Discussion of

INDIVIDUAL INVESTORS' HOUSING INCOME AND INTEREST RATES FLUCTUATIONS

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Quick Summary

- Q: Relationship between the level of interest rates and the share of individuals who own rental properties in Australia, 2002-2019.
- A: Declines in interest rates lead to a substantial increase in the share of landlords, in particular among middle-income retirement-age individuals.
  - As rates decline, retirees shift their portfolios from fixed income securities to rental properties.

They use tax filing data for their analysis.
They also complement their empirical analysis by surveying some of the investors.

The findings are important

Because of:

- the impact on homeownership rates
- the potential to increase the volatility of retirees' income (by exposing it to local economic shocks).

Comments and Questions

- Interest rate is only one component of credit conditions. The other component is availability of credit (banks' appetite to extend loans) and credit constraints (LTV, DTI, etc.).

  If credit conditions have also changed, the results may not be attributable to the change in interest rates only.
  - Does 'mortgage credit spread' capture this?
    - Not necessarily. We had relatively high mortgage credit spread in the US during the low interest rate period following the GFC.

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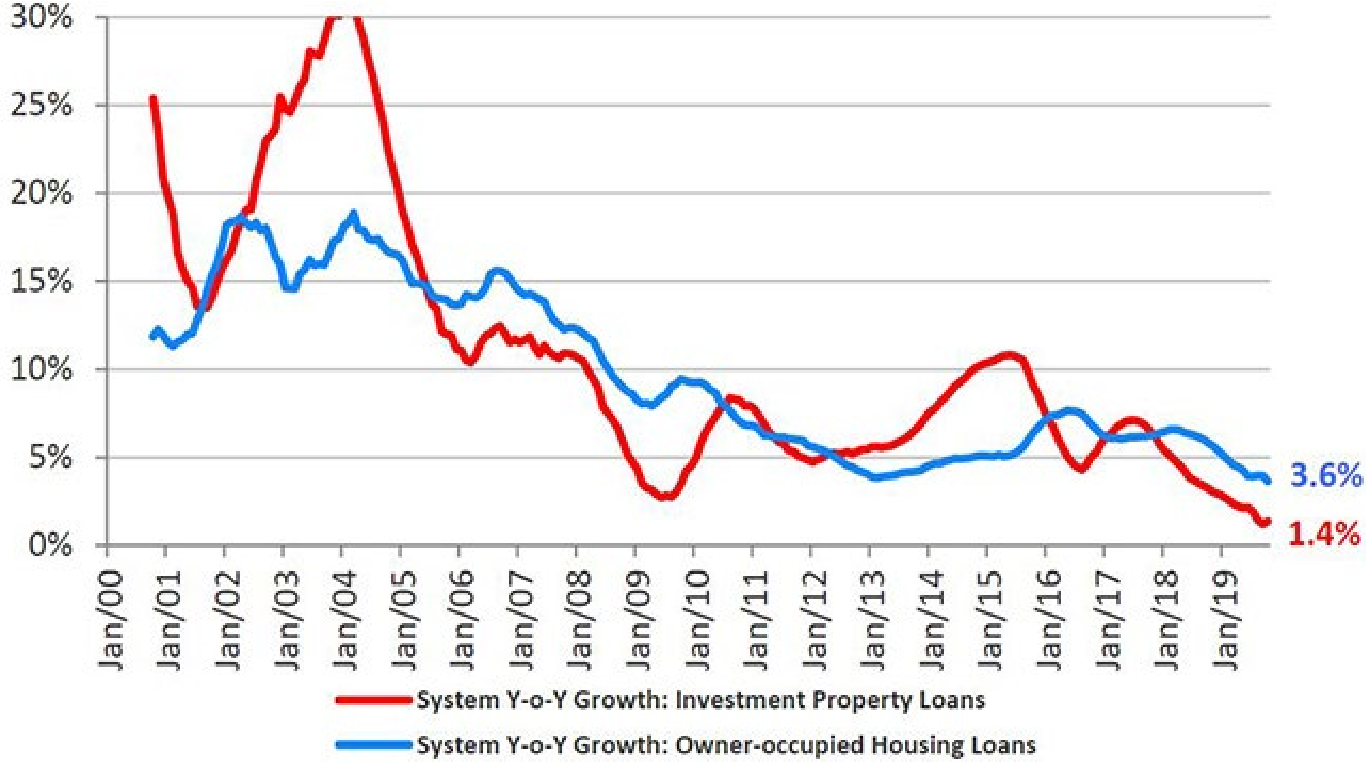
Indeed, mortgage credit growth slowed down in AU during that period

https://www.morganstanley.com.au/ideas/mortgage-growth-bottomed



Note: Seasonally adjusted data allowing for definitional change from July 2019 and restatements between OOL & IPL. Source: RBA, Morgan Stanley Research

reaching for income

- Claim: retirees are "reaching for income," not "reaching for yield":

$$FracBuyToLet_{i,t} = \gamma_{RY}\,(y_t \times RY_{2005,i}) + B_X X_{i,t} + a_t + a_i + e_{i,t},$$

Where $RY_{2005,i}$ is the average rental yield for postcode i between 2000 and 2005 (before the period of interest rate declines).

- This assumes that prices (and rents) have not reacted much to rate declines in the years following 2005?
- Would an investor in 2018 use the average rental yield in 2000-2005 period for decision making?

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Policy Relevance

Critical result: Lower rates have a negative impact on homeownership rate.

The reason: retirees purchase from homeowners; not a transfer of rental properties from one landlord group to another.

Compared to US where low rates led to higher ownership rate, until default crisis hit? (next slide)

