12 January 2018

The Hon Michael Sukkar MP
Assistant Minister to the Treasurer
PO Box 6022
House of Representatives
Parliament House
Canberra ACT 2600

RE: 2018-19 PRE-BUDGET SUBMISSION

Dear Mr Sukkar,

I have prepared this submission in response your invitation for public submissions with regard to the 2018-19 Commonwealth Budget.

This submission is prepared based on three areas I am actively involved with.

Firstly, one of my businesses, The Wealth Navigator (https://www.thewealthnavigator.com.au/) which is focused on helping ordinary Australians improve the health of their wealth so they can get off the treadmill of working till they drop.

Secondly, I have operated as a Virtual Chief Financial Officer (CFO) for many small and medium businesses including start-ups over the past 20 years.

Thirdly, I am the volunteer chairman of a Sydney based charity, Independent Living Villages (http://independentlivingvillages.org.au/) which builds homes for people with significant functional impairment and/or very high support needs because of their disability.

So this submission is focused on what the Federal Government can do towards:

- helping people improve their retirement outcomes;
- providing affordable housing; and,
- ease some of the administrative burden faced by small businesses.

Each of my submissions are detailed in Appendix 1 attached. In summary they are:

1. The $450 monthly income threshold on Superannuation Guarantee contributions should be removed as long as the ability for superannuation funds to charge fixed fees like administration and exit fees are also removed.

2. The definition of income on which Superannuation Guarantee contributions are calculated needs to be simplified. It would be far simpler that any payment made to the employee which is subject to pay as you go income tax is included in the income to determine how much superannuation guarantee contributions are to be made. Irrespective of what it was.

3. The superannuation guarantee contribution rate to be increased to 12% sooner than currently legislated. Ideally it should be increased closer to the 15% for considered when the framework for the compulsory superannuation system was put in place.

4. Negative gearing is not the real cause of housing affordability issues in Sydney and Melbourne. From my analysis, it is the focus of governments and business on the two metropolitan areas of Sydney and Melbourne which is driving jobs growth (and therefore demand for housing) in those two cities. So to reduce demand for housing in the big cities of Australia, the government should increase focus on job creation in regional and rural Australia.

5. If the government is concerned that negative gearing (whether for property, shares or other investments) is favouring the wealthy, then the government should consider the example of the USA's passive activity loss rules. These rules allow negative gearing in selected circumstances and limit the access to negative gearing by high income earners.

6. If the Government is concerned that capital gains tax discount is favouring the wealthy, then rather than reducing the discount for everybody, use a sliding scale based on the period the asset was owned.

7. There are many landlords who would offer below market rents for key workers like teachers, police persons, health workers etc. But under the current tax laws, these landlords may be punished by not being able to 100% deduct their costs. This could be avoided by allowing landlords who offer properties at below market rent to appropriately qualified tenants the right to claim 100% of their costs.

8. There is no currently no real incentive to encourage the construction of new affordable housing. The government could take the lessons learnt from the NRAS scheme and develop a new and better incentive possibly tied to the amount of GST paid on the property. An example of such scheme is in Appendix 1.

9. Currently there is a large incentive for couples to income split to reduce tax. In order to eliminate this, the government should consider developing a tax system that taxes couples as one tax unit.

10. Currently the pension means test rewards spending, not saving. A high income earner can spend all their money and get the same pension as a low income worker who never had the chance to properly save for their retirement. We need a pension means test that rewards saving not spending. An example of such scheme is in Appendix 1.

As noted above, the detailed comments behind each submission above is included in Appendix 1.

If you or anyone else has a question about the submissions, please feel free to contact me by phone on 0412 227 052 or by email at wayne@thewealthnavigator.com.au

Yours Sincerely

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1.0 The $450 monthly income threshold on Superannuation Guarantee contributions

Given the way technology has changed how superannuation payments are made these days, there is no longer the same administrative burden for employers on superannuation payments for people earning below the $450 minimum monthly income threshold.

No longer is there a potential need for business to prepare a cheque to a superannuation fund for $20 for someone's quarterly super payment.

These days, most business will use electronic payments and it takes no more effort to make a $5,000 payment than an extra $20 payment.

What it does do however, is leave the business with the administrative burden for low income earners in determining who qualifies in each pay period for superannuation payments and who does not.

