Household Wealth prior to COVID-19: Evidence from the 2018 HILDA Survey

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Abstract

This article examines the distribution of wealth in Australia prior to the COVID-19 pandemic and considers the implications for the financial resilience of households during the associated economic downturn. In terms of their wealth, most Australian households appear well placed to withstand a temporary fall in income. However, younger households and those working in industries most affected by activity restrictions are likely to be more vulnerable to income loss; only around half of these households could cover three months of expenses out of their liquid assets. Highly indebted households that experience shocks to their income and have limited liquid assets will also find this period particularly challenging. Policies to support household income, as well as those aimed at rescheduling debt repayments, should cushion these effects. The resilience of households will also depend on the timing and sustainability of the economic recovery.

Introduction

The outbreak of COVID-19 is causing major disruptions to economies globally, including Australia. These developments have affected the physical and mental health of Australian households and have also resulted in economic hardship for some due to a decline in income and wealth. An analysis of the distribution of household wealth prior to the pandemic is useful for understanding the financial resilience of households as they entered this challenging time. In particular, it is important to understand the distribution of liquid wealth (such as cash and deposits) and households' capacity to service their debts, as these can influence how resilient households might be if their employment situation changes.

This article explores the distribution of household wealth prior to the COVID-19 pandemic using the Household and Labour Dynamics in Australia (HILDA) Survey. The HILDA Survey is a longitudinal study that has followed a panel of approximately 9,000 households since 2001. Every four years the survey includes a wealth module, which collects detailed information on household assets and liabilities; the latest observation available is for 2018. The representative nature of the survey allows analysis of Australian household wealth (total assets minus total debt) over a range of dimensions and over time. The dataset also includes household demographic information, such as age, industry of current employment, and home ownership status, which is useful in trying to assess impacts of the current economic downturn. To track individual households over time, an individual is designated as the 'household head' and followed across waves of the survey.[1]

Average wealth increased strongly in recent years

Household wealth grew more strongly over the four years from 2014 to 2018 than in the decade prior (Graph 1). Over this period, real (inflation-adjusted) wealth grew by more than 4 per cent per annum, to be $930,000 on average in 2018, with median wealth around $500,000. The primary drivers of increased wealth were growth in the value of housing and superannuation.

Other measures of household wealth, such as the household-level data from the Australian Bureau of Statistics (ABS) Survey of Income and Housing (SIH) and aggregate data from the Australian System of National Accounts (ASNA) also indicate that wealth grew strongly over this period.[2]

Low-wealth households may be disproportionately affected by the COVID-19 economic shock

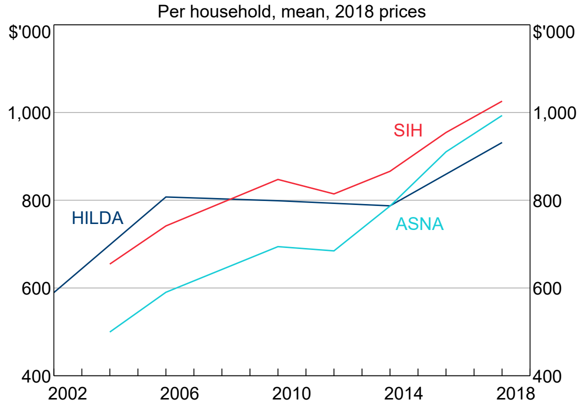
Some Australians are wealthier than others. The ages of household heads and the industry they work in both affect their incomes and thus their capacity to accumulate wealth, as well as the time they have had to do so. Households working in industries such as accommodation and food services, and arts and recreation services, typically had lower levels of wealth (Graph 2). This is partly because these workers earn less on average, and partly because they are disproportionately young people who have not had time to accumulate wealth.[3] Businesses and workers in these industries have been most affected by the current downturn, with one in three jobs in these industries lost between mid March and mid April of 2020 (ABS, 2020).

Households working in industries most affected by containment policies are more likely to work casually than workers in other industries, and are more likely to rent than own their own homes.[4]