https://fred.stlouisfed.org/series/RHORUSQ156N#0

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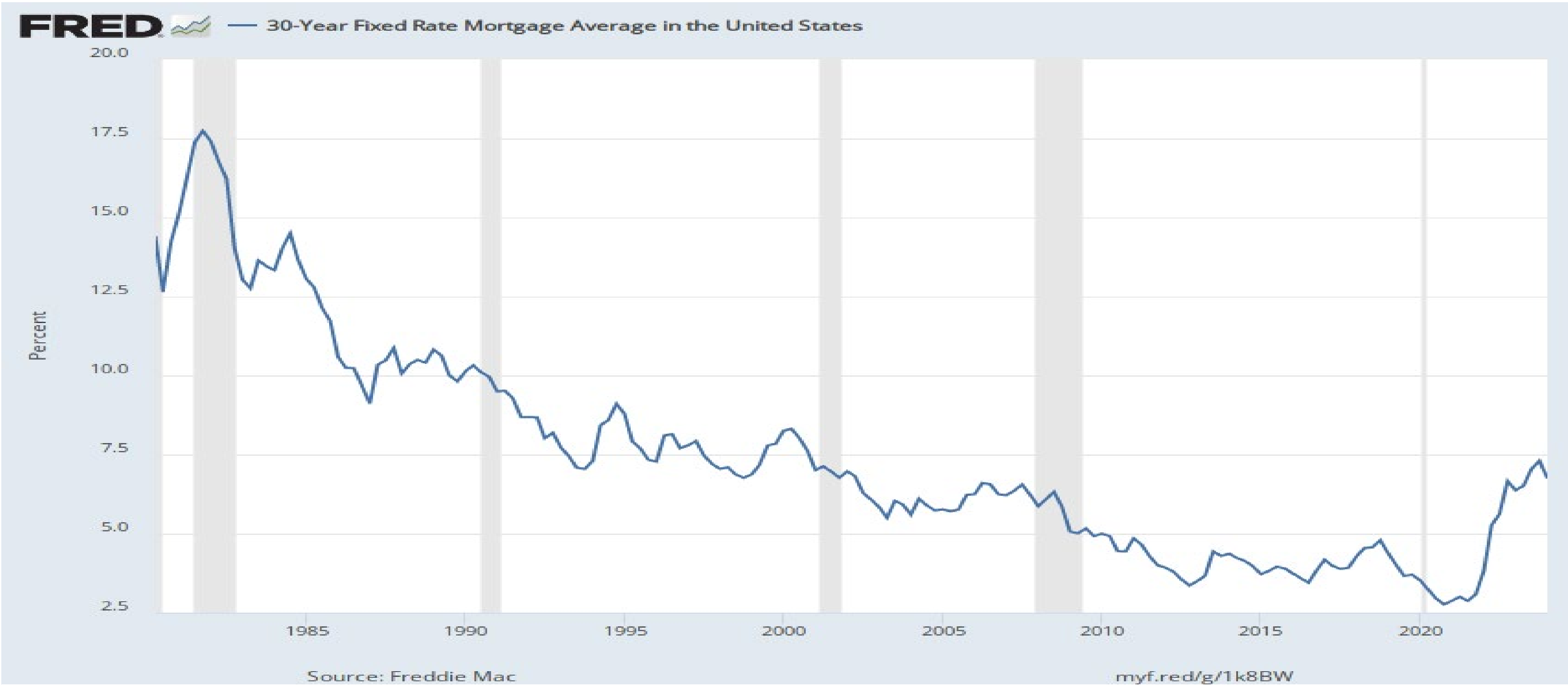
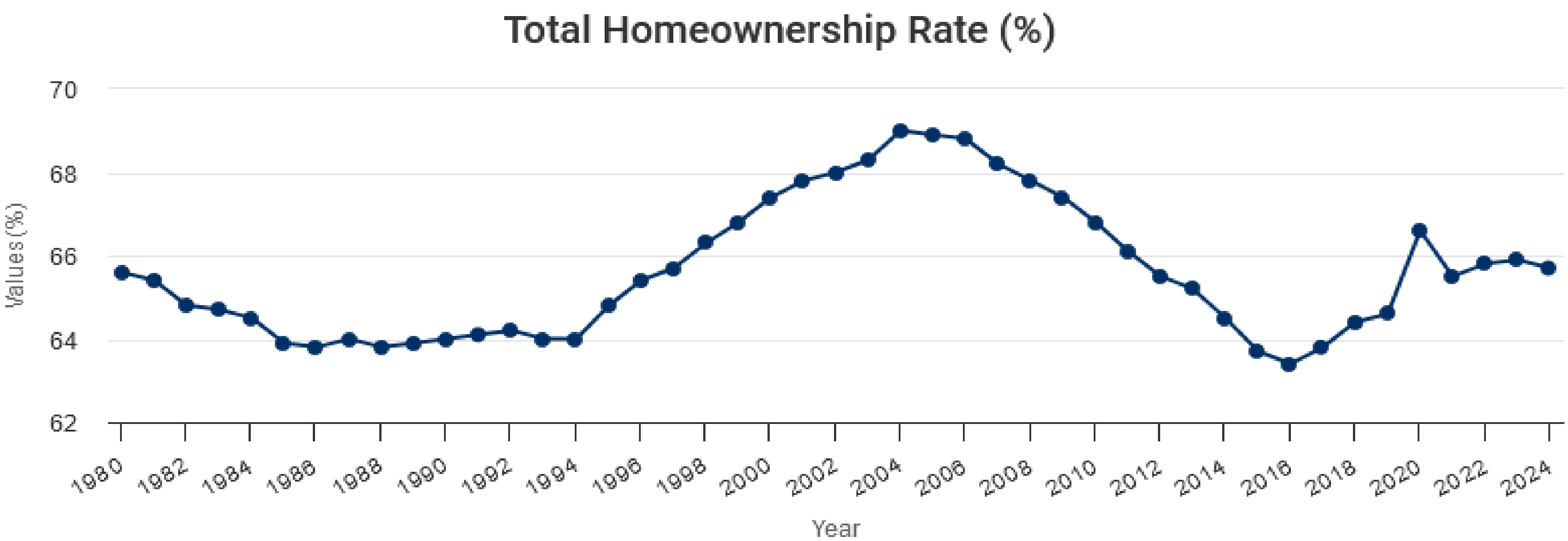


FRED
30-Year Fixed Rate Mortgage Average in the United States
Percent
20.0
17.5
15.0
12.5
10.0
7.5
5.0
2.5
1985
1990
1995
2000
2005
2010
2015
2020
Source: Freddie Mac
myf.red/g/1k8BW



Total Homeownership Rate (%)
Values (%)
70
68
66
64
62
1980
1982
1984
1986
1988
1990
1992
1994
1996
1998
2000
2002
2004
2006
2008
2010
2012
2014
2016
2018
2020
2022
2024
Year

Why did the homeownership rate in AU decline?

This is as important, if not more important, question than why retirees buy rental properties when rates go down.

