

Paper delivered at the 10th Biennial Conference of the
Australian Population Association
POPULATION AND GLOBALISATION:
AUSTRALIA IN THE 21ST CENTURY
Melbourne 28th November to 1st December 2000
Melbourne Australia

BABY BOOMERS AND PROPERTY BUSTS

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Approximately 3900 words

Abstract

In the latter half of the 20th century the baby boom generation created an increased demand for many aspects of society including education, housing and medical services. Only now are the negative aspects resulting from this unique demand being fully considered. One of the most important issues is the impact on residential housing values which directly or indirectly affects most residents whether owning, buying or renting.

The relationship between the ageing of the baby boomers and housing values is a current topic of debate throughout the world. Particularly in the U.S.A. warnings have been sounded of a dramatic decrease in property values causing a property bust as the baby boomers move into the older generation.

This paper revisits the baby boom generation and discusses previous research in the worldwide debate concerning their impact on housing values. The status of the Australian baby boomers is examined and the future impact on residential house values in Australia is contemplated.

The baby boom generation has been closely observed and well documented by demographers worldwide. Even though the baby boom is only one of many generations it has been easily recognisable by one unique characteristic - its overwhelming size. The sharp rise in population following World War 2 was recorded in many western civilisations with the arrival and subsequent ageing of the baby boom creating unprecedented demand for services and facilities. The impact of the baby boom generation has been likened the python swallowing an egg. The baby boom period has been described by some demographers as 'marriage madness' as it stimulated demand for suburban housing on a new and vast scale and subsequently created the baby boom (Mackay, 1997). This demand surge also affected a wide spectrum of public and private services and infrastructure including hospitals, educational facilities and employment/industry.

With the arrival of the baby boomers between 1946 and 1964 long since completed and the ageing process well underway, consideration must now be given to the aftermath resulting from baby boomers maturing into Older Australians, a period referred to as the 'baby bust'. The first of the baby boomers turn 55 years as early as 2001 and begin to retire. Although serious consideration has been given to planning for future needs of the baby boomers, it appears less emphasis has been placed upon the vacuum they will create and the effect on goods and services, especially demand for housing. Following an analysis of time series data in the United States there was evidence of a striking correlation between the age structure of the population and real house prices in the United States (Engelhardt & Poterba, 1991). It has been suggested that if this historical correlation continued with the passing through of the baby boomers, real house prices could fall substantially as we moved into the 21st century (Mankiw & Weil, 1989).

This research is concerned with this 'baby bust' vacuum and the subsequent effect upon demand for housing once the over-sized baby boom generation reaches retirement age. Furthermore, what will become of the surplus housing they no longer require and how will it affect the general housing market? This paper discusses the possibility of a population decrease and relevant global research in this area.

Baby Boom Generation

Differences of opinion exist as to the exact time span of the baby boom generation. From a chronological perspective a generation can be defined as 'the average period of time from an individual's birth until the birth of that person's first child', although time estimates for a generation have ranged from fifteen to thirty years (MacManus, 1997). While there is agreement the first baby boomer was born in 1946, the birth year for the last baby boomer is disputed and varies up to 1971 - refer to Figure 1. For this research the most popular time period of 1946-1964 was adopted with adults in this generation aged between 36 and 54 years today (Plane & Rogerson, 1994).