Graph 1

Real Household Wealth

Per household, mean, 2018 prices

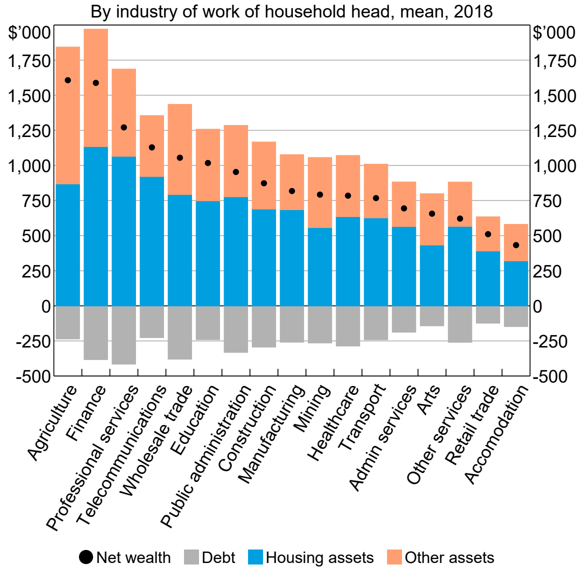


Sources: ABS; HILDA Survey Release 18.0; RBA

Graph 2

Household Wealth*

By industry of work of household head, mean, 2018



* Industries with less than 100 observations are excluded

Sources: HILDA Survey Release 18.0; RBA

Households headed by someone in casual work held, on average, around 30 per cent less wealth in 2018 than households headed by someone who was a permanent employee (Graph 3). Households that rent were much less wealthy than owner-occupier households, even when considering non-housing wealth, such as bank deposits and superannuation. This is partly because renters are on average younger than home owners.

Low-wealth households have smaller liquidity buffers to see them through the downturn

Total household wealth is likely not the best indicator of the financial resilience of households during a temporary contraction in the economy. Instead, it is the 'liquidity' of household wealth that will matter most, at least in the short term. Liquid wealth is defined as assets that can be readily and quickly converted and spent, such as bank deposits and equities. 'Liquid assets' can also include some share of superannuation balances to the extent that households meet the eligibility requirements to access the funds.[5]

Only about 15 per cent of total household wealth was liquid because a large share of assets held by households was in the form of housing or superannuation, which cannot be easily converted into cash. Liquid assets were much more unevenly distributed across households than total wealth: the bottom half of households when ranked by their liquid wealth held less than 2 per cent of all liquid wealth. By comparison, the bottom half of households held 9 per cent of overall wealth when ranked by wealth. Relatedly, the top 10 per cent of households held 44 per cent of liquid wealth, and 29 per cent of total wealth.

Low-wealth and younger households in particular held low stocks of liquid assets in 2018 (Graph 4). These assets are also small relative to expenditure: only half of households headed by someone under 35 held sufficient liquid assets to cover three months of their expenditure, compared with four-fifths of households headed by someone over 65. Household heads working in industries most affected by COVID-19 containment measures also had lower liquid asset buffers, with only half of households in service industries, retail, or accommodation and food services holding more than the equivalent of three months of expenditure in liquid assets, compared with 60 per cent of all other households.

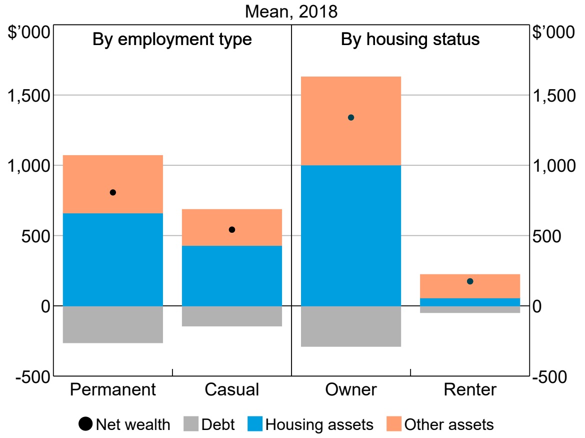
Indebtedness could pose challenges for some households, but appears manageable overall

When households are faced with changes in income over their lifetimes, debt can help to maintain their consumption and to accumulate assets, such as housing. The level of household debt in Australia relative to income increased noticeably