A simple example is someone who earns $100 a week. In some months there are 5 weekly pay runs and in those months the employee is entitled to superannuation. For the first 4 pay periods the employee is not yet entitled to any superannuation. In the last pay period they are now entitled to superannuation, but not 9.5% of $100, but 9.5% of $500.

How many business owners would get this correct?

To ensure that the employee gets the correct superannuation, it often relies on the business owner to manually check. And not all small business owners have either the appropriate systems, knowledge or time to check that the employee is getting the correct superannuation.

So today, the $450 minimum monthly income threshold is placing administrative burden on small business to ensure that the correct superannuation is paid. And as we often see in the media, lots of small businesses get this wrong.

So the simplest way to solve this issue is to remove the $450 monthly income threshold on Superannuation Guarantee contributions.

But, I would recommend that this change is not made unless one other change is made.

Currently a large number of superannuation funds charge fixed administration and exit fees irrespective of the fund balance. And for people with low superannuation balances these fees become very regressive.

As you can see in an opinion piece I published on 29 October 2017, (included in this submission as Appendix 2), these fees can be as much as 26% of the fund balance for low income earners. I have personally seen one of my own daughters superannuation accounts reduced to nothing from these fees, so in her case the fees equated to 100% of her superannuation.

Therefore, if you really want to also improve the retirement outcomes of low income workers as a result of this change, *you will need to remove the ability for superannuation funds to charge fixed fees like monthly administration and exit fees*.

2.0 Income on which Superannuation Guarantee contributions are calculated

Another issue small business face is the calculation of what income is included to determine how much superannuation guarantee contributions are to be made.

The definition of ordinary time earnings and how different businesses calculate this leads to confusion. Confusion for the employer and for the employee. I am a fully qualified chartered accountant and I always have to double check definitions when I review a new clients payroll systems and their superannuation payments.

And as we see on the television, there are a lot of businesses who get this wrong.

It would be far simpler that any payment made to the employee which is subject to pay as you go income tax is included in the income to determine how much superannuation guarantee contributions are to be made. Irrespective of what it was.

This would make it simpler for employers as there is no need to double check how each payment is classified. They could also double check their superannuation obligations quickly by ensuring it is 9.5% of gross payroll payments.

And it is simpler for employees. The superannuation on their pay slip should just be 9.5% of their gross pay. If not – they know the employer has made a mistake and challenge this.

3.0 Superannuation Guarantee contribution Rate need to be increased

Currently the Superannuation Guarantee contribution (SGC) Rate is 9.5%. This contribution rate is not enough to provide people with an adequate retirement.

For more information why I believe this, simple read the transcript of a video I produced in early 2017 which is in Appendix 3.

So in order to improve people's retirement, this SGC contribution rate needs to increase.

And this increase needs to be made sooner rather than later. At a bare minimum, the rate needs to *increase to the currently legislated 12% sooner than currently legislated*.

A 12% contribution rate would improve people retirement outcomes by about 25% of what is the situation today. So using the example in Appendix 3, it changes the number of glasses from just under 6 to just over 7 for someone who contributed all their life to super. This is still not enough for most people to have a comfortable retirement.

So the SGC rate should increase above 12% and be closer to the 15% for considered when the framework for the compulsory superannuation system was put in place.

4.0 Negative gearing and housing affordability

There has been a lot of discussion around negative gearing and housing affordability. I believe a lot of this is false reporting.

Included in Appendix 4 is a report I issued in January 2017 titled "The Real Reason for Sydney's House Price Growth – Is successive governments under investment in creating jobs in Regional Australia".

This report questions that if the same negative gearing tax laws exist across Australia, why can Sydney house prices rise 94 per cent in the last 10 years, but Brisbane house prices only increase by 51 per cent and only 12 per cent in Perth?

From my analysis it is the focus of governments and business on the two metropolitan areas of Sydney and Melbourne which is driving jobs growth in those two cities.

And people want to live where they want to work, so there is increasing demand for houses in Sydney and Melbourne continuing to push prices up.

Therefore changes to negative gearing rules are unlikely to change the demand for housing in Sydney and Melbourne.

Instead the *government should increase its focus on job creation in regional and rural Australia*.

Job creation in these areas will help in stopping the internal migration of people from regional and rural Australia to its big cities. And will also entice people already living in these big cities to move away and have both work and lower priced housing.

