Australian Institute for Progress

Analysis of ALP "Help to Buy" policy

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ALP's Help to Buy policy

Summary

The ALP's "Help to Buy" policy is a "rich uncle scheme", or a variation on "the bank of mum and dad" where the federal government becomes the rich uncle to a small group of homeowners, or goes *in loco parentus* to get them into the housing market. The federal government will co-invest with a first home buyer up to 40% of the price, for new homes, and 30% of the price of an established home if they meet income caps and price caps.

There is no evidence that the ALP's policy will increase home ownership in Australia. Rather it will only change the composition of first home buyers by increasing the capacity of some purchasers to buy and service a loan, pushing up prices from where they would have been, and squeezing other purchasers out of the market.

If an Australian government wants to increase home ownership then it must increase the supply and lower the cost of developing new houses – the new housing market sets the price of established housing and this will reduce prices and increase opportunities. This requires an overhaul of our interest rate regime, as well as reform of taxes and regulations that inhibit the production of new dwellings. Most of the taxation and regulatory regime is imposed by the states, so solving the housing crisis is a complex project.

While the major barrier to entering the housing market is saving the deposit, the ALP policy is poorly targeted so that it not only reduces the deposit required but also subsidises occupancy costs. As our Housing Affordability Index demonstrates, occupancy costs are not unusually unaffordable and are close to the cost of renting. However, the time taken to save a deposit is at, or close to, record highs. So the purchasers favoured by Labor's scheme are receiving a taxpayer subsidy not just for their deposit, but also for their repayments where it is equal to around 30%-40% of the market rent of the property.

Specific problems with the policy are:

1. It will have marginal effect as it will only be available to 8% of first homeowners each year, and many, if not most of these, will displace others who would have been in the housing market.
2. Other programs offer greater leverage. The ALP program will fund approximately 10,000 first homeowners each year for four years – a total of 40,000. By contrast, the Commonwealth Government's HomeBuilder grant, instituted in June 2020, has been accessed by 80,000 applicants so far, with a total of 137,000 applications[i] – this in less than two years. The ALP program will have a greater cost than HomeBuilder. Total cost of the Labor scheme, will be $76,525 per capita over its life, plus administrative costs, versus HomeBuilder's per capita cost of $20,000.
3. It is a regressive expenditure measure which gives more money to first homeowners who are better off and can afford a more expensive house.
4. It is inequitable between Australians, and, for example, provides up to an $18,000 p.a. benefit to Australians who are in the workforce in savings on their occupation costs. This compares to money spent on other welfare measures. For example, the maximum payment

under rent assistance is $10,068 p.a.; $25,678 pa is the pension paid to a single aged pensioner; and $17,960 is the JobSearch allowance for a single parent with children.

5. It enriches some buyers at a cost to other buyers who will be squeezed out of the market because they have to service 100% of their debt while the beneficiaries of this scheme only need to service 60% to 70%, so they can afford to bid higher for the same property even though the rest of their circumstances are the same.
6. It would appear, given the promise that borrowers will avoid mortgage insurance, which would be mandatory on a 2% deposit, that the Commonwealth would underwrite any loss on the property in the case of sale or default. This is an unquantifiable, but real additional financial risk.
7. At the moment there are around 120,000 first home buyers a year, and it will assist 10,000 purchasers - just one month's demand. So it discriminates against the other 91.5% who cannot access the scheme.
8. Its claims are false and misleading. It does not "cut the cost of housing". The same, or higher costs, will remain. However, some of these costs and risk will be shuffled across to the taxpayer, while the recipient will receive a rent benefit paid for by the taxpayer.
9. It represents a transfer of tax-payer wealth to Sydney and Melbourne where government equity will be more than twice what is available to purchasers in parts of Tasmania, South Australia and Western Australia, and still significantly more than the other capitals.
10. It represents a financial risk to the government which will own up to 40% of an asset that is likely to decrease in price in the short term as interest rates rise. The government will then forgo income on the money invested, capitalise the interest cost (this scheme will be funded by borrowings in the absence of a budget surplus) and hope to recoup its interest and opportunity costs out of the eventual sale of the house. As it will have no control over when the sale occurs or how the asset is maintained, this compounds the risk.
11. The real problems with housing are that interest rates are at thousand-year lows, which contributes around 70% to current house prices, and regulatory and tax imposts contribute the other 30% by inhibiting supply. These problems need to be solved, rather than applying a band aid of *ad hoc* discriminatory measures which will increase the problem.
12. An alternative solution to the affordability of home deposits is to allow first home buyers to borrow from their superannuation for their deposit. As we have shown, this will give them a better investment return, and it does not involve the Commonwealth in extra risk, or discriminatory practices.