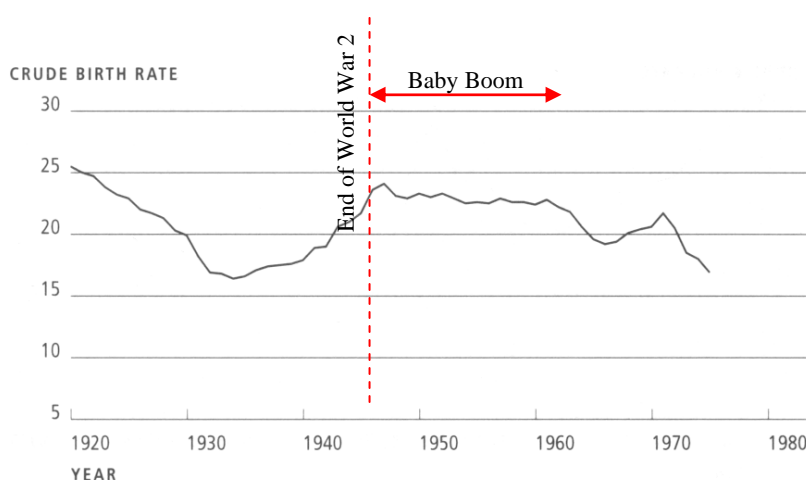


Figure 1 – Births per 1,000 Population, Australia, 1920-80 (Falkingham, 1997)

Most often the baby boom generation is associated with the end of World War 2 and the subsequent explosion in birth rates as shown in Figure 1, although it should be recognised that other factors contributed significantly to this post-war increase in the population base. The baby boom generation was the end product from two other booms that commenced after the WW2 and lasted until the early 1960s, namely the marriage boom and the economic boom (Mackay, 1997). The synergy from these three factors laid the foundation for the sharp increase in births and were accompanied by initial changes in:

- marriage age;
- couples entering into marriage;
- birth spacing;
- fertility rates (Borrie, 1981).

However the upward trend in fertility rates has long since reversed and the natural increase is projected to continue decreasing as shown in Figure 2. This can be partly attributed to a demographic transition affecting household formation rates that accompanied the baby boomers and continues today, including:

- postponement of marriage;
- delayed first childbirth;
- rise in single living;
- cohabitation;
- prolonged residence in parental household;
- increased divorce rates;
- high separation rates of cohabitants. (Lesthaeghe, 1998).

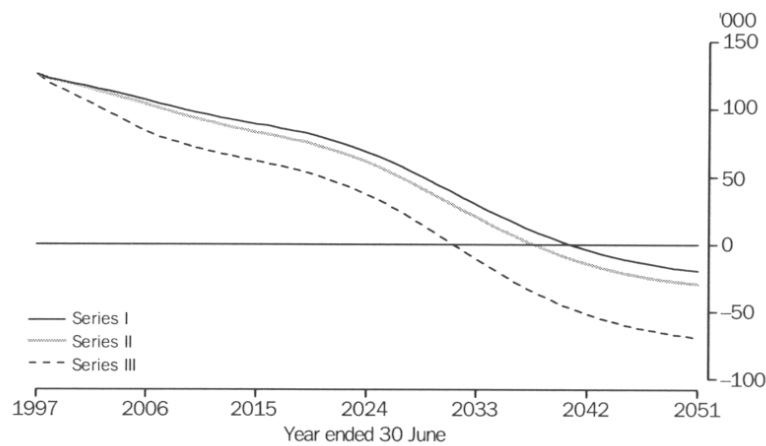


Figure 2 – Projected Natural Increase - Australia (ABS 3222.0, 1998).

The baby boom generation stood as a symbol of optimism, with the large-scale production of babies signaling a return to peace, normality and the contentment of stable family life. Furthermore 'home and family' became the focal point of Australian society (Mackay, 1997). Today the ageing of the baby boom generation and the maturing of the baby bust generation into adulthood are the most significant trends affecting potential household formation (Apgar, Brown, Masnick & Pitkin, 1994). However attention should also be given to life after the baby boomers. In many respects, the ageing of the baby boomers is a ticking 'demographic time bomb' which will only take effect when this generation matures into older residents (Thau & Heflin, 1997). The direct and indirect effect of this vacuum can be compared to original arrival of the baby boom generation, although in reverse when considering the 'before' and 'after' scenarios.

The Baby Boom and Population Projections in Australia

The ageing of the baby boomers has been acknowledged and well documented by the Australian Bureau of Statistics (ABS) in numerous ABS publications.