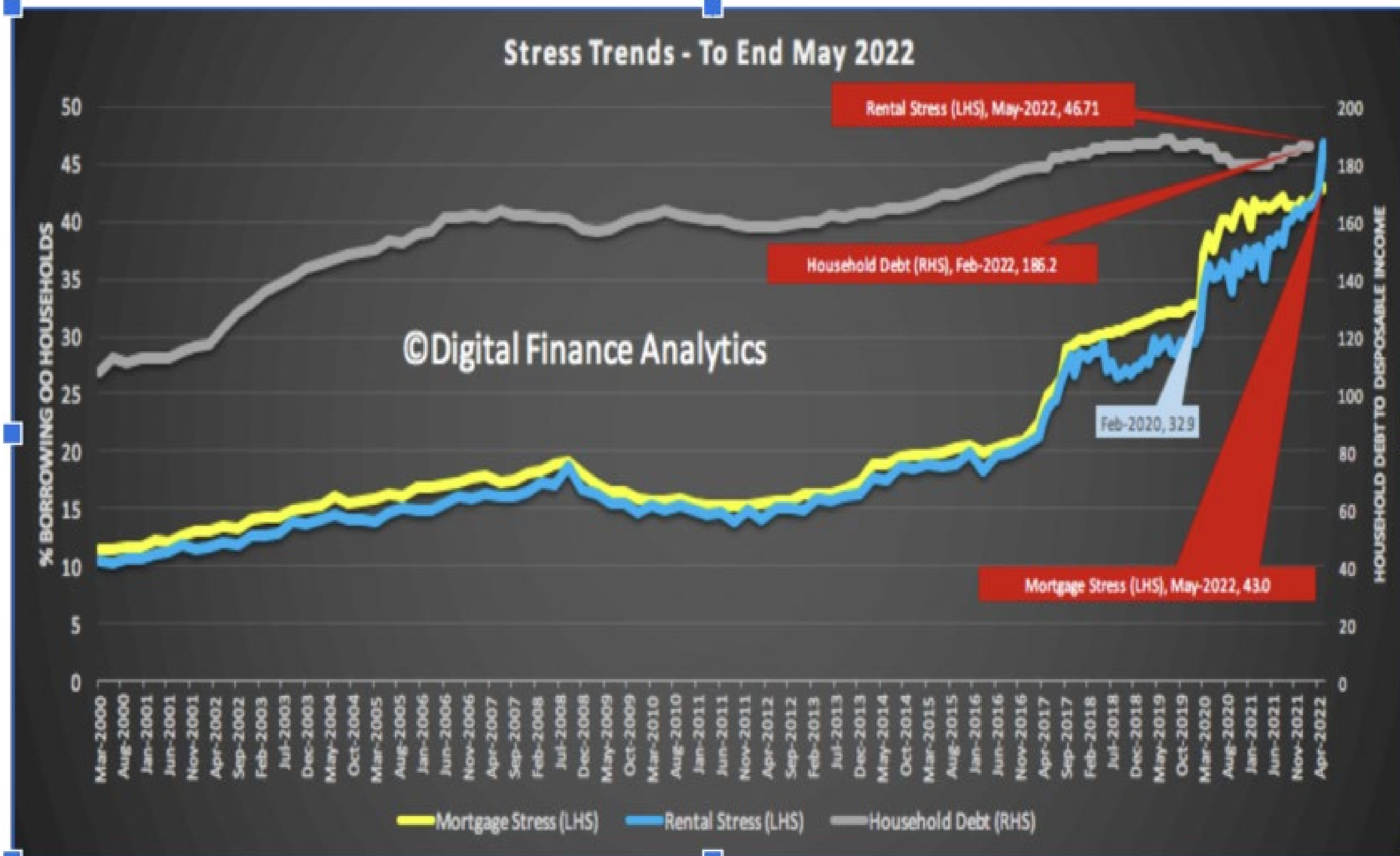
a. Higher home prices due to additional demand from investors (retirees and non-retirees) more than offsetting lower mortgage rates, hence making it less affordable to own?

and/or

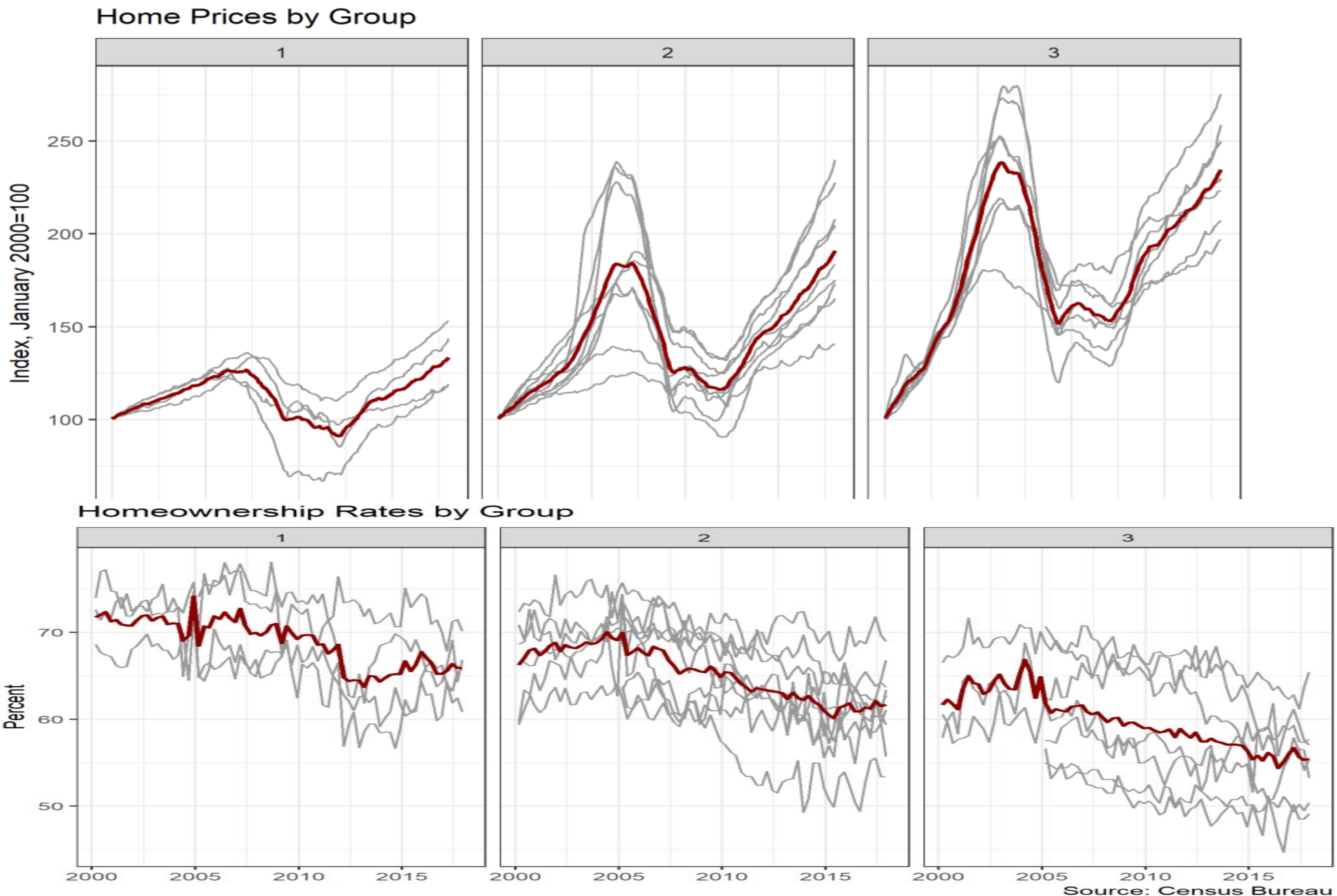
b. Lower rents due to additional supply of rental units by investors making it more attractive to rent?