What is the "Help to Buy" scheme?

It is a "rich uncle scheme", or a variation on "the bank of mum and dad" where the federal government becomes the rich uncle to a small group of home owners, or goes *in loco parentus*. The federal government will co-invest with a first home buyer up to 40% of the price, for new homes, and 30% of the price of an established home.

The home buyer has to meet certain income and deposit criteria. They must have 2% of the gross price of the house as a deposit, and the money to pay for legals, stamp duty and any other conveyancing costs. A single person who earns $90,000 or less per annum would be eligible as would a couple earning $120,000 or less. The purchaser will also be responsible for maintenance and other outgoings.

Purchasers do not pay interest or rent on the government's equity and can progressively buy the government out, if they wish, and if their income exceeds the cap, they will be required to buy the government out immediately, on unspecified terms.

What is the problem to be fixed?

Housing affordability has been an issue for a number of years, but only in terms of the deposit. Our research establishes that repayments in most capital cities are not radically higher than they were in the 90s, and show a cyclical pattern. The area where housing affordability is a problem is in the case of the deposit required to purchase a dwelling.[ii]

Our research also shows that the increase in dwelling prices has been significantly driven by the decline in interest rates, which accounts for around 70% of the increase. This is confirmed by RBA research.[iii]

Deposits are not normally a problem for owners up-grading as they already have equity in their existing dwelling, but it is a problem for first home buyers.

What solutions exist to the problem currently

There is a number of formal and informal solutions to this problem which work with the current structure of the housing market. There are also superior solutions which reform the structure of the market to make it more efficient.

First Homeowner Schemes

Various state governments provide first homeowner schemes which give a cash amount upfront to eligible buyers to help with the purchase of a dwelling. While some economists (eg Saul Eslake[iv]) criticise these as doing nothing for affordability because they theoretically push the price of housing up by the amount of the grant, they are wrong that it doesn't increase affordability. If the lack of a deposit is the bar to owning a house, a first homeowners scheme helps to ameliorate that, and the cost to the purchaser is a marginal increase in repayments.

Shared equity schemes

Victoria[v] and Western Australia[vi] both have shared equity schemes, which are similar to the proposed Labor national scheme.

HomeBuilder Grant

The Commonwealth Government also has the HomeBuilder scheme.[vii] This was a measure to stimulate the building industry during COVID by making new construction more affordable which also brought first home buyers into the market. It was a fixed sum available to anyone anywhere in Australia who met the criteria, and was the same amount everywhere.

Other government schemes

Other government schemes include:

- Home Purchase Assist
- The Indigenous Home Ownership Program
- The First Home Loan Deposit Scheme
- The Family Home Guarantee[viii]

"Rich Uncle" or "Bank of Mum and Dad"

Anecdotally a lot of Australian first home buyers solved the problem by borrowing from friends or relatives. This might be on the basis of paying the loan back over time; an effective, but undocumented equity stake in the property; or a straight-out gift (perhaps viewed as an early instalment of inheritance).

Borrowing from own Superannuation fund

The federal government has the First Home Super Saver Scheme whereby eligible Australians can save additional money in their superannuation account towards a deposit. This gives them some tax advantages in saving.

We have advocated[ix], based on schemes overseas, and our own financial modelling, that first home buyers should be able to borrow from their superannuation for a first home deposit.

