

Box B: Inflation, Interest Rates and Household Debt

The structural decline in inflation in Australia during the 1990s has allowed a major decline in interest rates. The fall in interest rates for home borrowers has been particularly marked, due to the additional effect of increased competition in the housing loan market. As a result, housing loan rates are now well below their low points reached in the early 1990s, when the economy was much weaker than at present, and are at levels last seen in the late 1960s and early 1970s.

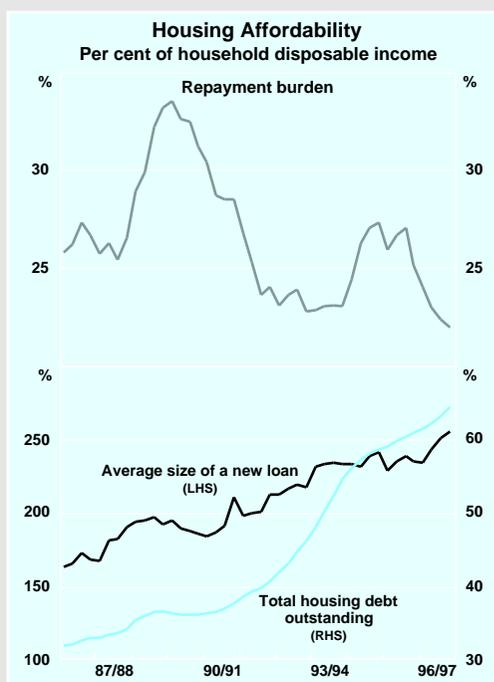
Quite important implications have flowed from this structural change. The first is that the 'affordability' of housing has increased considerably. Servicing costs on a standard variable-rate loan relative to average household disposable income have fallen sharply, and are currently lower than at any time since housing loan rates were deregulated in the mid 1980s (Graph B1, upper panel). It would be possible to find periods prior to deregulation when the servicing costs for the standard loan were lower than at present, but that is not a relevant comparison since loans were much less widely available (at least from banks) and borrowers often needed to take out more than one loan in order to fund a house purchase. Hence, it is safe to conclude that the accessibility of housing finance has increased markedly over the 1990s. It is likely that this change, other things equal, will prove to be of considerable advantage to low-income earners.

Households are tending, in many instances, to use the decline in interest costs to service much larger loans. The average size of new loans approved to owner occupiers has increased by 60 per cent since 1990, and is now about 2½ times average annual household income (Graph B1, lower

panel). It is also likely that more households have loans, though there are no timely data which measure that directly (and in fact, as of 1995/96, the majority of households were not paying off a housing loan, either owning their home outright or renting). The repayment burden would have fallen much further in the absence of this increase in loan size.¹ It is also likely that in some areas, the lower interest rates and larger loans are serving to accommodate upward pressure on house prices, though that is not widespread at this stage (see main text).

These trends have lifted the levels of gross debt carried by the household sector considerably. For the purposes of making international comparisons, it is necessary to

Graph B1



1. Results in Graph B1 are derived using average household disposable income, which is the national accounts measure excluding imputed rent on owner-occupied dwellings divided by the number of households in Australia, taken from Census data.

add other personal loans and loans to unincorporated businesses. Data compiled on this basis are shown in Graph B2. Until recently, Australian households and unincorporated businesses carried relatively little debt compared with those in other developed countries. As of 1996, Australia was closer to the median for this group of countries. As such, the present level of debt is not a major concern, though its current rate of increase (of around 10 per cent) is unlikely to be sustainable indefinitely in an economy where growth of nominal incomes is of the order of 5–6 per cent. ❧

Graph B2