Mortgage stress rose faster than rental stress in AU (due to higher prices?)

https://eliteagent.com/homeowners-and-renters-facing-record-levels-of-financial-stress/

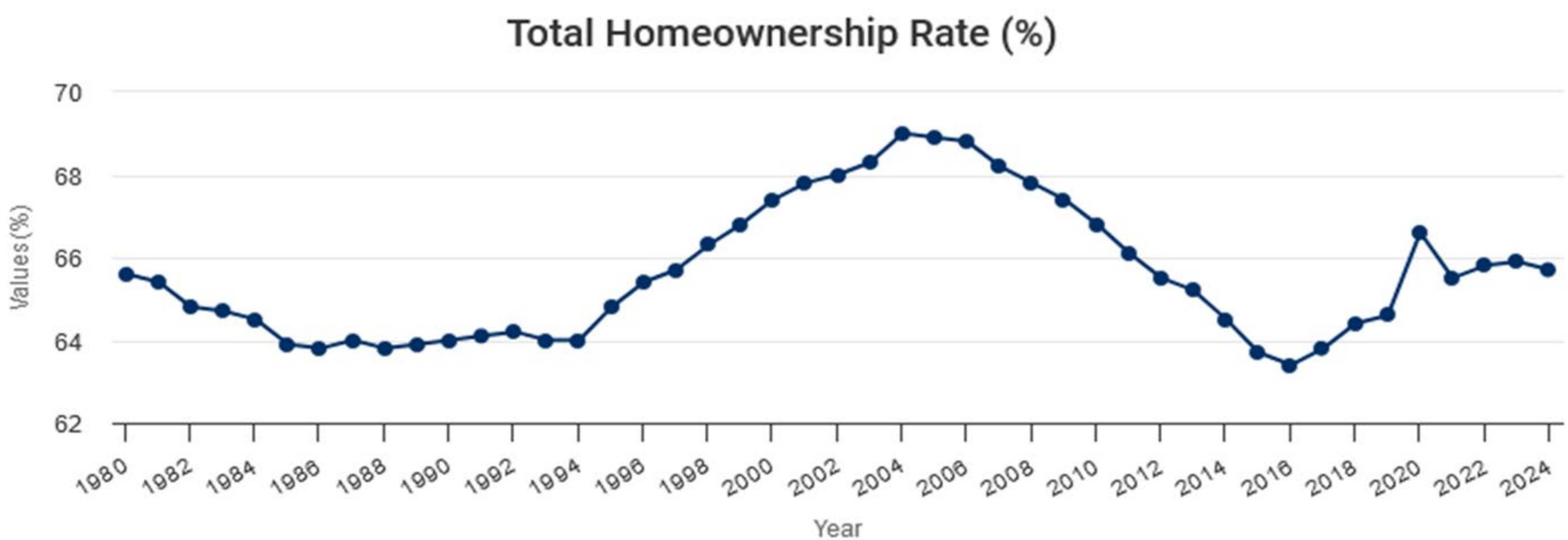


HOUSE PRICES AND OWNERSHIP RATES ACROSS MSAs in the USA
(Garriga, Gete and Hedlund, 2024)

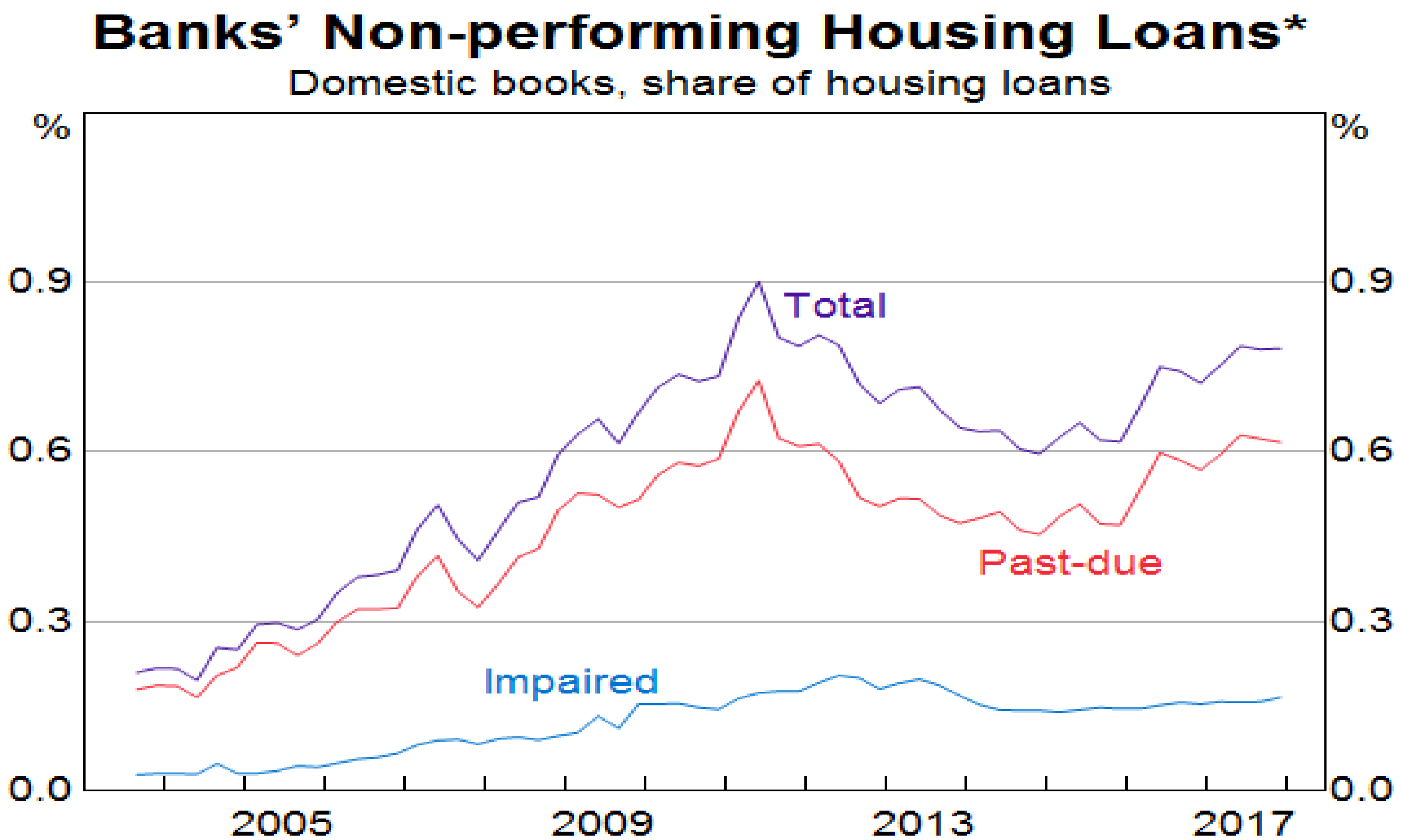


Why did the homeownership rate decline: 2009-2014?

- "we find that…most of this decline has taken place between 2009 and 2014.."
- This lines up with the decline in homeownership rate in the US during that time period.
- The driving force in the US was massive defaults that forced many homeowners out of their homes. Not a factor in AU?