This is the only way in the long term to avoid housing in Sydney and Melbourne remaining unaffordable for new home owners

5.0 Negative gearing and implication it benefits the wealthy

There is some conjecture that negative gearing (whether for property, shares or other investments) is favouring high income earners.

If this is something that is concerning the government, rather than removing negative gearing in totality, the government should consider the example of the United States of America.

The USA has negative gearing but they call it be a different name. They call it Passive Activity Loss and they have specific passive activity loss rules.

Effectively under these rules, only people with incomes below a certain threshold can offset passive income losses (whether property shares etc.) against salary and wage income. And there are other limits imposed.

This could remove the issue that high income earners unfairly benefit from negative gearing.

6.0 Capital Gains Tax and implication it benefits the wealthy

There is some conjecture that the current 50% capital gains tax discount for individuals (whether for property, shares or other investments) is favouring high income earners and there is some discussion about this discount being reduced.

For long term owners of capital items, any such change could be considered unfair.

So if the government is considering any changes to the capital gains discount, *a more appropriate approach would be a scaled discount*.

For example:

- No discount as currently for assets held less than a year
- 10%- 15% discount for assets held more than one year but less than 5 years (or the inflation rate whichever is higher)
- 20% - 25% discount for assets held more than five years but less than 10 years (or the inflation rate whichever is higher)
- Etc.

This would reduce any unfair advantage between someone who sells an asset after 18 months as compared to 18 years.

7.0 Landlords offering Affordable Housing and the tax implications

There are many landlords who would offer below market rents for key workers like teachers, police persons, health workers etc.

But the current tax act does not allow this.

As detailed in Australian Taxation Office (ATO) publication" Rental properties 2017, "If you let a property, or part of a property, at less than normal commercial rates, this may limit the amount of deductions you can claim."

So, if I as a landlord was to rent my property at below market rates to a teacher or police officer, I run the risk that the ATO may not allow me to claim 100% of all the associated costs.

Why would I want to run the risk of not only getting lower rent but some of my expenses not being deductible?

So a simple solution would be *for the ATO to allow landlords to rent their property to appropriately qualified tenants at below market rates and still claim 100% of the costs*.

To ensure that the tenant is appropriately qualified, possibly the tenant needs to be vetted by a community housing authority and they sign off on this.

The qualified tenants could be based on income, occupation or a combination of both.

8.0 Affordable Housing and developer / landlord incentives

There is a lot of conversation about building affordable housing in Australia.

There is one simple problem. Most developers are for profit businesses and most landlord want to maximise their returns.

So why would they offer properties at below market rent, when they can get tenants paying full rent.

There is no real incentive. *So to encourage the construction of new affordable housing, the government could put in place an incentive for the landlord to offer properties at below market rent*.

Previously the government did this via the NRAS scheme. This scheme was subject to a number of abuses and failed to deliver an appropriate solution. One of the issues was that the incentive was a fixed dollar amount irrespective of the property. Another issue was that developers with NRAS allocations tended mark up the price of these properties.

To overcome these issues, the government could implement a different and better incentive system. And here is my recommendation.

Every new property constructed gets a certificate stating date of completion, construction cost / sale price and amount of GST in the construction cost / sale price. Irrespective of the developer / builder.

If the landlord wants to offer the housing at a below market rate, they approach approved community housing providers (who are not associated with the developer / builder). These housing providers vet the potential tenant to confirm they are qualified to rent at the agreed below market rate (say 80% of market rent). The housing provider gives a certificate confirming this and receives a one off fee for this.

The landlord rents the property at the below market rent to the tenant.

At tax time, the landlord signs off that they have rented to an approved tenant at the agreed market rent. That they have the certificate from the housing provider. The landlord then claims a rebate of 1/20 of the GST detailed in the construction certificate (assuming the property is rented for a full year). They can claim this for the first 20 years only.

Every two years the housing provider confirms that the tenant is still eligible for the below market rent.

If the landlord sells the property, the certificate and the eligibility to claim the tax rebate goes to the new owner, providing they rent the property to approved tenants at the agreed below market rate.

Under this solution, the value of the rebate relates to the value of the housing and is only given if the tenant is signed off by approved community housing providers.

