature of the issues involved, given their disparate nature across departments and levels of government, and to frame renewed government approaches, a **Royal Commission on Housing Future Australia** should be set up.
- A **Cabinet-rank post responsible for Housing Policies and Outcomes** should be re-established in the Commonwealth Government, a position that – given the highly diverse range of relevant policy instruments – should be closely linked to the Department of Prime Minister and Cabinet.
- As a crucial vehicle for inter-government co-ordination in this policy area, a **permanent Housing Committee** should be created as part of the National Cabinet structure.
- The Commonwealth Government should commit to developing a **National Housing Strategy**, including a housing market strategy.
- Expand the National Housing Finance and Investment Corporation (NHFIC) as an enduring **National Housing Agency** tasked with informing government policy-making, championing actions to enhance housing-economy outcomes, promoting affordable housing development and re-establishing the analytical capacity of the former National Housing Supply Council.
- In the immediate term, Australian governments should give consideration to **switching housing stimulus** efforts from market housing to the social rental sector with potentially lesser inflationary consequences.
- The Australian Government should **expand the formal accountabilities of the RBA** to include maintaining a more price stable and well-functioning housing market.