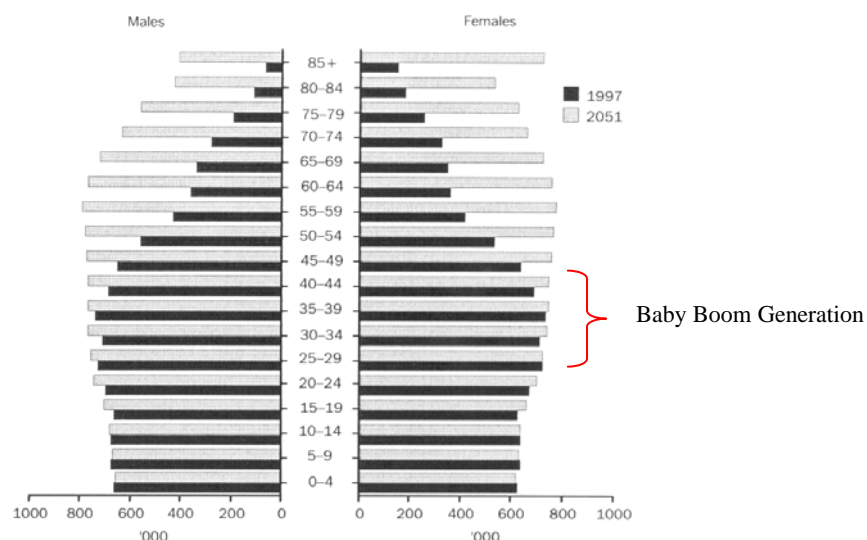


Figure 3 – Projected Population, Series 2, Australia (ABS 3222.0, 1998).

Of most interest in this analysis is the 65 years and over age bracket which is predicted to increase from 12% in 1997 to between 24% and 26% of the Australian population by 2051 as highlighted in Figure 3 (ABS 3222.0, 1998). The highest annual rates of growth for this age group will occur between 2011 and 2021 and are due to the aging of the baby boom generation (ABS 3222.0, 1998). Of parallel importance in this analysis is the shrinking size of the younger age brackets (Figure 3) and the reduced proportion of the population participating in the housing market.

Implications for older age groups are even more startling. It was predicted the Australian population aged 85 years and over will increase from 241,000 (1.3% of the total population) in 1999 up to approximately 1.3 million (5% of the population) in 2051 (ABS 3222.0, 2000). Questions must now be asked ascertaining which other 5% of the population will buy housing vacated by the baby boomers. Furthermore an increasing proportion of the 1.3 million older residents would be living alone. For example in N.S.W. over 25% of the 65 years and over group already live alone (ABS 4108.1, 2000). Although the ageing process in Australia is confirmed and can be accurately predicted, the size and characteristics of ensuing generations are less certain.

Housing Markets

Real house prices are directly determined by the willingness of households to pay for (and the willingness of a supplier to supply) a constant-quality house (Green & Hendershott, 1996). According to standard economic theory, when demand exceeds (relatively fixed) supply, prices rise. The real estate analyst may use demographic information to estimate this demand for housing units in a given area, with the basic assumption that each new household formation requires some type of housing unit (Runnels, 1989). This follows the premise that as growth in the adult population slows, so will the demand for new housing although these changes may take decades to play out (Hill & Peterson, 1994). Unfortunately the housing market is more complex and less than efficient in many respects.

As well as providing basic shelter, the housing market is a pivotal element in Australia's economic landscape and is intertwined with interest rates, the consumer price index and inflation. Already 25,000 less houses have been constructed in Australia during 2000 which is already set to cause major retrenchments, having widespread implications for this country's economy (Voorhaar, 2000). House construction and renovations are an important provider of employment with direct and indirect implications for providers of construction materials, urban land and financial services. A downturn in this industry can have dire economic and political consequences and all levels of governments are quick to identify and address decreases in housing demand. This is a different scenario to an increase in housing demand creating full employment, as was the situation to some extent when the baby boomers originally left home in the 1970s and 80s.