This solves problems of developers over pricing property, or building accommodation not really addressing housing affordability (such as student accommodation). Community Housing providers get access to properties without having to incur the construction costs. People get access to affordable housing. Landlords now have an incentive to rent below market.

And the maximum cost of this is just effectively refunding the GST paid on the property in the first place.

9.0 Tax couples as couples to eliminate income splitting issues

Currently there is a large incentive for couples to income split to reduce tax.

For example a couple who each earn $90,000 per year, pay $45,552 in tax. A couple who one partner earns $150,000 and the other $30,000 pay $48,984 in tax. That is an extra $3,432 in tax on the same gross income.

That is why there is a whole industry around income splitting. An example of this is negatively geared property where typically 99% of the ownership is with the taxpayer with the highest income so they get the biggest tax break.

In order to eliminate this, the government should consider *developing a tax system that taxes couples as one tax unit*. In simple term this would reduce the cost of negative gearing without changing any of the other rules.

10.0 Pensions – Are we testing the right means

Right now we have a pension means test that rewards spending, not saving. A high income earner can spend all their money and get the same pension as a low income worker who never had the chance to properly save for their retirement.

If you don't believe me, let's look at Dennis, Jeff and Lennie. Three blokes who met at university in Sydney in the early 1970's when they were studying engineering.

After university all three had very similar careers and generally all three men earnt about the same amount of money each year.

Each of them married and had children of similar ages. In terms of their wives income, there was no significant difference in the women's pay, even though they worked in different jobs.

So for over 40 years, their income patterns were very similar.

But when it came the pension, only Dennis and Lennie qualified. Jeff failed the assets test and was ineligible for the pension.

But what set Jeff apart from Dennis and Lennie. It was not his income. So it had to be his spending habits.

So let's have a look at the spending habits of Dennis, Jeff and Lennie.

Dennis

Dennis and his wife were into snow skiing. And they soon tired of Australian ski fields and spent a lot of time and money skiing in New Zealand, Europe and North America. They would spend most Christmas holidays somewhere in the Northern Hemisphere skiing. On top of that they loved their toys. They had a new car every couple of years. They had the jet skis, the dirt bikes, the big televisions in every room. You name it they had it.

So Dennis and his family spent most of their money after the mortgage and other living expenses on toys and travel. In fact they spend more than they earned so when they stopped working they had credit card debts of $40,000 and still owed $200,000 on their home as they kept increasing their home loan every 5 or so years.

So after cashing in their super balance of $425,000, and paying off this debt, they had their house (worth about $800,000 in Western Sydney) and less than $200,000 in super. Based on this, they were eligible for the pension.

Lennie

Lennie and his wife were more into a big McMansion. With the triple garage, swimming pool, media room etc. And instead of living in Western Sydney they lived on the northern beaches of Sydney in a much more expensive house. So their mortgage took up a large chunk of their incomes. And on top of this the kids went to expensive private schools.

By the time they wanted to retire, they still owed over $400,000 on their mortgage and needed all of their super to pay this off. So after paying this off, they had their house (worth about $1.6 million) and very little cash left. So based on this, they too qualified for the pension.

Jeff

Now let's look at Jeff. Jeff and his family lived simply in western suburbs of Sydney, just around the corner from Dennis. They often had camping holidays in Australia and the kids went to the local public schools. Instead of spending money on toys like Dennis, or on a big house and private school fees like Lennie, they bought a positively geared investment property and worked hard to pay off the debt.

So when Jeff and his wife retired, they had, on top of their home worth $800,000, about $425,000 in super and an investment property worth $750,000. And because of this, they did not qualify for the pension

So what was the difference?

The only real difference between getting the pension for Dennis and Lennie and Jeff not getting the pension was their spending habits, not their income.

So right now we have a pension means test that rewards spending, not saving. A high income earner can spend all their money and get the same pension as a low income worker who never had the chance to properly save for their retirement.

Is that a fair system?

No.

What is the alternative?

It is time to start to have a system that focuses on getting people to save for their own retirement.

And whilst I am no policy expert or behavioural economist, the only way I can see that we can develop a fairer system is to base access to the pension on your earnings pre-retirement.

For example, if your average income for say the last 10 years before applying for the pension, was below the current pension rate, you are entitled to 100% of the pension.

For every dollar of average income above the base pension, you start to lose entitlement to the pension.

