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EXECUTIVE SUMMARY

A new look at the channels from housing to employment decisions

Inquiry into housing policies, labour force participation and economic growth

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Paul McBride	Department of Social Services, Australian Government
Marty Robinson	Treasury, Australian Government
Iain Scott	Department of Social Services, Australian Government

Executive summary

Key points

The purpose of this study is to investigate the role of current housing assistance arrangements, housing wealth and mortgages in individuals' employment decisions. The study also explores whether bequests or parental cash transfers, which are typically financed (directly or indirectly) through housing wealth, lower work effort and participation in skills and training programs.

Key findings from the study indicate that:

- Housing assistance to private rental and public housing tenants has little effect on employment. For example, our modelling estimates suggest that even if Commonwealth Rent Assistance were to be removed the probability of continued employment would increase by only 0.3 percentage points, from 91.1 per cent to 91.4 per cent.
- Higher levels of housing wealth seem to help older 'inactive' owners (i.e. not in the labour force) regain employment, and help precariously employed younger home owners secure their employment.
- Rising levels of mortgage indebtedness appear to be extending working lives—these findings are consistent with AHURI research reported in Atalay, Barrett et al. (2016).
- For persons aged 45–54 (55–64) in 2001, mortgagors' odds of leaving the labour force is only 19 per cent (27%) of outright owners' odds of leaving the labour force (all else being equal).
- Longer working lives will help mitigate declining rates of employment and productivity slowdown due to population ageing. However, it comes at the expense of a higher investment and repayment risk burden in later life.
- Beneficiaries of parental cash transfers or bequests have better educational qualifications, and in particular are more likely to hold a bachelor's degree, than a control group of non-beneficiaries.
- Beneficiaries also have average bank deposit account balances that are more than double those of non-beneficiaries, and average net investment income is roughly one-third higher.
- The proportion of beneficiaries in the labour force is roughly the same as for non-beneficiaries, but a significantly higher proportion is self-employed.

Findings from the project will broaden the current evidence base to inform a policy reform agenda that features increasing employment participation rates in order to counter the labour market consequences of population ageing.

Key findings

Do different government transfer programs, and especially housing assistance, blunt the incentive to work and depress employment participation rates?

There are two main housing assistance programs: Commonwealth Rent Assistance (CRA) and public housing. Our modelling suggests that CRA has a negligible influence on the future employment outcomes of those already employed. Its removal is estimated to increase the probability of continued employment by only 0.3 percentage points, from 91.1 per cent to 91.4 per cent. Hence, CRA is only a marginal influence on the incentive to work. Even among unemployed adults receiving income support payments such as Newstart or Youth allowance, CRA has little influence on the chances of a successful transition back into employment. An important reason is a judicious CRA design feature that restricts eligibility to those in receipt of an income support payment, but only withdraws CRA once eligibility to the underlying income support payment is lost. Thus, Newstart (or Youth) allowance and CRA are never simultaneously withdrawn. Our modelling results suggest that blunt work incentives are not the main cause of this group of housing assistance recipients' low rates of employment participation.

Public housing tenants are a severely disadvantaged group who face multiple barriers to employment. Hence, reforms that reduce the burden of taxation on additional earnings, or lower taper rates in income support programmes will have only small effects on employment rates. An integrated approach that addresses barriers to employment for those in public housing (e.g. drug and alcohol abuse, mental health problems, skills deficiencies and so on) is likely to be a more effective approach to improving the employment outcomes of public housing tenants.

Home buyers are taking on larger mortgages (relative to household incomes) and repaying outstanding mortgage debt later in life. Is this going to delay age related declines in rates of employment?

Our empirical analysis as well as earlier AHURI research reported in Atalay, Barrett et al. (2016), confirms a finding that higher mortgage indebtedness is linked with stronger labour market ties. For instance, we find that for mortgage holders aged 45–54 (55–64) in 2001, the odds of leaving the labour force is only 19 per cent (27%) of outright owners' odds of leaving the labour force (all else being equal). Growing indebtedness among Australian home owners approaching retirement appears to be associated with longer working lives. These higher levels of mortgage debt may be in part the product of higher real house prices that prompt home buyers to take on high levels of debt in order to finance their preferred housing choices. An alternative explanation is that Australians now expect to live longer lives, plan to work beyond pensionable age and are therefore comfortable with decisions to pay off mortgages later in life. Whatever the explanation, the result is the same: longer working lives and a more gradual decline in rates of labour force participation as Australians age. This will help the Australian economy mitigate declining rates of employment and productivity slowdown due to population ageing.

