Cut immigration by half to improve housing affordability

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I’ve been having this recurrent nightmare. I’m trapped alone in the budget media lockup and left clutching a booklet; it’s the only thing I have to read. It’s about housing affordability and it has lots of charts and boxes.

There are little stories about Jim and Jenny, Mick and Nick, and how the government’s budget initiatives on housing affordability are going to help them. It is pitched to someone aged about 12. I guess because the previous attempt to improve rental affordability worked out so well (who can forget the massive rorting in the National Rental Affordability Scheme?) the Coalition government thinks it can intervene in the rental market and make things even better.

Important as renters are, the main game is housing affordability for owner occupiers. This is where the politics are hurting the government, but it’s not clear that the Turnbull administration will really have anything to offer up in the budget. Just take a look at the figures. In the mid-1960s, 73 per cent of Australians owned or were purchasing their own homes. The present figure is about 67 per cent. For younger Australians, the fall in home ownership has been particularly steep. During the past 20 years, home ownership among those aged 25 to 34 has fallen from 39 per cent to 29 per cent, and for those aged 35 to 44 the drop in ownership has been from 63 per cent to 52 per cent.

There is conjecture that a much higher proportion of Australians will never own their own home, which in turn has implications for retirement incomes policy. The strongest correlate of poverty in old age is being in rental accommodation.

Mind you, the policy challenges don’t simply relate to the failure of first-home buyers to get into the market but also to the economic risks that the hot residential real estate markets in Sydney and Melbourne — the largest markets by far — will develop into a bubble that eventually will pop.

In other words, the government needs to set out a medium-term plan to improve housing affordability to boost the rate of home ownership but also deal with the short-term problem of runaway property prices, escalating household debt and the potential threat to the stability of the financial system.

One obvious step is to cut the annual permanent migration intake — called the migration program, which includes skilled and family entrants — from 190,000 to less than 100,000. This would take out a significant element of new demand for housing.

Commentators will point out that the net overseas migration numbers peaked in 2010 (a peak associated with the end of the mining investment boom) and now stand at about 200,000.

But the NOM numbers include a variety of immigrants and emigrants including overseas students, backpackers, 457 visa holders as well as permanent entrants. The definition of migration is simply that the incoming traveller stays in Australia for 12 months or more within 16 months.

This definition does not correlate well with the demand for housing and is not a good indicator of the pressures on the housing market. By contrast, the numbers securing permanent entry correlate more accurately, and this is the number that must be adjusted. The fact 70 per cent of permanent migrants head for Sydney or Melbourne reinforces this point.

Do I expect the government to restrict the numbers in the migration program? Given various comments made by senior members of the government, including the completely erroneous statement by Scott Morrison that we can’t restrict immigration because of the ageing of the population, the answer is probably not.

Mind you, the fact Assistant Immigration Minister Alex Hawke lamely advised that new migrants might consider living in regional areas suggests that the government does understand that rapid population growth (which is principally being spurred by immigration) is undermining housing affordability.

So what else has the government got up its sleeve? Not much would have to be the answer. Moreover, it is pretty clear that the blistering state of the housing markets in Melbourne and Sydney has a lot to do with ill-considered policies that the government itself has introduced.

By restricting the benefits of superannuation as a means of funding a comfortable retirement, many older people are turning to negatively geared housing investments as a means of supplementing their retirement incomes.

The changes to the asset test attached to the Age Pension also have created an incentive for people to stay in their (exempt) houses or even to upgrade. The effect is to remove some stock from the housing market that otherwise might be available.

There is also the overlay of Labor’s proposed policy to scrap negative gearing for all existing residential real estate as well as halve the capital gains tax discount from 50 per cent to 25 per cent, all on a grandfathered basis.

These potential changes are creating an incentive for people to lock in the benefit of having tax-preferred assets within their portfolios. The debate now is whether the government should pre-empt Labor by introducing less radical changes to negative gearing and capital gains tax to demonstrate that something is being done to address housing affordability, as well as deflate the housing bubble.

As the Treasurer correctly notes, if these two factors were really driving the housing market, we would expect to see bubble conditions across the country, which we don’t. (House prices are actually falling in Perth.) Moreover, these two arrangements have been a consistent feature of the regulations for some time.

Assuming that the government quite rightly leaves the negatively gearing provisions as they are — and don’t forget they need to protect renters — the question remains whether there will be an adjustment made to the capital gains tax.

One of the points made about this tax is that the 50 per cent discount is an allowance for inflation. Because inflation is now low, the argument is that the discount should be reduced.

In point of fact, the real rationale for the discount is to introduce an element of smoothing to offset the punitive impact of bringing a capital gain to book in one year (for an asset held over several) and taxed at marginal income tax rates. Note also that Australia’s capital gains tax is high by international standards.

By all means, the government could reduce the capital gains tax discount from 50 per cent to 40 per cent, say, but this would be on a grandfathered basis. Whether this would have any noticeable impact on the housing market is debatable — and it would have a broader chilling impact on investment that would be economically undesirable.

In the context of interest rates that have been too low for too long, inadequate prudential regulation, unsustainably high population growth and barriers to new housing (and related infrastructure), the best the federal government will be able to do to address the housing affordability crisis is to issue feeble booklets.