And as a safety net, there is a review board, (similar to where people ask for early access to their super) to consider people who have experienced hardship and whether they should get access to the pension.

Maybe this type of pension means test will start to "nudge" people to focus on saving for their own retirement, rather than spending so they get the pension.

Appendix 2 – Opinion Piece Issued 29 October 2017
Who really wins if the $450 monthly earnings threshold for superannuation is removed?

Analysis by Sydney Author and Chartered Accountant Wayne Wanders shows that unless regressive fees charged by superannuation funds like administration and exit fees are removed, it will be the superfund, not the low income earner who wins.

There has been a lot of talk lately about removing the $450 minimum monthly earnings threshold for superannuation. Fundamentally, there are a lot of reasons why it makes sense to remove this threshold and have all employees get paid superannuation irrespective of what they earn.

But this change has to be made properly, or the only real winners from this change will be the superannuation funds themselves.

Why?

Because most superannuation funds, whether they are retail or industry funds, charge regressive administration and exit fees. Because these fees are the same whether you have $500 or $50,000 in superannuation, they are regressive. And what's worse, these regressive fees eat away quickly at the superannuation balances of low income earners.

Don't believe me, then let's look at three people who are just about to start working part time at a local pool teaching people to swim. We have Mike and Jenny, both 18 and just about to start their first year of university and want some party money, and Paula, a 35 year mother, wanting some part time work whilst her kids are at school.

For the sake of this analysis, let's assume they start on 1 July and each get paid the same $400 per month. Under the current super rules, their employer does not need to pay super, but being a good corporate citizen, the employer decides to pay super on top of the $400 each earns per month. Their employer pays the super on the due date each quarter and gives them a 3 per cent pay rise each year.

Now, not thinking about their super, all three just have their super put in their employers default fund, which has consistently returned 5 per cent, per annum. This fund charges what seems to be a nominal weekly administration fee of $1.50 and a $35 exit fee.

Roll forward 12 months and the super statements arrive. Paula realises her mistake of creating a new account and transfers the balance to her previous fund. Jenny and Mike have no other funds, so they don't change.

Two years later, Jenny and Mike start full time jobs and Jenny transfers her super to her new employer's fund, but Mike does not do this for 2 more years.

So what happened to their super?

Appendix 2 – Opinion Piece Issued 29 October 2017
Who really wins if the $450 monthly earnings threshold for superannuation is removed?

Table 1: Analysis of Jenny, Mike and Paula's super accounts

Employee Employer contributes to default fund for Employee transfers to another superfund	Paula 1 Year After 1 Year	Jenny 3 Years After 3 Years	Mike 3 Years After 5 Years
Staring monthly income	$400.00	$400.00	$400.00
9.5% Contributions (after 3% pay increase each year)	$456.00	$1,409.40	$1,409.40
Contributions tax	-$43.32	-$133.92	-$133.92
Low income superannuation tax offset (LISTO)	$43.32	$133.92	$133.92
Fund Administration Fees	-$67.50	-$211.50	-$337.50
Fund Exit Fees	-$35.00	-$35.00	-$35.00
Fund Income at 5% return after investment fees	$11.40	$98.14	$210.48
Balance Transferred	$364.90	$1,261.04	$1,247.38
Super contributed	$456.00	$1,409.40	$1,409.40
Super Transferred	$364.90	$1,261.04	$1,247.38
Superannuation effectively "lost"	$91.10	$148.36	$162.02
Amount of superannuation returned	80.02%	89.47%	88.50%
Effective admin / exit fee %	22.48%	17.49%	26.43%

Notwithstanding the superfund reported a 5 per cent investment return, Jenny, Mike and Paula all lost money. That's right, their super went backwards.

For every dollar that their employer contributed to super, Jenny, Mike and Paula got less than 90 cents back! And it was not the government, who refunded the tax via the low income superannuation tax offset (LISTO).

It was because, in each instance, the superfund pocketed more in administration and exit fees, than was credited in fund income.

So a real killer for people with low superannuation balances is the regressive nature of fixed account fees such as administration fee and exit fees that most funds charge. In the case of Jenny, Mike and Paula, the effective rate of these fees was in excess of 17% of the funds contributed.

There is no way to describe this other than highway robbery. And it applies equally across industry and retail superfunds.