Structural solutions

While repayment affordability has stayed relatively constant over the last almost 30 years within Australia, we do have some of the highest housing prices in the world. This is as a result of structural issues – town planning restrictions on land use; attenuated approval processes; taxation of development; and ultra-low interest rates. This has resulted in deposits being relatively unaffordable compared to 30 years ago.

Any serious attempt to improve housing affordability has to address those issues over time. This will be difficult as three of the four are mostly set by state governments, and the fourth, interest rates, is set by an independent body, the RBA. The federal government has limited levers to improve housing affordability, apart from persuasion.

The RBA has just raised interest rates, and this will eventually have a cooling effect on house prices, but rates have a long way to rise to be back to any sort of historical average. Current interest rates are the lowest ever in recorded history since money first started to be lent and records kept in Babylon[x].

Added to that, any increase in structural affordability will come at the cost to existing homeowners of a real decrease in housing values. This could have economic effects by inducing a negative wealth effect, as well as alienating the majority of the Australian community who are homeowners.

Does the ALP policy address the problem?

The straight answer is yes, but not in a significant way. The policy is political theatre – it is meant to signal that the ALP cares about housing affordability, but not to cost it too much to do so.

By helping with the deposit it will make it easier for some Australians to purchase a house, because the deposit is the issue. By providing such a generous benefit it will also push house prices up for all other first home buyers. Because only a small percentage of home buyers can access this scheme, this will mean that some other purchasers who were not quite as marginal will now become more marginal. As a result it probably won't change the number of first home buyers, just the composition of who they are.

Projections of new home buyers are difficult to quantify, but ABS figures show that in February this year there were 9,994 first home buyers[xi] suggesting around 120,000 per year. The ALP policy would assist only 8% of those. The effect is likely much lower as some of the 8% may well have found other ways to finance a house purchase, and as noted some other buyers will be forced out of the market because they don't quite meet the criteria.

To see how marginal the policy is, compare it to the government HomeBuilder grant which since June 2020 has provided finance for new builds or renovations to 80,000 home buyers, with a total of 137,000 applications. The eventual figure will be higher than 80,000 because the scheme has sometime to run and some of the additional 57,000 will be successful. Most of this grant went to new home buyers, many of whom were first home buyers.[xii]

Is the ALP policy well-designed?

The straight answer to this is no. Apart from not making a significant contribution to overall housing affordability it is inequitable and regressive.

A regressive policy

The table below taken from the ALP online policy document "Helping More Australians into Housing"[xiii] shows how much is available to home buyers. The most striking aspect is that, unlike any other affordability policies of which we are aware, it proposes different amounts of assistance depending on where the purchaser lives. For a new house it ranges from $380,000 in Sydney and NSW Regional Centres down to $160,000 in country SA, Tasmania or WA. For existing homes the range is $285,000 to $120,000.

ELIGIBLE REGION	PROPERTY PRICE CAP	MAXIMUM SAVING ON NEW HOME PURCHASE	MAXIMUM SAVING ON EXISTING HOME PURCHASE
NSW – capital city & regional centres	$950,000	$380,000	$285,000
NSW – rest of state	$600,000	$240,000	$180,000
VIC – capital city & regional centre	$850,000	$340,000	$255,000
VIC – rest of state	$550,000	$220,000	$165,000
QLD – capital city & regional centres	$650,000	$260,000	$195,000
QLD – rest of state	$500,000	$200,000	$150,000
WA – capital city	$550,000	$220,000	$165,000
WA – rest of state	$400,000	$160,000	$120,000
SA – capital city	$550,000	$220,000	$165,000
SA – rest of state	$400,000	$160,000	$120,000
TAS – capital city	$550,000	$220,000	$165,000
TAS – rest of state	$400,000	$160,000	$120,000
ACT	$600,000	$240,000	$180,000
NT	$550,000	$220,000	$165,000

This means that the wealthiest home purchasers (as defined by those who can afford the deposit etc. for the higher priced properties) get the most benefit from the government. As the homebuyer does not have to pay rent on the government's equity they effectively receive a subsidised rent, which is higher, the higher the government equity. On top of that, assuming capital gains are constant across the nation, the purchaser will also receive a larger capital gain on sale.