There have been fears that growing indebtedness among Australians in midlife reflects a deliberate plan to 'de facto' access superannuation balances before reaching preservation age (when access to superannuation balances becomes possible if you have retired). This would of course undermine an important goal of retirement incomes policy—that is, alleviating pressure on government age pensions. However, the evidence that we present here suggests that those carrying mortgage debt as they approach retirement age have much stronger employment ties and are working later in life than their outright-owner counterparts. These longer working lives imply accumulation of larger superannuation balances, as well as a later drawdown of those balances.

Housing remains the most important component of most households' wealth portfolio. Intergenerational transfers are an important feature of contemporary family life and housing wealth will be an important direct or indirect funding source for these transfers. Are these transfers helping to shape the education and employment outcomes of beneficiaries?

To estimate the effects of intergenerational transfers on education and employment outcomes we use a research method that mimics clinical trials. Every person that has received an inheritance or cash transfer from their parents is matched to a control person who has not been a beneficiary, but is judged to be similarly likely to have received one given their personal characteristics.

There are three key findings;

1. Beneficiaries have better educational qualifications, and in particular are more likely to hold a bachelor's degree.
2. Beneficiaries' average bank deposit account balances are more than double those of our control group, and average net investment income is roughly one-third higher.
3. The proportion of beneficiaries in the labour force is roughly the same as for non-beneficiaries, but a significantly higher proportion are self-employed.

The recipients of transfers therefore have more financial assets that can act as a buffer to meet income shocks, and collateral to relax borrowing constraints. In view of these differences, beneficiaries might take more risks, and are in a better position to borrow, whether to take advantage of educational opportunities or to finance business start-ups. The evidence confirms expectations about education and business start-ups, but whether this is because beneficiaries are less risk averse or better able to relax borrowing constraints awaits further research. It would therefore seem that the intergenerational circulation of housing wealth helps recipients achieve their educational goals, as well as establish business ventures that might not otherwise 'get off the ground'.

Offsetting the above positives are negative implications for equality (see also Barrett, Cigdem et al. 2015b). The evidence shows that children from affluent socio-economic backgrounds are more likely to receive intergenerational transfers than those from a disadvantaged background. Intergenerational wealth transfers may help entrench and even exacerbate inequality in lifetime economic opportunities. If intergenerational transfers become increasingly important as a pillar supporting educational, housing and business start-up opportunities, policy-makers will need to heed the consequences for those children of less well-off parents who are bypassed by the intergenerational circulation of housing wealth.

Policy development options

There are a number of recent policy initiatives that aim to increase employment participation, and these typically fall into three types. The first focuses on delaying eligibility for non-work sources of retirement income, including the age pension and superannuation pay-outs. The second aims to incentivise workforce participation by lowering the tax on income earned through tax offsets. The third is a general tightening of eligibility criteria governing access to income support payments. Reforms to housing assistance programs have played a negligible role in policy-making around the issue of work incentives. The findings presented in this project are largely supportive of this neglect.

However, none of the above initiatives address the fact that a majority of older Australians have typically accumulated large reserves of housing wealth, encouraged by tax and means-test concessions that offer preferential treatment of the family home. They can increasingly draw down on this housing wealth without undergoing a costly application process, as a result of financial innovations that have turned housing wealth into an 'ATM' that borrowers can draw from as and when they choose (Ong, Jefferson et al. 2013; Smith and Searle 2010). This growing fungibility of housing wealth, combined with growing reserves of housing wealth, appears to play a role in influencing workers' decisions to either continue in or withdraw from the labour force as pensionable age approaches.

Our findings also suggest that some Australian home owners are dipping into their housing wealth in order to finance business initiatives. While these findings are subject to caveats, they are of potential importance as they could (if found to be robust) have significant economic spin-offs. Governments might wish to encourage this use of housing wealth by alerting home owners to the tax advantages of using their homes to launch business start-ups. Planning regulations that discourage the use of homes for business purposes might also deserve attention.