So if we really have low income earners superannuation balances at heart, not only should we remove the $450 monthly earnings threshold for superannuation on, but we should also remove the regressive fees such as administration and exit fees, charged by retail and industry super funds alike.

Appendix 3 – Opinion Piece
Why Your Super Will Never Be Enough

Based on current legislation your super will never be enough for you to retire on.

And I can show you why just by using some drinking glasses.

Let's use this glass of water as an example of your annual income and superannuation. As we know most people only ever save their compulsory superannuation every year. They are spending 90% of their income every year.

Putting this another way, you are drinking over 90% of the water in their glass every year leaving just a small amount of water for your future.

Now we know the government takes taxes out of your super, – so you are left with just about a small amount of water in your glass every year - About 8% of your income!

Now let's say you started this at 20 and did this for 45 years. What would you end up with?

Well about 3.6 glasses of water.

Now with luck, the returns of the superannuation fund were better than inflation – big assumption I know! Let's say your superannuation fund returned two per cent above inflation each year. This would turn these 3.6 glasses of water into just under six full glasses when you want to stop working.

So how long would these six glasses last?

When you were working you consumed about 90% of your water each year. Now you have stopped working you may be able to spend less, maybe your house is paid off by now, so you may only need to spend about 80% of a glass of water in each year.

So after 7 to 8 years, no glasses left. Your superannuation finished.

I don't know about you but I plan to live longer than 7 or years after I stop working.

How long do you plan to live?

And those 7 or 8 years assumes that you had 6 full glasses!

What if you are a woman who took time off to raise the children? I saw a survey recently that said women have about 65% of the super of men, so those six glasses of water turn into 4.

And do you want the really bad news? Women live longer than men – so less super to last longer!

What if you are an overseas immigrant and started work in Australia at a later age?

What if your health gave way, or you worked in a hard physical job? Could you continue to work for 45 + years?

And what about your mortgage. According to another study I saw, nearly 1 in 4 homes will still have a mortgage when their owner wants to retire. Your superannuation will be needed just to pay the mortgage off.

All of these situations reduce the amount of superannuation you may have left when you stop working.

So if this was you, chances are that after 4 or 5 years, your super is all gone

Nothing left. On the pension. Where's the golden future in that?

And that's why I firmly believe your super WILL NEVER BE ENOUGH

Appendix 4 – Opinion Piece
The Real Reason for Sydney's House Price Growth – Is successive governments under investment in creating jobs in Regional Australia

Executive Summary

The current contention around house prices in Sydney, is that Mum and Dad investors who are able to negatively gear investment properties, are driving demand and pushing house prices up.

Mr Wayne Wanders, Chartered Accountant and author of the book "Avoid the Poverty Trap", set out to determine if this contention is true. Mr Wanders undertook analysis using the publicly available housing data from sources such as the Australian Bureau of Statistics.

As negative gearing tax laws are consistent across Australia, Mr Wanders believes that, if Mum and Dad negative geared property investors were the major cause behind the growth in Sydney house prices, you would expect to see similar growth rates in other locations around Australia.

But what Mr Wanders found is that the facts do not support this.

The facts clearly show that apart from Melbourne, Sydney house prices have grown by nearly double other capital cities in the last 10 years, and nearly double regional NSW in the last six years.

Mr Wanders said that "if the same negative gearing tax laws exist across Australia why can Sydney house prices rise 94 per cent in the last 10 years, but Brisbane only increase by 51 per cent and only 12 per cent in Perth."

"Why can Sydney house prices go up significantly higher than regional NSW?"

So, the facts show that negative geared Mum and Dad investors are not the prime reason behind the growth in Sydney house prices.

There has to be another cause!

Given that Sydney's population has grown twice as fast a regional NSW, one could draw the conclusion that this population growth is a driver for increased demand for Sydney houses, and is a major factor behind the growth in Sydney house prices.

So the next question is why is the population growing more in Sydney that in regional NSW?

It has to be jobs.

People go where the work is.

If there is no work in the regional cities, irrespective of how cheap the housing, why would you live there?

So maybe the real cause of Sydney's house price growth is the fact that successive governments have under invested in regional towns to drive jobs growth in those towns.

And this lack of jobs is pushing people back into Sydney, placing pressure on Sydney's housing stock and driving up house prices.