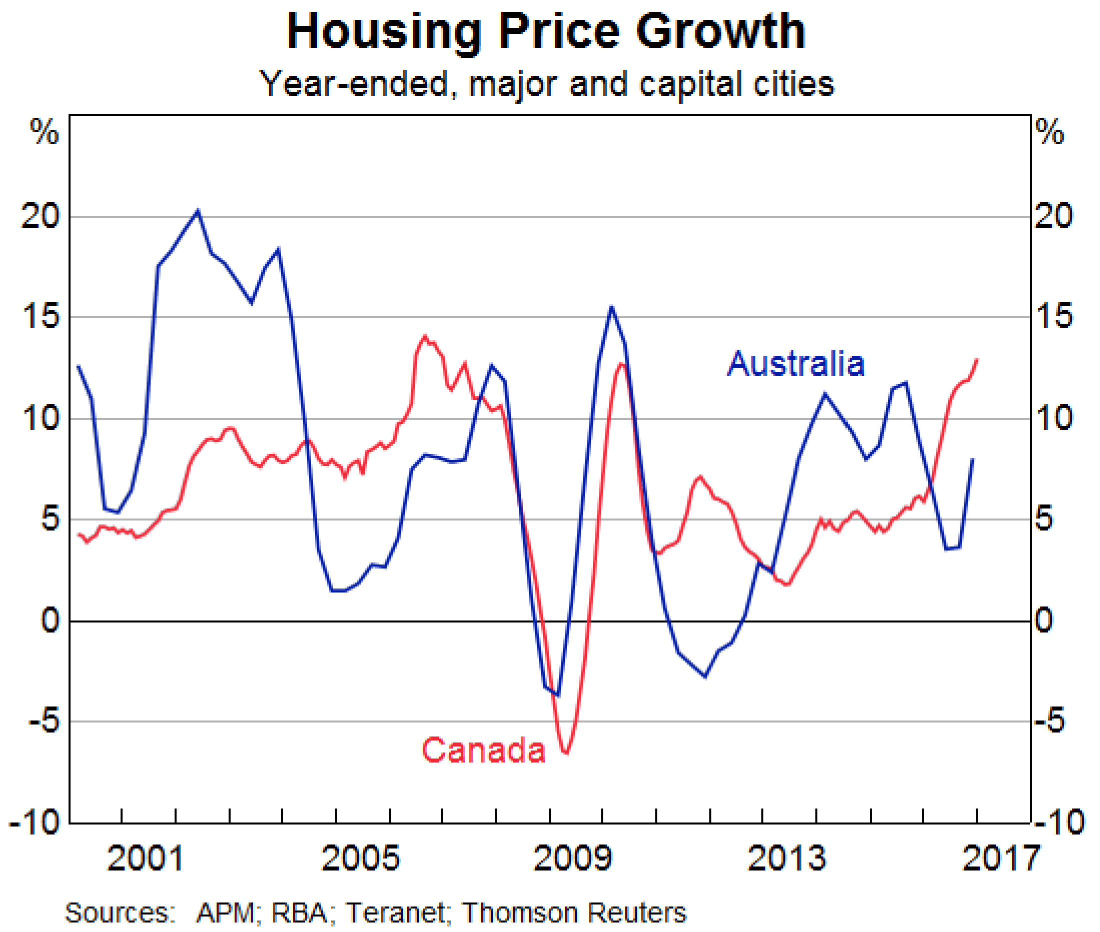
Default rates in AU went up as well, but nothing like in the US



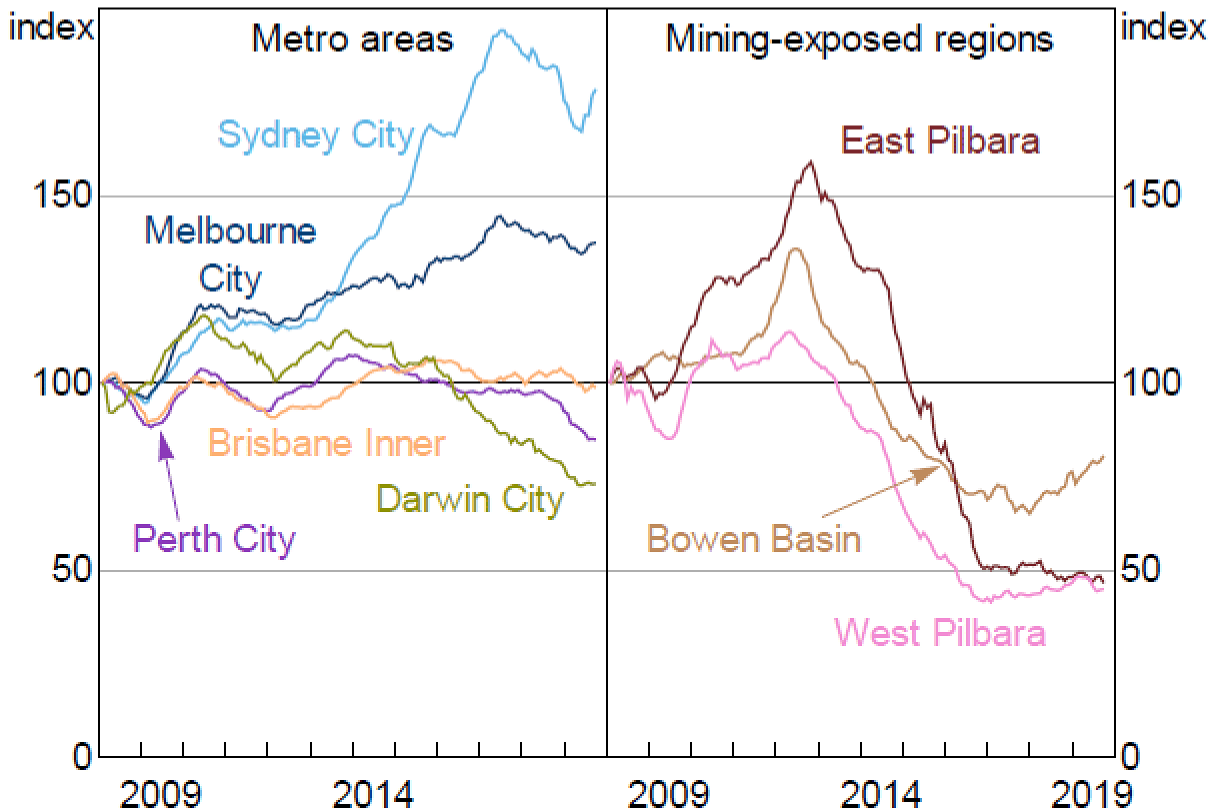
* Past-due loans are 90+ days in arrears and well secured; impaired loans are in arrears or otherwise doubtful and not well secured