Graph 3

Household Wealth

Mean, 2018

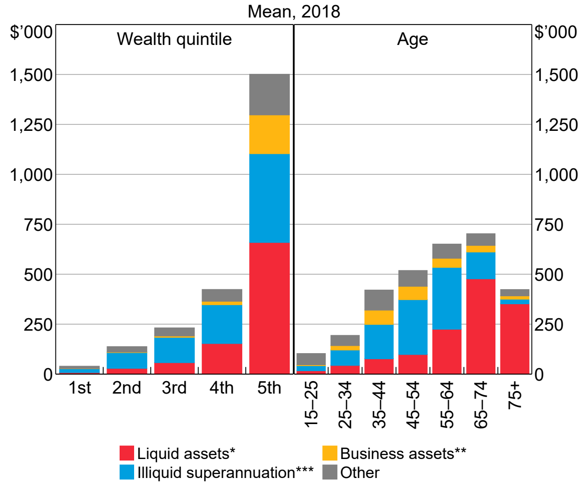


Sources: HILDA Survey Release 18.0; RBA

Graph 4

Non-housing Assets

Mean, 2018



* Cash deposits, equity & cash investments and retiree superannuation

** Value of any businesses owned by the household

*** Superannuation balances held by households yet to retire

Sources: HILDA Survey Release 18.0; RBA

over the four years from 2014 to 2018 and remains high by international standards; the aggregate debt-to-income ratio was close to 190 per cent in 2018.[6] High debt levels can test the resilience of households and their ability to maintain their consumption should they experience an unexpected decline in income. That being said, households with the greatest capacity to service debt – high-income households and households in their prime working years – held the highest levels of debt on average (Graph 5).

Housing debt accounted for a little over 80 per cent of household debt in 2018. High-income households and households headed by people between the ages of 35 to 64 held the largest share of housing debt (Graph 6). Conversely, low-income households and younger households held a small share of housing debt. However, as low-income and younger households are more likely to be employed in industries heavily affected by the virus containment measures, they may find it increasingly difficult to access credit. This is likely to result in challenges in entering the housing market in the near term. If these effects persist, their ability to use debt to accumulate wealth in the longer term will be inhibited.

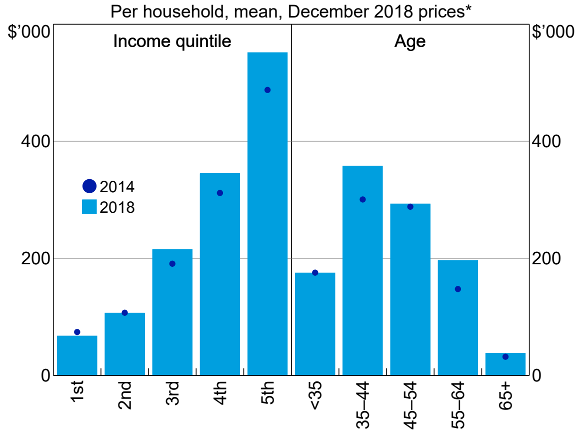
Investor housing debt was highly concentrated among high-income households. This is because high-income households have greater capacity to service debt and greater tax incentives to invest in rental housing. However, the potential low resilience of renters to the COVID-19 crisis poses a risk to indebted investors. Renters generally report experiencing more financial stress events than other household types and hold very limited liquid assets (RBA 2020). Given this, financial stress incidence is expected to be disproportionately high among renters during the COVID-19 crisis, though this will be largely mitigated in the short term by the introduction of rent discounts and deferrals, as well as a temporary suspension of evictions. While these support measures will assist renters, they will result in a permanent loss of rental income for investors. This may leave some investors vulnerable to mortgage stress, particularly those reliant on rental income to service their debts.

Of the households that have owner-occupier debt, the typical (median) low-income household allocated nearly twice the share of disposable income to meet their repayments than the typical high-income household (Graph 7). This suggests that some low-income households have limited capacity to service further debt and are more vulnerable to mortgage stress should they experience a decline in income. However, many households hold sizable buffers in the form of excess mortgage repayments (RBA 2020).[7] While the HILDA Survey does not provide information on excess mortgage repayments, liquid assets can act as an alternative measure of household buffers. High-income households with debt were much more likely to hold enough liquid assets to cover more than three months of housing debt

Graph 5

Real Household Debt

Per household, mean, December 2018 prices*



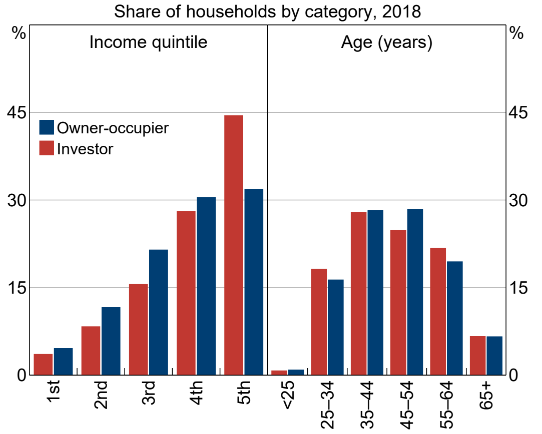
* Excludes households with no debt

Sources: HILDA Survey Release 18.0; RBA

Graph 6

Housing Debt

Share of households by category, 2018



Sources: HILDA Survey Release 18.0; RBA

repayments than low-income households. These buffers, alongside the temporary support measures to mortgagors (discussed below), may support the resilience of households affected by the economic downturn in the short term.