To put this into context, according to the ALP document it provides up to an $18,000 pa benefit in repayments the homeowner will not have to make, but other Australians in the same situation will. This is a significant sum compared to other government welfare outlays. For example maximum Commonwealth Rent assistance is $10,068 per annum; JobSearch for a single person with a child is $17,966 per annum and a single pensioner will receive $25,678 pa.

It is also a significant sum compared to other first homeowner schemes. The first homeowner grant is a one-off sum which varies by state. In Queensland it is a total of $15,000[xiv]; in NSW a relaxation transfer duty - $38,055 on a $950,000 house[xv] plus a capital amount of $10,000 for a new house[xvi]; Tasmania $30,000[xvii], South Australia $15,000[xviii], Western Australia $10,000[xix]

We've highlighted the difference between cities in this analysis, but the same thing will be true within cities and states. The person buying the more expensive property will receive a larger boost from the federal government and regions are discriminated against in favour of capital cities.

Inequity

It is axiomatic that government policy should treat two people in the same situation the same way. This proposal breaches that principle. This problem is related to the regressive nature of the tax which increases assistance on the basis of the size of the asset being purchased. Because average dwellings are more expensive in cities, it ties higher rates of assistance to those who live in cities, particularly Sydney and Melbourne, irrespective of their circumstances. So two people in different parts of the country become eligible for different amounts of assistance even though their incomes and needs may be exactly the same.

Consider if this were to become a general principle of welfare. That would mean different rates of welfare depending on where a recipient lived. Rather than seeing all people as equal, the policy privileges those who choose to live in certain locations and steals resources from the smaller states and non-metropolitan areas and transfers them to the large cities.

It contrasts with the way in which all other housing assistance is provided by the various governments where support is a fixed sum, available to all who meet the income and other criteria. So, for example, HomeBuilder was originally $25,000, whether you lived in Townsville, Toowoomba, Brisbane or Sydney.

Financial aspects of the scheme

The policy says that the cost over the forward estimates (ie the next four years) is $329 million. This was confirmed by the Opposition Housing Spokesman in an interview with Newscorp "The $329 million is part admin costs for the scheme and part of the interest that we pay on the money we borrow to invest in the homes." He also claims this has been costed by the Parliamentary Budget Office. [xx]

The Parliamentary Budget Office ignores the capital cost of the program because the borrowings are matched by assets, however they have said they are $7.3 Billion[xxi]. This tends to confirm that the PBO used 2% or so as the interest rate. As a result of the RBA's raising of the cash rate Commonwealth 10-year bonds are now trading at approximately 3.5% rather than the 2.078% they were trading at on March 7[xxii].

If we apply a rate of 3.5% the scheme is costing the government $516 m in interest over the forward estimates, but this is uncapped and will cost $256 m each year after that until the owners repay the Commonwealth or sell the property. With the average tenure in an Australian dwelling being approximately 10 years[xxiii] and assuming no repayment of the government's equity by purchasers, this will amount to $3.075 billion, making this a $10.375 bn scheme, plus administration costs.

Year	Capital Investment pa	Total Government investment	Interest pa	Interest rate
1	1,825,000,000	1,825,000,000	36,500,000	3.50%
2	1,825,000,000	3,650,000,000	95,812,500	3.50%
3	1,825,000,000	5,475,000,000	159,687,500	3.50%
4	1,825,000,000	7,300,000,000	223,562,500	3.50%
Forward estimates			515,562,500	3.50%
5		7,300,000,000	255,500,000	3.50%
6		7,300,000,000	255,500,000	3.50%
7		7,300,000,000	255,500,000	3.50%
8		7,300,000,000	255,500,000	3.50%
9		7,300,000,000	255,500,000	3.50%
10		7,300,000,000	255,500,000	3.50%
11	- 1,825,000,000	5,475,000,000	223,562,500	3.50%
12	- 1,825,000,000	3,650,000,000	159,687,500	3.50%
13	- 1,825,000,000	1,825,000,000	95,812,500	3.50%
14	- 1,825,000,000	-	31,937,500	3.50%
Total			**3,075,125,000**	

Notes:

1. As the average tenure in the first home is around 10 years some will exit the scheme earlier, and some later. We have not tried to simulate this over the whole life of the scheme but used 10 years as an approximation. Costs will stretch out over more than 10 years.