The housing wealth of older Australians is likely to affect the education and work career paths of their adult children. This is because parents may dip into (or bequeath) their housing wealth in order to assist children. Those anticipating transfers from their parents may factor this expectation into their education and employment decisions. We know little about how this intergenerational circulation of housing wealth is impacting young adults' working careers and education outcomes. The evidence presented in this report confirms expectations that intergenerational transfers help beneficiaries to 'get ahead', by being better able to complete a university education, while also more prepared to start business and self-employment ventures. Policy-makers might welcome these links and consider options that encourage parents to circulate their housing wealth between the generations. Encouraging financial institutions to launch small-business loans that parents can secure using their homes is one such option. While perhaps attractive as an option for the wealthy, it would be remiss to ignore those bypassed by the circulation of housing wealth between the generations. As intergenerational transfers become more important, they could become an increasingly significant cause of inequality of opportunity, and so this growing wealth divide will warrant attention from policy-makers.

Yet another housing-related development with potentially important implications for labour markets, and hence productivity, is that growing numbers of Australian households are taking on higher levels of mortgage debt (relative to household incomes) and paying down their mortgages later in life (Wood, Ong and Cigdem 2014). Our findings suggest that home owners are prepared to work longer in order to pay down their mortgages. While this appears to be good news as far as retirement incomes policy and employment participation rates is concerned, carrying debt later in life exposes older Australians to risks that seniors in earlier, largely debt-free, generations have not been accustomed to facing. An important hazard is ill health and disability, and it is one that is more likely to occur as we get older. A premature exit from the work force that is precipitated by unexpected bouts of ill health or disability can be disastrous for mortgagors at any stage in the life cycle, but especially so in later life. Governments might therefore consider options that could assist older mortgagors to hedge these risks. A requirement that mortgagors take out mortgage insurance once an age threshold is reached would be one such option; it anticipates an issue that will become more important as the Australian population ages.

The study

This study is one of five supporting projects that will inform a broader inquiry into the key channels through which housing policies might impact upon the economy. The focus of this study is to examine the implications of current housing assistance arrangements, housing wealth and mortgages on individuals' employment decisions. It seeks to broaden the current evidence base to inform a policy reform agenda that features raising employment participation rates in order to counter the labour market consequences of population ageing.

The key aims of the project can be summarised in the following four research questions.

1 Do different government transfer programs, and especially housing assistance, blunt the incentive to work? How do any such effects vary by age cohort, wage range, geographical location and individual/demographic characteristics?

2 What are the impacts, in terms of direction and magnitude, of Australia's tax and benefit system—particularly housing assistance—on employment participation decisions?

3 What role does housing wealth and mortgage debt play in shaping employment participation decisions at different stages of individuals' employment life cycles?

4 Do intergenerational transfers such as bequests lower work effort and participation in skills and training programs?

To undertake the above research inquiry, we rely on the Household, Income and Labour Dynamics in Australia (HILDA) Survey, focusing particularly on years 2001–10. HILDA has become a staple Australian longitudinal data source owing to its abundant reserve of household- and individual-level information covering a wide array of themes. Of key relevance to this research is information relating to individuals' labour market outcomes, demographic profiles, as well as their housing and superannuation wealth.

We employ a variety of quantitative techniques to tackle the main research questions. Random effects logit models and multinomial logit modelling techniques offer estimates of the extent to which interactions between tax provisions and income support programs programs discourage continued engagement in employment, or the engagement in employment of previously unwaged individuals, taking into account individuals' demographic and socio-economic characteristics, the geographical location in which they reside (Major Statistical Region), wealth and, importantly, their replacement rate (RR) variable, to capture effects on their incentive to work. The work incentive measures incorporate housing allowance parameters, thereby permitting simulations that provide estimates of the direct impact of housing allowances on employment participation. Information on housing equity, mortgage debt and superannuation wealth offer a measure of their respective roles in shaping individuals' labour supply decisions.

'Nest egg' and indebtedness effects are likely to be especially important in the later stages of labour market careers. Logit and multinomial model specifications are therefore modified to include interactions between age and wealth, as well as debt variables. However, we choose to explore their importance in more depth, by selecting a sample of employed persons over the age of 45 and estimating hazard models of the duration of their continued participation in the labour force. We are especially interested in comparing the employment trajectories of mortgagors and outright owners—there being an expectation that the former group's employment ties are stronger.

Finally, we investigate ideas around the links between intergenerational transfers, employment and training using a propensity score matching approach.[1] We empirically examine these possible links by designing a control group whose labour market behaviour can be contrasted with a 'treatment group' who have received a bequest or cash gift over the study time frame (2001–10).

[1] See Barrett, Cigdem et al. (2015b), where this technique is explained and applied.

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