Appendix 4 – Opinion Piece
The Real Reason for Sydney's House Price Growth – Is successive governments under investment in creating jobs in Regional Australia

Introduction

As Australia's property market operates under free market practices, the price of property is determined largely by supply and demand.

If demand exceeds supply, then prices rise. If supply exceeds demand then prices fall.

Overall property supply is determined by the existing number of houses plus any new housing being built. Property supply at any one time relates to how many new and existing homes are on the market for sale.

Property demand is either from owner occupiers or from Australian and international investors.

The current contention around house prices in Sydney, is that Mum and Dad investors who are able to negatively gear investment properties, are driving demand and pushing house prices up.

So Mr Wayne Wanders, author of the book "Avoid the Poverty Trap" extended the research done whilst writing his book to review whether negative gearing is the prime cause of the increase in house prices in Sydney.

So What is Negative Gearing?

A lot of people talk about the term negative gearing, but Mr Wanders feel very few people understand exactly what it is.

It simply means that the revenue earned (in the case of investment property, rents) is less than the expenses incurred (in the case of investment property things like interest, insurance, rates, water, etc.).

In plain English, you would say it was a loss. The person who has a negatively geared investment property has an annual loss. They are hoping this annual loss is more than compensated for by appreciation in value via capital gains.

Appendix 4 – Opinion Piece
The Real Reason for Sydney's House Price Growth – Is successive governments under investment in creating jobs in Regional Australia

Detailed Analysis

The current negative gearing tax laws are uniform across Australia. Whether you own a property in Sydney or one in Broken Hill, the tax treatment is the same. Therefore the starting point in this analysis is to compare Sydney's hosing price growth rate with other locations in Australia

Table 1 below compares Sydney's housing price growth rate over the last 10 years with the other capital cities.

Table 1: Capital City House Price Growth Sept 2006 to Sept 2016

	Residential Property Price Index				
	Sep-2006	Sep-2016	Change	% Change	Average per Year
Sydney	82.0	159.3	77.3	94.27%	9.43%
Melbourne	68.1	132.9	64.8	95.15%	9.52%
Brisbane	78.5	118.8	40.3	51.34%	5.13%
Adelaide	73.8	113.3	39.5	53.52%	5.35%
Perth	95.1	106.3	11.2	11.78%	1.18%
Hobart	84.6	113.4	28.8	34.04%	3.40%
Darwin	67.3	104.0	36.7	54.53%	5.45%
Canberra	76.0	113.5	37.5	49.34%	4.93%
Weighted average of eight capital cities	78.4	135.0	56.6	72.19%	7.22%

Source: ABS Report 6416.0 Residential Property Price Indexes: Eight Capital Cities

If negative gearing alone was the cause of the price growth in Sydney, you would have expected growth in other capital cities to be similar.

As you can see from Table 1, Sydney and Melbourne house price growth over the past 10 years has been nearly double of most of the other capital cities. This would tend to suggest that factors other than negative gearing are having a significant impact on house price growth in Sydney (and in Melbourne).

The comparison in Table 1 was between capital cities. Tables 2 and 3 below compare the housing price growth rates of selected Sydney suburbs with the housing price growth of selected regional towns in NSW.

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Table 2: Housing Price Growth of Selected Sydney Suburbs 2010 to 2016

		Median House Price				
Suburb	Postcode	2010	2016	Change	% Change	Averrage per Year
Chatswood	2067	$1,150,000	$2,255,000	$1,105,000	96.09%	16.01%
Penrith	2750	$318,000	$600,000	$282,000	88.68%	14.78%
Epping	2121	$880,000	$1,644,000	$764,000	86.82%	14.47%
Blacktown	2148	$354,000	$650,000	$296,000	83.62%	13.94%
Bradbury	2560	$310,000	$535,000	$225,000	72.58%	12.10%
St Ives	2075	$1,060,000	$1,828,000	$768,000	72.45%	12.08%
Bankstown	2200	$495,000	$842,000	$347,000	70.10%	11.68%
Rockdale	2216	$665,000	$1,120,000	$455,000	68.42%	11.40%
Sutherland	2232	$512,000	$861,000	$349,000	68.16%	11.36%
Kellyville	2155	$669,000	$1,070,000	$401,000	59.94%	9.99%
Maroubra	2035	$1,100,000	$1,745,000	$645,000	58.64%	9.77%

