

Not on struggle street yet, but mortgage stress risk is rising

Written by The Conversation

Newly released analysis from Roy Morgan reaffirms that it is the lowest-income households that face the highest mortgage stress. And, contrary to what many might expect, the worst stress is not in Sydney and Melbourne, where property prices have [hit record highs](#).

The Roy Morgan report estimates that 18.4% of Australian households are experiencing mortgage stress, a situation where over one-third of their income goes towards servicing a home loan.

Mortgage stress can lead to many complex social issues. It is considered one of the underlying causes of the Global Financial Crisis.

For many households affected by mortgage stress, defaulting is the last resort. Yet, as the mortgage-servicing pressure increases, so does mortgage risk.

Mortgage risk, the chance of a borrower defaulting, has increased to 83.2% for households earning under \$60,000 per year. It is, however, virtually non-existent for households earning more than \$150,000.

Income is more important than interest rates

The Roy Morgan report highlights the importance of income, more so than house prices and borrowing costs, to mortgage stress. In fact, interest rates would need to more than double to match the impact of a loss of income on housing stress.

The previous peak in mortgage stress was in 2008-09, a period of high interest rates and bubble-like price growth in Sydney and Melbourne.

This time around, record low interest rates appear on the surface to be counter-balancing the default rate. Yet this is tied to a stagnation in income levels.

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House prices and income levels moved in step until 2013. While house prices have continued to increase, household income levels have flattened since then, when the cash rate dropped to a historic low of 2.75%. The cash rate is now even lower at 1.50%, with [further cuts](#) forecast.

The troubling prediction from this is that mortgage stress among Australian households is set to remain high, despite the current low interest rates.

Widening inequality

As home ownership concentrates among wealthier households, this report also shows that higher-income households are more resilient to increases in interest rates. This means, too, that home ownership increasingly requires a dual income.

The owner-occupied home is often referred to as the [largest single asset that most households own](#). In countries like Australia and the USA, home ownership is promoted by government and linked to many aspects of [future wellbeing](#). However, as recent [HILDA analysis](#) shows, owner-occupied households are becoming far less common.

The “Great Australian Dream” is expected to apply to only a minority of households next decade. With those in the already most marginalised parts of society most affected by mortgage stress, a change in the structures that incentivise home ownership is required to minimise the growing inequality gap.

Pockets of pain

The limitation with national averages is that pockets of pain are brushed over. The report drills into state-by-state analysis and metro vs regional comparisons.

While the largest mortgages across the country, averaging over \$300,000, are in Sydney, mortgage stress is highest in Tasmania and South Australia.

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Mortgage stress in Tasmania and South Australia sits well above the national average, as do their [unemployment figures](#) , 6.5% and 6.9% respectively, against a national average of 5.7%. Households in regional areas are also facing more acute mortgage stress than their city counterparts.

The housing market underpins the Australian financial sector

Regulators aren't taking any chances. With nearly \$1 trillion in outstanding mortgage debt, double the pre-GFC level, the [2014 Financial Systems Inquiry](#) identified that mortgages are now a significant systemic risk. In a [recent speech](#) on the prudential regulator's outlook, APRA general manager Heidi Richards stated that "the housing market now underpins our financial sector".

APRA has been tightening the lending standards of the big banks. Effective from July 1, the big banks have been required to apply [higher “risk weightings”](#); to residential mortgages. These determine the amount of capital held against assets to limit the likelihood of insolvency.

The silver lining to this otherwise depressing analysis is that the risks to financial stability are relatively low. Home ownership concentrated amongst wealthier households actually means there is a high degree of aggregate resilience to changes in future interest rates and incomes.

However, the report's focus is on current incomes. To brace for a true housing market downturn, the key will be monitoring employment and income statistics – unemployment rates as well as hours.

Danika Wright does not work for, consult, own shares in or receive funding from any company or organization that would benefit from this article, and has disclosed no relevant affiliations beyond the academic appointment above.

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