Sources: APRA; RBA

and house prices declined

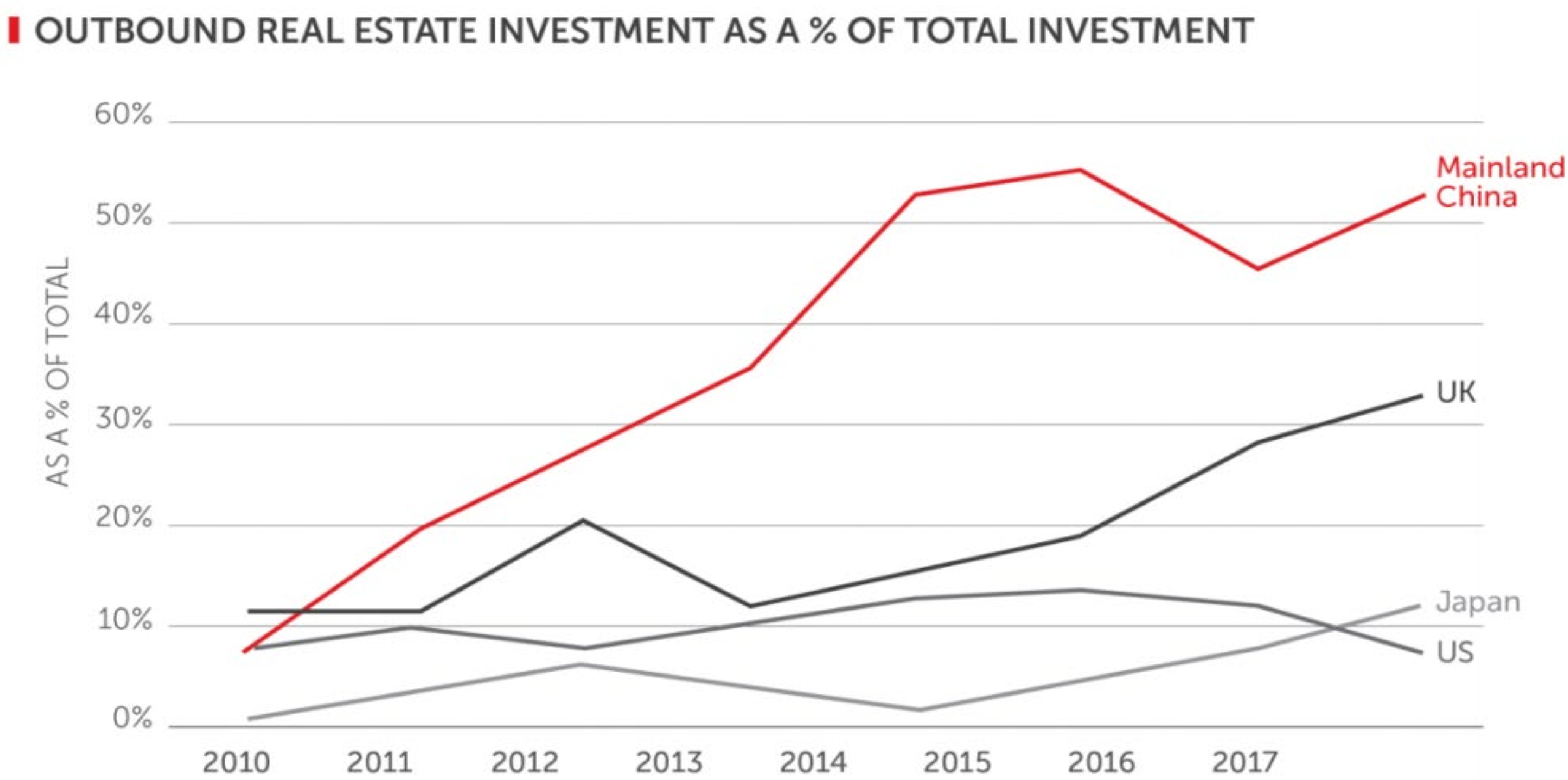


But not all cities are the same.
compare different cities with different default rates?



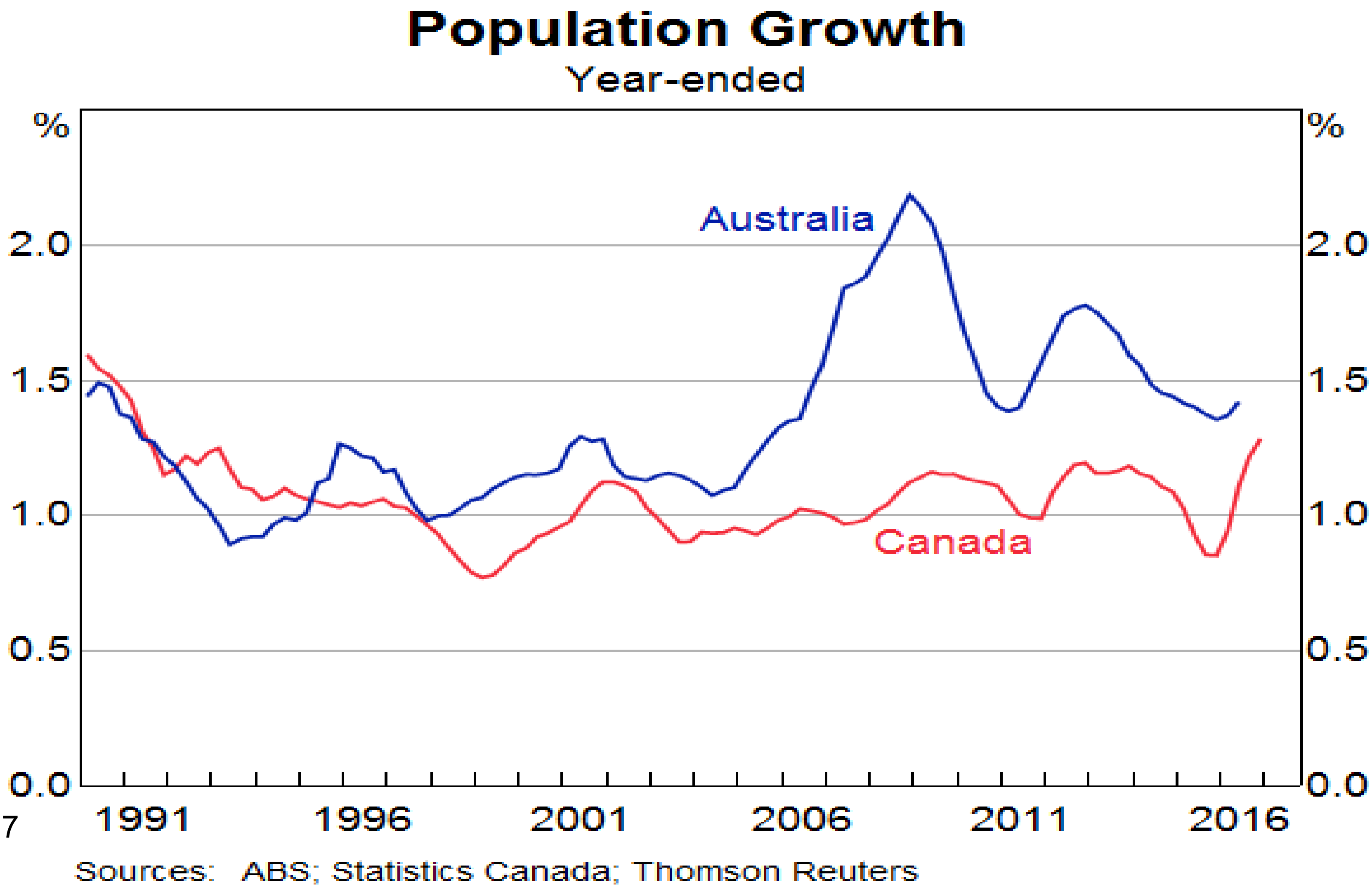
 Selected Regional Housing Price Indices
https://www.rba.gov.au/publications/rdp/2020/2020-03/full.html

Foreign Buyers in AU Property Market; what if they are mostly retirement age?



