



# State of household formation



State of the Nation's Housing 2021–22

# State of household formation



-41k

Hit to annual net overseas migration (NOM) in 2021–22

due to closed borders, low arrivals, and continued departures of residents



1.7m

Net new households by 2032



Big is back

Households preferred larger houses with more bedrooms and space during the pandemic, especially in regional and coastal towns

## KEY POINTS

- With international borders reopening and stronger economic activity anticipated after a period of prolonged pandemic-related restrictions, new household formation is expected to recover strongly over the next few years.
- During 2020–21, population growth remained weak on the back of negative NOM. NOM is expected to remain weak in 2021–22 (at -41,000) but thereafter is expected to recover to 180,000 in 2022–23 and then 213,000 in 2023–24.
- The relaxing of international border restrictions and expected recovery in NOM and broader economic recovery is expected to underpin more than 1.7 million net new households forming across Australia from 2022 to 2032. On the back of an expected recovery in NOM, average household growth of 175,000 is expected annually over the 10 years to 2032.
- By household type, the strongest growth in new households is expected from lone person households (around 595,000 or 35% of total), then couple families without children (488,000 or 29% of total), then couple families with children (361,000 or 21% of total).
- The impact of the population shock has been felt differently across regional and city housing markets. Inner areas of major cities have borne the brunt of negative NOM (in particular the drop in international students), with outer areas of major cities and regional areas seeing stronger than normal household formation.
- The pandemic induced shock and lower household formation caused rental vacancies to rise sharply and rents to decline in 2020, particularly in Sydney and Melbourne. But vacancy rates are now back to pre-pandemic levels in these cities. This suggests some latent household formation may be occurring that isn't explicitly accounted for in our projections.
- The pandemic introduced stronger preferences for larger dwellings and for living in wide-open spaces, such as in regional and coastal towns. It will take some time and better data to determine whether these behaviours are distinct from pre-pandemic urban-regional trends.
- While there is considerable uncertainty, household formation rates could increase quickly as international borders reopen. Given vacancy rates are already back at (or close to) pre-pandemic levels, delays in getting new housing stock to market in a timely way will have adverse consequences for affordability, particularly for renters.

---

## Introduction

# This chapter provides projections of new household formation

It outlines the factors that drive new household formation (as distinct from housing demand, which is more a reflection of the state of the market and the amount of transacting in the market – see Box 1), while also assessing the current and future state of household formation in the context of Australia's economic reopening and the likely return of strong population growth.

COVID-19 precipitated Australia's largest population shock in a century – the biggest fall in NOM since records began, substantially reducing the rate of new household formation. But now international borders restrictions are being relaxed, together with a strengthening economy, rates of new household formation are likely rebound strongly over the coming years.

The population shock has led to highly uneven outcomes across cities and regions, and different housing segments. Fewer people have left regions seeking work in the cities and many people migrated (at least temporarily) to regional and coastal areas during the pandemic to escape pandemic restrictions. The ability to work from home has helped exacerbate this behaviour, which is putting pressure on certain (particularly regional) housing markets around the country.

Household formation rates are expected to increase quickly as international borders reopen. Given the lead times for new housing developments, planning authorities should start acting now to facilitate adequate supply to market in a timely way. Otherwise, Australia's already poor housing affordability is likely to worsen over the coming years – particularly for the nation's renters.



**Box 1: Defining household formation**

## Housing demand and household formation

New household formation measures the number of households expected to form based on assumptions about population growth, living preferences of different age groups and the state of the economy.

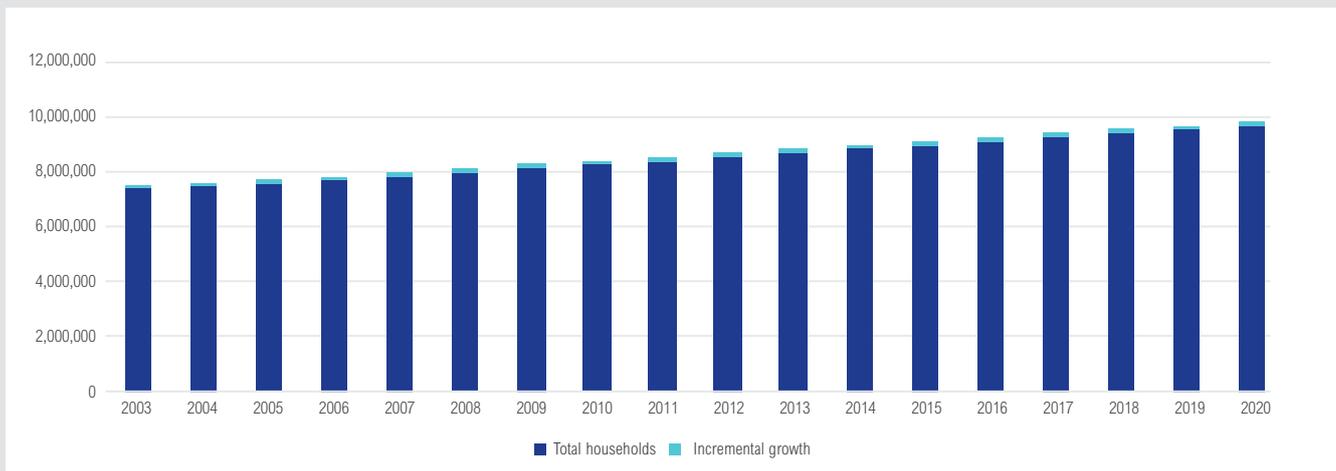
Australia has close to 10 million households, with new household formation amounting to around 1–2% of total households each year.