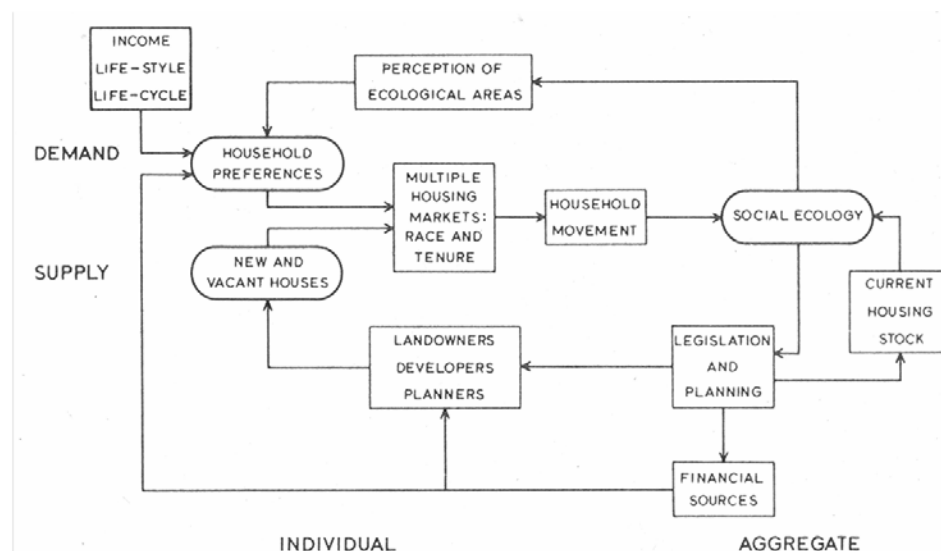


Figure 3 – Aggregate Housing Market Structure (Robson, 1975, p.29).

The merits of demographic methods in housing market research have been widely recognised although it is accepted that demographic changes are not the sole factors affecting residential markets. Figure 3 is a simplistic representation of the major influences in a residential market highlighting the role of lifecycles and lifestyles from a demand perspective. Overall demographic-based forecasts provide information on the fundamental aspects of demand and can be more reliably projected than the other factors (Myers, 1987). In an attempt to segment housing demand, Feitelson (1993) proposed there are several categories can describe members of a household:

- different ethnic, religious or racial group; and
- different needs depending on the lifecycle of the household.

With the passing through of the baby boom generation resulting in a shrinking population base in the prime home buying years, many are concerned about decreased demand and subsequent lower prices. However housing analysts disagree over how the ageing baby boom generation will affect house prices. It was argued that house prices would either (a) decrease markedly, or (b) show little or no change. The main points from previous research supporting both arguments are presented below.

Consensus A - House Prices will Decrease

* The suggestion that house prices will decrease with the aging of the baby boomers is partly based on historical evidence from soaring house prices in the 1970s and 1980s commonly attributed to the baby boom generation (Braus, 1995). It was considered 'what goes up must come down'.

* In a high profile study, it was predicted that house prices in the USA would decline by 47% as the baby boom generation passed through due to lower than average real per capital housing expenditure from a decreased population base (Mankiw & Weil, 1989). This research created substantial interest and rather than planning for the needs of the baby boom generation, for the first time serious consideration was given to the backwash and downward influence on house prices.

* Relying heavily on the premise that the value of residential land and improvements depend on the presence of sufficient bidders to support prices, Myers (1987) suggested the ageing of the baby boom generation in the USA must depress the growth of housing demand from previous levels. It was added that decreases in house prices would occur but were not as certain as lower demand.

* Following research into the effect of demographics on the Japanese house market, Ohtake & Shintani (1996) concluded the ageing of the baby boomers over the long term would only affect the housing market from a housing stock perspective as opposed to house prices. However over the short term the passing through of the baby boomers should have a significant effect on house prices before there is an adjustment in the market (Ohtake et al, 1996).