Or because of the spike in population growth (assuming it was not anticipated by builders)?

Is this due to immigration – diff than what population variable captures?

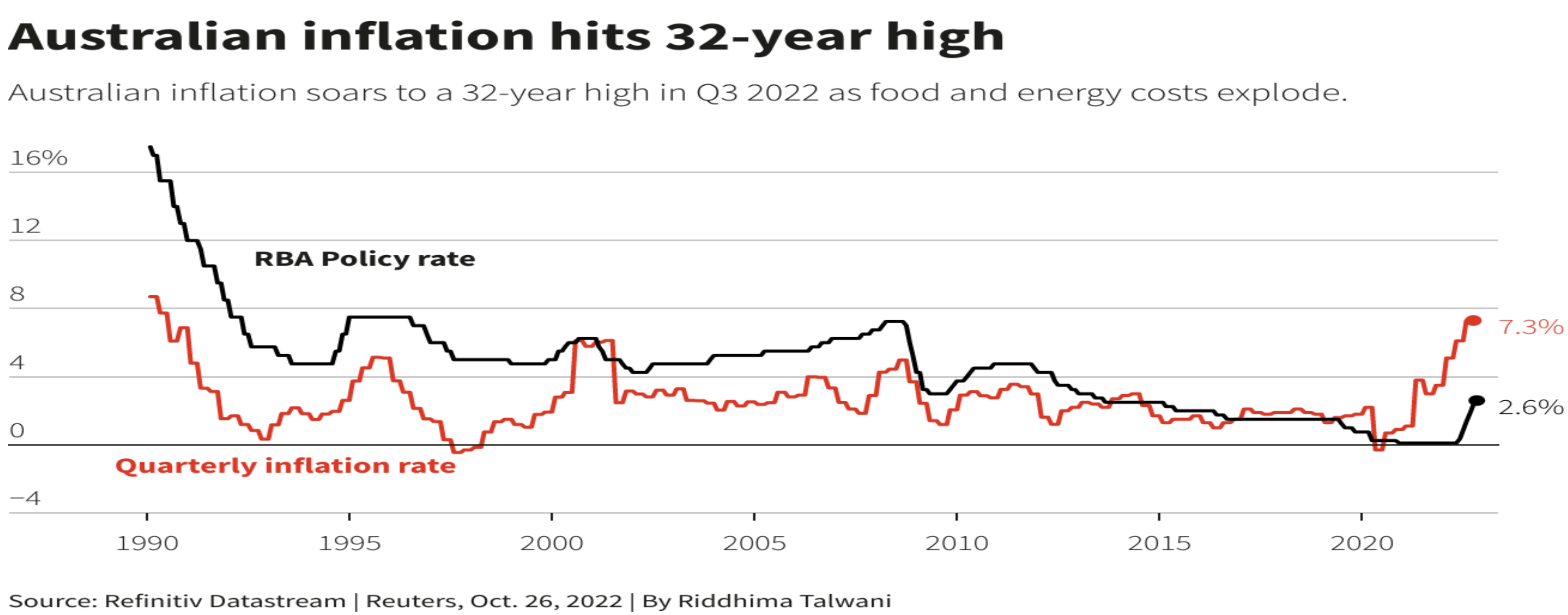


Inflation / inflation expectations?

MALMENDIER and WELLSJO, “Rent or Buy? Inflation Experiences and Homeownership within and across Countries,” JF, forthcoming.

Finding: Past inflation experiences strongly predict homeownership within and across countries.

Older generation / retirees definitely had more experiences with inflation!



Retirees are more likely to earn positive income?

“90% of retirement-age individuals earn positive income after interest and capex vs 70% for landlords in the youngest age group. Thus, retirement age landlords are indeed more likely to extract income from their properties.”

Total expected return (Rental yield + appreciation rate) should be comparable across age groups and locations;

older/retiree investors prefer properties/locations with higher rental yield and lower appreciation rate.

The survey response supports this argument.

Why?

Areas with high rates of retirees are low growth areas, and individual landlords typically prefer to buy rental properties close to where they live?

Is the driving force the location choice, not the high rental yield choice?

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Or, given location choice, is it because of less leverage by retirees?

"Approximately 50% of retirement-age landlords have no interest expenses, while for the median landlord in the middle-age and youngest group, interest expenses represent 50% of total expenses."

Couldn't this explain why a higher % of retirees earn positive income?

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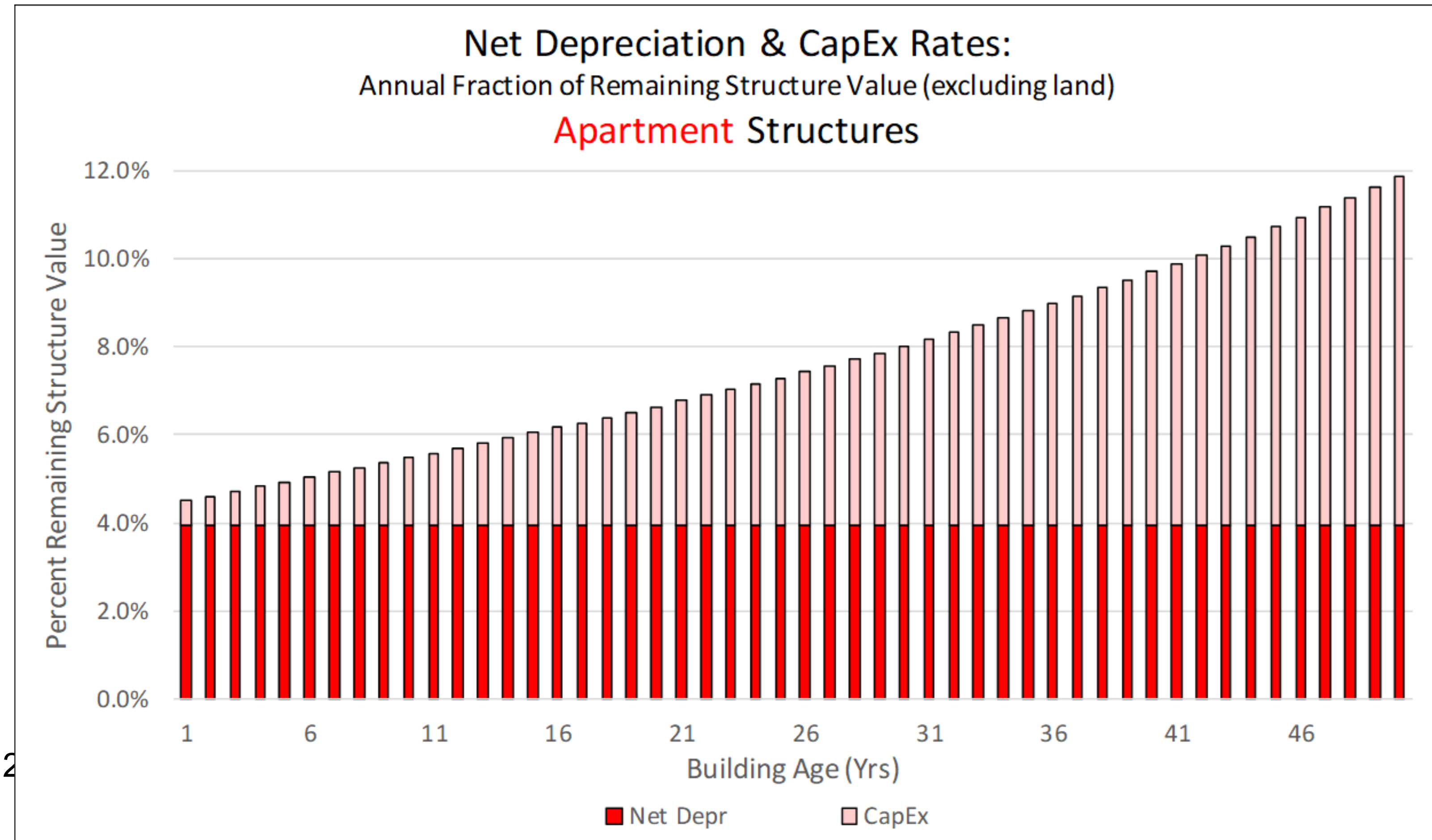
Or because they buy newer properties?