Source: Domain.com.au Suburb Profiles 27 January 2017

Table 3: Housing Price Growth of Selected NSW Regional Towns 2010 to 2016

		Median House Price				
Suburb	Postcode	2010	2016	Change	% Change	Averrage per Year
Goulburn	2580	$250,000	$363,000	$113,000	45.20%	7.53%
Nowra	2541	$245,000	$350,000	$105,000	42.86%	7.14%
Dubbo	2830	$257,000	$350,000	$93,000	36.19%	6.03%
Bathurst	2795	$273,000	$359,000	$86,000	31.50%	5.25%
Albury	2640	$365,000	$449,000	$84,000	23.01%	3.84%
Gunnedah	2380	$245,000	$325,000	$80,000	32.65%	5.44%
Tamworth	2340	$250,000	$326,000	$76,000	30.40%	5.07%
Wagga Wagga	2650	$309,000	$375,000	$66,000	21.36%	3.56%
Orange	2800	$295,000	$347,000	$52,000	17.63%	2.94%
Armidale	2350	$299,000	$350,000	$51,000	17.06%	2.84%
West Kempsey	2440	$197,000	$235,000	$38,000	19.29%	3.21%
Cobar	2835	$200,000	$230,000	$30,000	15.00%	2.50%
Cooma	2630	$208,000	$230,000	$22,000	10.58%	1.76%
Broken Hill	2880	$108,000	$130,000	$22,000	20.37%	3.40%
Grafton	2460	$265,000	$285,000	$20,000	7.55%	1.26%
Moree	2400	$205,000	$222,000	$17,000	8.29%	1.38%
Lismore	2480	$305,000	$308,000	$3,000	0.98%	0.16%
Casino	2470	$265,000	$237,000	-$28,000	-10.57%	-1.76%

Source: Domain.com.au Suburb Profiles 27 January 2017

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As you can see from Tables 2 and 3 the house price growth rate in various Sydney suburbs over the past 6 years, is much higher than the housing price growth rates seen in various regional towns in NSW for the same period.

Once again this would tend to suggest that factors other than negative gearing are having an impact on house price growth in Sydney verses regional NSW.

The comparisons of the house price growth of Sydney, verses most other places in Australia, (other than Melbourne) would suggest that investors and negative gearing tax laws are not the prime factor behind the high house price growth seen in Sydney in recent years.

If it is not investors and negative gearing, what else can drive up prices?

One such area that seems to be overlooked is owner occupier demand.

What drives owner occupier demand?

One of the largest contributing factors is population growth.

Table 4 sets out the population growth for Sydney and Regional NSW.

Table 4: NSW Population Growth 2010 to 2015

	Population			
	2010	2015	Growth	Growth %
Sydney LGA's	4,119,934	4,466,878	346,944	8.42%
Country NSW LGA's	3,024,358	3,150,806	126,448	4.18%
Grand Total	7,144,292	7,617,684	473,392	6.63%

LGA's – Local Government Areas
Source: ABS Report 3218.0 Regional Population Growth, Australia

From this table you can see that population growth in the Sydney Local Government Areas is more than double what the rest of NSW experienced.

You could then draw the conclusion that this population growth is a driver for increased demand for Sydney houses and is a major factor behind the growth in Sydney house prices.

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Conclusion

Given that negative gearing tax laws are consistent across Australia, if Mum and Dad negative geared property investors were the major cause behind the growth in Sydney house prices, you would expect to see similar growth rates in other locations around Australia.

However, the data in this report clearly shows that apart from Melbourne, Sydney house prices have grown by nearly double other capital cities in the last 10 years and nearly double regional NSW in the last six years.

So, the facts show that negative geared investors are not the prime reason behind the growth in Sydney house prices.

There has to be another cause!

Given the way Sydney's population has grown compared to regional NSW, one could draw the conclusion that this population growth is a driver for increased demand for Sydney houses and is a major factor behind the growth in Sydney house prices.

So the next question is why is the population growing more in Sydney that in regional NSW?

It has to be jobs.

People go where the work is.

If there is no work in the regional cities, irrespective of how cheap the housing, why would you live there?

So maybe the real cause of Sydney's house price growth is the fact that successive governments have under invested in regional towns to drive jobs growth in those towns.

And this lack of jobs is pushing people back into Sydney, placing pressure on Sydney's housing stock and driving up house prices.