2. Half the interest cost of total new outlays each year is assumed to be paid in the year of outlay.

3. We have assumed on average the Commonwealth is paid out on sale of the property rather than in 5% increments during occupation.

4. The model ignores appreciation in the value of properties.

This compares unfavourably to the HomeBuilder scheme where we estimate from Budget Paper No 1[xxiv]that the total cost of the scheme is $2.4 billion and that this would cover 120,000 Australians. On a per capita basis Help to Buy will cost some $76,878, while HomeBuilder cost $20,000, almost a quarter.

But there is an additional element to the Labor scheme which will affect its cost. HomeBuilder is a straight cash benefit, but Help to Buy is a co-investment, and exposes the Commonwealth to the potential of capital loss which would increase the actual cost, or capital gain, which would decrease it. With interest rates on the way up[xxv]and 70% of the price of housing explained by interest rates, then there will be a real decrease in dwelling prices over the next few years. Major banks are forecasting around a 13% drop in prices in 2023[xxvi]. That would potentially add $325m to the cost of the first tranche of $2.5 billion over the next 12 months. Added to that is the real value of the money which at the RBA’s inflation forecast of 4.75% next year and 3% the year after would add a combined $268.75m.

Apart from overall market risk the Commonwealth would also be exposed to property and site-specific risk. This might be expected to even-out over a large portfolio, but this is not necessarily the case as one would expect the properties purchased under this plan to be cheaper than average, and therefore not as well-positioned. Owners may be less inclined than average to maintain their properties, and more likely to experience financial problems. This could, at the least, substantially increase administrative costs. As outlined in the next section there would also be the possibility of an increased capital loss in the case of a distressed, mortgagee in possession sale.

The policy states that the purchasers will also avoid mortgage insurance. The only way this could be avoided on a 2% deposit is if the Commonwealth is guaranteeing the banks against loss across the whole of the asset. Given the purchaser is unlikely to have surplus capacity in the event of a default, the risk to the Commonwealth is leveraged from 30 to 40 per cent of the asset to 100 per cent.

A further issue is that the scheme assumes that purchasers will pay the Commonwealth government out at some stage, but why would they? The subsidy in the scheme is significant, and disappears when the property is sold and another property purchased, or when the purchaser pays out the government (which it can do in 5% blocs). If the subsidy is $18,000 a year, then 5% represents $900 a year subsidy that is lost. Why would one assume that the purchaser would be happy to forgo that. Indeed if one assumes that interest rates will rise, the subsidy becomes substantially more than that. It's likely that, as with social housing, once an owner/tenant is ensconced in a scheme they get used to the benefits and are resistant to any change. This liability could carry on much longer than the scheme envisages.

Fiduciary Duty

One should also ask whether it would be wise for the Commonwealth to offer an additional inducement to the more vulnerable purchasers to enter the housing market at what is likely to be a peak. While the Commonwealth is not strictly speaking a fiduciary for citizens, it surely owes them a duty not to recklessly put them in a position of personal financial risk.

The alternative to buying a house is to rent. According to Domain the average rental yield in Sydney is 2.5%[xxvii], which would imply rent of $1,979 per month on a $950,000 house (the price cap). Using the Commonwealth Bank’s online “Home loan repayments” calculator repaying a loan for 60% of that less 2% deposit over 30 years at the CBA’s current rate of interest of 2.1% would cost $2,090 per month[xxviii], line ball with rent, omitting maintenance and rates. However, raise it to 4% and repayments jump to $2,641 per month. 5% (still historically cheap) would see that increase to $2,968 per month, approximately 50% higher.