"retirement-age individuals have the lowest level of capital expenditures, with more than 60% of them reporting zero capex."

Capex is **endogenous** to the age of the property.
Thus, one needs to control for age.



A note on flippers vs buy-to-rent investors

“We use the listing data to identify buy-to-resell transactions (house flips), defined as properties re-listed for sale within 9-months of purchase.”

- **Suggestion:** As stated in a footnote, there could be other reasons for property owners to sell in a short period of time after the purchase (job changes, financial constraints, etc.). **One way to reduce this concern** is to control whether the property is vacant or occupied.

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Individual vs Investor buyers

A useful experiment would be to compare retirees' buy-to-rent decisions to investors' decisions.

(Allen, Rutherford, Rutherford and Yavas; JREFE 2018, JREFE 2023, Mills, Molloy and Zarutskie, REE 2022; Lambie-Hanson, Li and M. Slonkosky, REE 2022)

Did retirees purchase more relative to institutional / non-retiree investors during this declining interest rate period? Or was everyone buying more at the same rate?

Retirement-age landlords have little leverage

→ Lower rates must make buy-to-rent investments more attractive for institutional investors (or non-retiree individual investors) relative to retirees.

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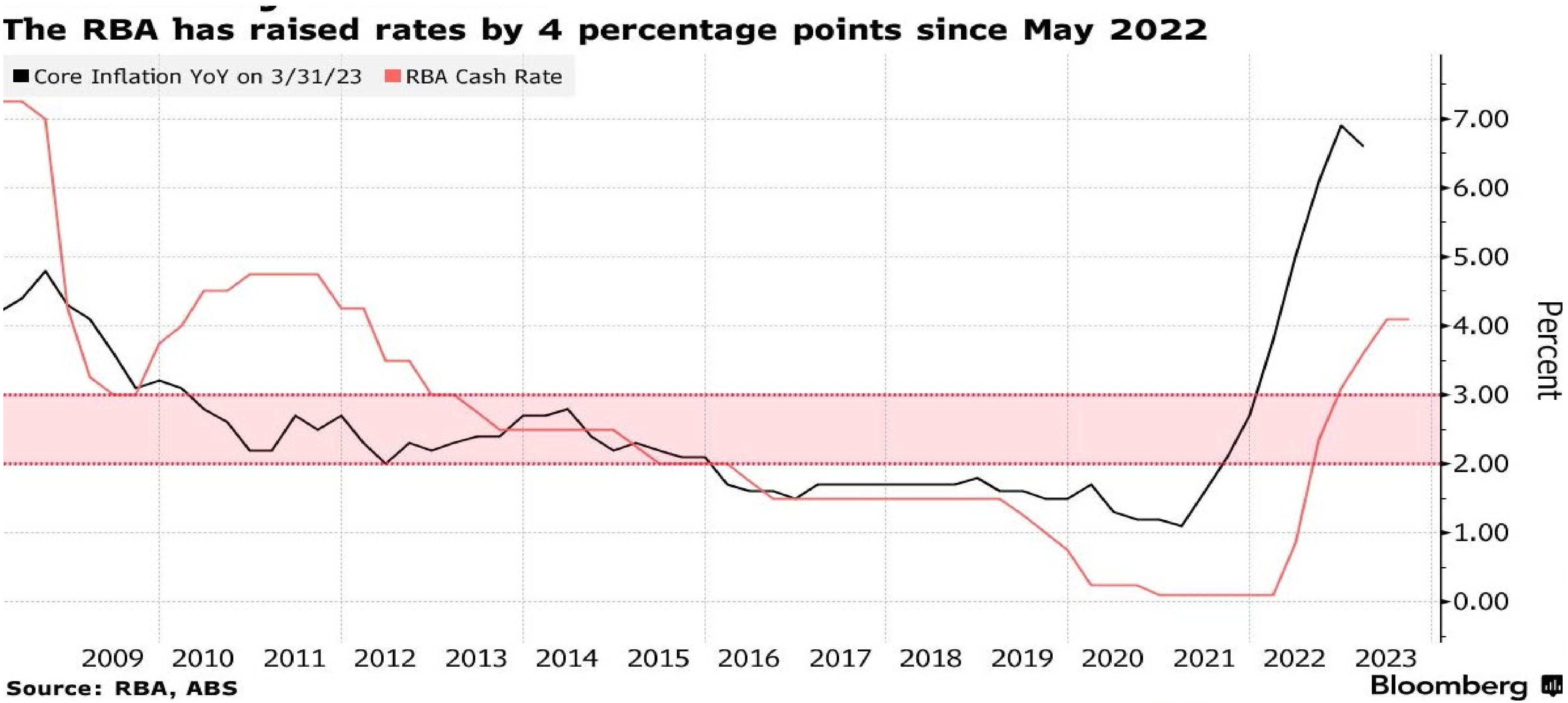
More importantly….

- Any policy implications to further motivate the paper?
  - What is the impact on rents?
  - What is the impact on affordability?

Is the effect **symmetric**?

- If rates go up, do we expect the homeownership rate to go up at the same rate? Or is there significant inertia?



Temporary?

- As interest rates decline, property values go up, and this eventually reduces the incentives for investors to switch from bonds to rental properties, unless rents go up as well.
  This brings up the following Qs:
  - Are you capturing a transition period effect, rather than a long-term effect?

LT Implications?

- Is this driven by the fact that we have aging population; retirees making up a bigger % of the population (rather than lower rates)?
  - The paper refers to the Appendix to claim that this is not so, but the graph in the appendix simply plots the ***correlation*** between Change in Fraction of 60+ yrs old and Change in Fraction of Landlords.

- What are the LR implications as retirees make up a bigger and bigger % of the population: Lower and lower homeownership rate?

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Conclusion

The findings and potential implications of this study are important for policy makers.

Expansionary policies by the Fed and other central banks have been accused of worsening income and wealth distribution.

This paper shows that home homeownership is one channel through which monetary policy might be affecting income and wealth distribution…