* With the baby boomers ageing and moving into retirement, real house prices seem more likely to fall unless there is a return to levels of real growth (Hendershott, 1991). Nevertheless the research concluded the decline would be less than the suggested 47% reduction in real house prices.

Consensus B - Little or No Change in House Prices

* Research into the US housing market concluded it was difficult to see in the population numbers a compelling reason for average house prices to fall (Hill et al, 1994). Even so, it was conceded that the population slowdown is an important economic and social event with the potential to substantially reduce the homebuilding in the economy and alter the prices of some single-family homes. Additional predictions included:

- demand for housing will fall for those in the 35-44 age group during the first decade of this century as this age group traditionally includes larger families with children, and prices of housing for this bracket may weaken;
- demographics will serve to strengthen the price of homes that are popular with older adults or empty nesters (Hill et al, 1994).

* In reference to the Canadian housing market, it was argued that the sharp increases in house prices could not be completely explained by the baby boom generation but the causes remain undetermined and influenced by other factors (Engelhardt et al, 1991) as indicated in Figure 3. Nevertheless it was accepted that large changes in relative house prices from demographic influences are neither unprecedented nor impossible.

* According to Green et al (1996) the shift in the baby boom generation in the 1970s and most of the 1980s positively influenced house prices, especially in household formation when the baby boomers left the houses they were reared in for their own houses. Rather than influenced by demographic factors substantial changes in real prices are more likely to be due to shifts in non-demographic variables such as real construction costs and interest rates rather than from demographic change. Establishing the direct link between demographic demand and house prices had been challenging due to the influence of:

- impact of supply factors;
- effect of other factors such as interest rates;
- housing markets are not 'efficient' in their operation (Green et al, 1996).

* After acknowledging the baby bust will undoubtedly exert downward pressure on the real price of housing, Garner (1992) concluded that fluctuations in the housing market depend on *both* economic and demographic conditions. It was also proposed that demand-side influences such as the increase in single person households could partly offset the effects of the baby bust on housing demand (Garner, 1992).

* The well-publicised inefficiency of the housing market was the main unknown variable if assessing the effect of the post baby boom on house prices (Holland, 1991). Although the baby boom has been the major factor behind housing investment, it has not been the major factor behind increased prices.

* It was argued that demographics would only affect rental prices as capital house prices are influenced by an array of additional influences considered too difficult to measure (Hamilton, 1991). Furthermore it was considered that increases in house values are linked to income rather than the baby boomers.

* After analysing previous research supporting a decline in house prices, Swan (1995) concluded that the demand factors were misinterpreted. Rather than measuring demand in the traditional manner, these researchers used overall population levels that were closely correlated with adult population. This in turn was correlated with income which is recognised as one of the main determinants of housing demand.

Other Demographic Considerations

In addition to the ageing of the baby boomers there are other demographic changes to be factored into the equation, which have not been fully considered. Although age composition will alter considerably due to the passing through of the baby boom generation, it appears little attention has been devoted to the influence of future changes in household formation rates upon housing values. At times housing researchers to place all their interest upon demographic trends, ignoring the important implications of headship rates possibly due to a lack of understanding (Smith, 1984). Although demographers traditionally use individuals as their basic unit of analysis, the household is the practical concept (Plane et al, 1994). The importance is drawn to demographic factors affecting changes in population levels and are centred around:

- (a) **Lower fertility rate:** peaking at a high of 3.6 births per woman in 1961, the fertility rate has steadily decreased to around 1.8 or 1.9 per year. According to ABS (3222.0, 1998) the fertility rate is expected to stabilise to approximately 1.75 per year as shown in Figure 4. This equates to a 50% reduction to the level recorded in the baby boom era and is below the replacement rate of 2.1;
- (b) **Overseas migration:** the level of overseas migration has traditionally fluctuated and is subject to political influences. It can adversely increase or decrease household formation rates and consequently is difficult to forecast over the long term.