If 50% higher payments were too high for the borrower and they had to sell, they would also face a capital loss, for which they would have no buffer as their initial deposit was only 2%. In this situation walking away and declaring bankruptcy might be their only option. This would lead to a distressed sale and an even greater than average capital loss. What assessment has the ALP done of this risk? Is it a risk they believe they should be encouraging less well-off Australians to take?

The other situation that might result in a forced sale is if the income of the borrower were to rise over the cap. This could also force a sale at an inopportune time.

The Commonwealth would share in these capital losses for its 40% of the property.

Cheaper Housing

The ALP document says at its first claim: “An Albanese Labor Government will help more people buy a home sooner by cutting the cost of buying a home by up to 40 per cent.”

This is untrue. The price of a house will stay the same. A purchaser will have to come up with 100% of the price if they want to own the home. The only difference to cost will be in the subsidy the purchaser would receive from the government by not having to pay interest on the government’s equity. On the $950,000 Sydney property, the total cost of purchasing it over 30 years would be $1,284,869 at 2.1%. 40% of that would be $513,947.60, which represents 28.5 years of co-ownership with the Commonwealth, with the homeowner still being no closer to owning the whole property.

This claim is wrong and ought to be corrected as soon as possible.

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[i] https://treasury.gov.au/coronavirus/homebuilder

[ii] https://aip.asn.au/2022/01/australian-housing-affordability-index-september-2021/

[iii] https://www.rba.gov.au/publications/rdp/2019/2019-01.html

[iv] https://www.domain.com.au/news/the-future-of-victorias-first-home-owner-grant-scheme-is-in-doubt-1047782/

[v] https://www.vic.gov.au/homesvic-shared-equity-initiative

[vi] https://www.housing.wa.gov.au/sharedstart/Pages/default.aspx

[vii] https://treasury.gov.au/coronavirus/homebuilder

[viii] https://www.aihw.gov.au/reports/australias-welfare/home-ownership-and-housing-tenure

[ix] https://aip.asn.au/wp-content/uploads/2021/02/Superannuation_and_Housing_21_02_13_V2.1.pdf

[x] *A History of Interest Rates, 4th Edition*, Homer and Sylla (Wiley, 2005)

[xi] https://www.abs.gov.au/statistics/economy/finance/lending-indicators/latest-release

[xii] https://treasury.gov.au/coronavirus/homebuilder

[xiii] https://www.alp.org.au/policies/helping-more-australians-into-home-ownership

[xiv] https://www.qld.gov.au/housing/buying-owning-home/financial-help-concessions/qld-first-home-grant/apply-first-home-grant

[xv] https://www.apps09.revenue.nsw.gov.au/erevenue/calculators/fhba.php

[xvi] https://www.revenue.nsw.gov.au/grants-schemes/first-home-buyer

[xvii] https://www.sro.tas.gov.au/first-home-owner

[xviii] https://www.apps09.revenue.nsw.gov.au/erevenue/calculators/fhba.php

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[xxi] https://www.adelaidenow.com.au/news/opinion/samantha-maiden-prime-ministers-crack-at-alp-housing-scheme-reveals-he-is-getting-desperate/news-story/e70bfb6f342d42378f4d19a353391276

[xxii] https://tradingeconomics.com/australia/government-bond-yield

[xxiii] https://www.realestate.com.au/news/australians-are-holding-onto-their-homes-longer-than-ever-corelogic-data-shows/

[xxiv] https://budget.gov.au/2022-23/content/bp1/download/bp1_bs5.pdf

[xxv] https://www.rba.gov.au/media-releases/2022/mr-22-12.html

[xxvi] https://www.news.com.au/finance/real-estate/major-banks-forecast-that-housing-prices-will-drop-in-2023-but-interest-rate-rises-put-some-at-risk/news-story/062a1a8ed7bb2abe6eac2384e99d20d2

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[xxviii] https://www.commbank.com.au/digital/home-buying/calculator/home-loan-repayments