Government policies will ease the pressure on many households

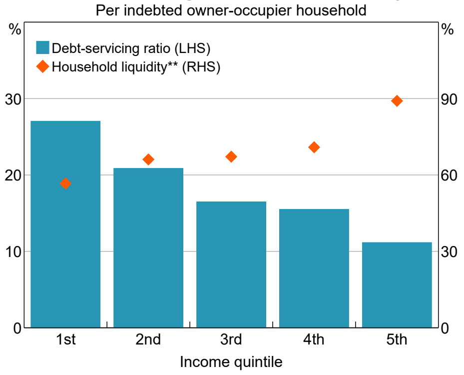
The Australian Government has introduced a number of economic measures to support households during the current economic downturn. These include 'economic support payments' for eligible households and a temporary fortnightly income supplement for recipients of JobSeeker and other selected payments. There have also been temporary changes to eligibility and obligations under Services Australia payments, which has broadened the number of households that are able to access income support.

The government has also introduced the JobKeeper Payment, which pays a flat fortnightly wage to eligible workers at firms that have seen substantial declines in their turnover. Eligible workers include full-time and part-time employees, casual employees who have been with their employer for at least 12 months as at 1 March, including those who had been stood down after this date, and certain business owners. These temporary support measures will provide cash flows to many households affected by the economic downturn resulting from the COVID-19 pandemic, and should

Graph 7

Debt-servicing Ratios and Liquidity*

Per indebted owner-occupier household



* Median; include 'minimum' owner-occupier housing debt repayment as a share of household disposable income

** Share of households that held enough liquid assets to cover more than three months of housing debt repayments

Sources: HILDA Survey Release 18.0; RBA

reduce the need for them to draw down on their liquid assets to cover their basic living expenses.

An additional program introduced to allow more than 1½ million people to access their superannuation early will support household cash flow, but could lead to lower wealth in the future, particularly if it takes some time for these households to rebuild their balances; for example, if withdrawal is followed by a period of unemployment. Eligible individuals are able to access up to $10,000 from their superannuation for each of the 2019/20 and 2020/21 financial years, effectively boosting their liquid assets. The conditions for this early access program include being unemployed, being made redundant or having working hours reduced by 20 per cent or more. Although households that are normally employed in the most affected industries are more likely to be eligible for early superannuation withdrawal, these households also tend to have the lowest superannuation balances. In 2018, one in three households working in food and accommodation services, retail trade, and other services industries held less than $20,000 in superannuation. There are also potential longer-term implications for the accrual of wealth from these early withdrawals because growth in superannuation comes in part from capital gains and interest and dividend earnings on existing balances, as well as from contributions.

Conclusion

Overall, many Australian households entered the economic contraction associated with the COVID-19 pandemic in a strong wealth position. However, some households are vulnerable to economic hardship. This is due to both the nature of the shock that has hit certain industries and workers more than others, and to the uneven distribution of household wealth, particularly liquid assets, across working households. Households working in the most affected industries are typically younger and less wealthy than others. They tend to hold fewer liquid assets, and as a result are more dependent on government policies to see them through this challenging period. Though these households hold less debt, they are also more vulnerable to financial stress given their limited cash buffers and lower debt-servicing capacity. ✠

Footnotes

[*] Nicole Adams and Lorenzo Schofer are from Financial Stability Department, Cara Holland is from Economic Analysis Department and Gabrielle Penrose is from Economic Research Department.

[1] The household head is determined by applying the following criteria, in order, until a unique person is selected: i) in a registered or de facto marriage; ii) a lone parent; iii) the person with the highest financial year income; and iv) the eldest person.

[2] For more information on the differences between HILDA and the aggregate national accounts, see Headey, Warren and Wooden (2008).

[3] Around one in four household heads working in service industries, retail, or accommodation and food services was under 30 years old, compared with around one in seven in all other industries.

[4] While here we only consider the industry of the household head, the majority of workers (around 60 per cent) in service industries, retail, or food and accommodation are not the head of their household. For these workers, 80 per cent live in households where the head does not work in one of these industries, meaning income losses in these households may be mitigated.

[5] Here we consider typical eligibility requirements, and exclude the government's early superannuation access scheme that has been implemented over recent months. Implications of the scheme are discussed in more detail below.

[6] See RBA (2020), 'Household Finances – Selected Ratios – E2', Statistical Tables, Household and Business Finance. Available at <https://www.rba.gov.au/statistics/tables/>.

[7] Alternative sources indicate that more than half of households with housing debt have over three months of mortgage repayments in offset accounts or redraw facilities. This suggests households are likely to have larger buffers than those implied in this article.

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