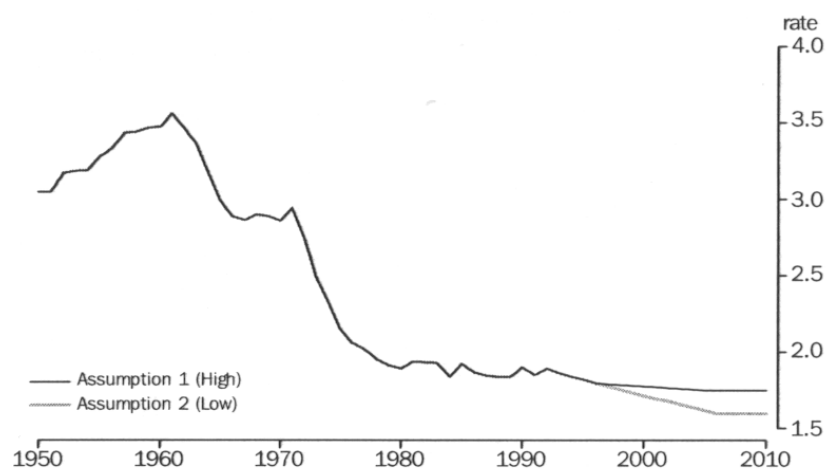


Figure 4 – Total Fertility Rate -Australia Observed and Assumed (ABS 3222.0, 1998).

The ageing of the baby boomer generation has substantially raised the profile of the imminent baby bust and the subsequent impact on house prices. The two primary methods of replacing this void, especially in regards to the labour force would be through increasing fertility rates and/or immigration rates. In respect to fertility rates, many women have decided to postpone or forgo childbearing and coupled with an increased female participation in the workforce it appears unlikely that fertility rates will increase dramatically in the foreseeable future. Substantial decreases have already occurred and are forecast to drop even further. Recognition of this scenario is required from all levels of government, which should also be accompanied by possible solutions to rectify this decline. Levels of overseas immigration are harder to predict, although demand to live in this country has been encouraged by the higher profile of Australia in recent times due to the Olympics and lifestyle advantages. Collectively it appears these two factors would have a negligible or perhaps small counter-balance to the baby bust.

Conclusion

There remains substantial conjecture over the degree to which house prices will be affected by the passing through of the baby boom generation. In addition, numerous other macroeconomic factors influence Australian housing markets and could counter-act the impact of a population decrease including changes in fertility rates and immigration policy. If demand fell due to a smaller population base a chain reaction would commence, decreasing the supply of new and established housing stock and indirectly influencing house prices. Changes in household formation rates including single person households should also be factored into the equation. On a brighter side, after considering the close analysis traditionally placed on new house construction any signs of a slowdown from the baby bust would be quickly recognised and acknowledged by the relevant authorities and transmitted to the marketplace. Potential remedies would include repackaging the housing product towards the children of the baby boomers, placing more emphasis on one bedroom apartments and two bedroom houses as in past eras. This would have the effect of redistributing demand and recognising the days of the four bedroom house may be as limited as the baby boomers.

After acknowledging arguments for and against the influence of baby boomers on the housing market, it appeared the advancing baby boom generation presented more questions than answers. Previous research failed to reach a general consensus regarding the effect on house prices and true answers will only be provided in reality. The cliché 'watch this space' applies to the influence of ageing baby boomers upon the housing market. Even as market sectors such as retirement homes prepare for the next stage of increased baby boomer demand, it appears few are realistically accepting the possibility of a downturn. Perhaps the baby boom generation has conditioned the marketplace to accept a continually rising population base with the reality of a shrinking population almost impossible to comprehend, drawing similarities to a sharemarket bust. Originally demographers provided a higher appreciation and better understanding of life when the baby boomers first arrived, and they should convey the impending baby bust including the broad implications for house prices as they become clearer. This paper highlighted the chasm between demography and housing research and doesn't belong to either field but is somewhere in-between as the emerging area of *housing demography*. Finally, in regards to the passing through of the egg known as the baby boomers only time will tell what the python will digest next and if it will 'fill the hole'.

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