New household formation is distinct from observed market demand, which is reflected in transaction volumes, clearance rates and prices. New household formation is a relatively small component of overall market demand as it measures the incremental change in number of households (Figure 2.1).

Tracking household formation is important because when the number of new households forming over time is greater than the new supply coming into the market (net of demolitions) it can reduce vacancy rates and feed through to higher rental costs, with adverse consequences for affordability. In the short term, new household formation rarely coincides with housing market cycles.

In 2020–21, new household formation was affected by the sharp falls in NOM. But demand was supported by substantial fiscal and monetary stimulus. As a result, NHFIC's industry liaison suggests demand for detached housing continues to outstrip supply in many areas across Australia, including Sydney (see table 2.1).

**Figure 2.1: Incremental growth in households relative to total stock of households**



Source: ABS, NHFIC



## New household formation is a relatively small component of overall market demand as it measures the *incremental change* in number of households

The central projections in this chapter measure new household formation. They not only account for population growth and demographic factors but also adjust for a broader suite of economic factors, which impact on living arrangements – and hence household size – over the short and long term. The central projections do not indicate the strength of demand in the market.

**Note:** NHFIC's first State of the Nation's Housing report used a concept called 'adjusted underlying demand', which was another name for new household formation. In this report, to improve understanding, we refer only to household formation.

**Table 2.1: Demand outpacing supply in Sydney greenfield areas**

Estate	Timing	Size of Lot Release	Amount of Release Sold	Level of Interest	Developer
Catherine Park	Early October	10	100%	700 calls within 5 minutes	Harrington Estates
Catherine Park	Mid October	30	100%	Over 700 expressions of interest, sold by ballot	Harrington Estates
Gregory Hills	Mid October	4	100%	1,200 real estate agent page views	Dartwest
The Gables	Mid October	30	100%	1,400 requests for appointments	Stockland
Rosella Rise	September	11	100%	All lots secured within 2 minutes	AVJennings
Multiple Estates	Mid October	66	99%	140 clients actively waiting for further releases	Anvest Holdings

Source: UDIA

## Factors affecting new household formation

This section briefly discusses the main factors that drive household formation and the unusual factors at play during the pandemic affecting household growth.

Generally, new household formation is driven by a range of factors, but the main considerations are population, demographic and ageing factors, economic variables, and housing preferences.

### Population

The key driver of new household formation (and dissolution) is population growth, which is driven by natural increase (births and deaths) and NOM.

Natural increase is not a significant predictor of household formation: births rarely trigger the creation of a new household (as most just add an additional resident to an existing household); and only lone person deaths reduce the total number of households.

In our State of the Nation's Housing 2020 report, NOM was projected to come in at around -72,000 people for 2020–21. In the year ending June 2021, NOM was -88,800.

Australia's population growth is typically dominated by the flow of more than 200,000 temporary and permanent migrants looking to study or to work. Due to closed borders during the pandemic, overseas migration has been running at around -90,000 (annually) – a net change of around 300,000 – due to very low levels of arrivals, while departures of temporary residents have continued.

The Centre for Population estimates that NOM will recover slowly in 2021–22 to around -41,000, but then more strongly in 2022–23 to 180,000.

The age structure of the population also influences new household formation. People have different propensities to form new households depending on their age and social and economic circumstances. Compared with decades ago, people tend to form households later in life due to studying longer and having families later.

### Demographic and ageing factors

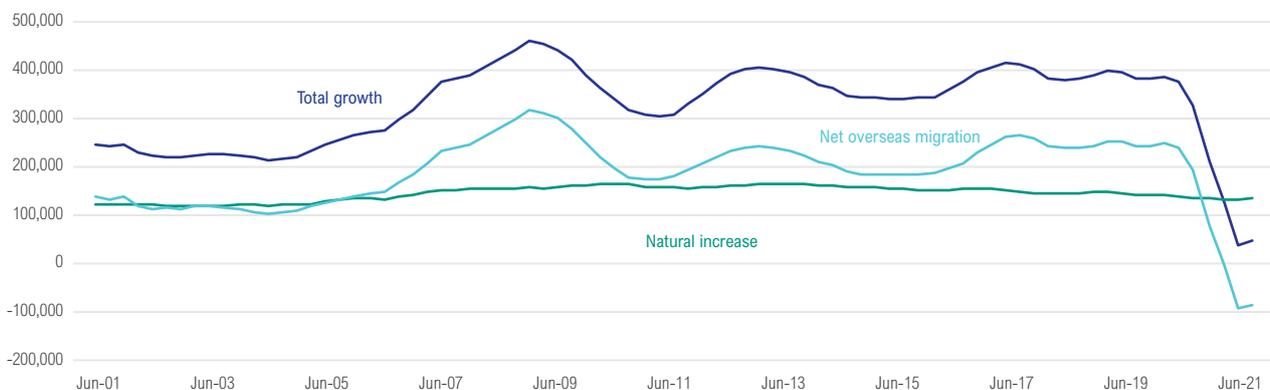
Household formation increases due to lifecycle changes, such as young adults leaving the family home or couple families divorcing. Likewise, household formation decreases due to lifecycle changes, such as lone person households forming couple families, ageing (as older residents move into non-private dwellings, such as residential aged care) or death of a lone-person household. Births have a negligible effect on household formation.

### Economic variables

The state of the economy also effects the rate of household formation. When people have jobs and are earning income it increases their ability to move out of their parents' homes and either move in with friends/partner or live alone. Conversely, when people lose jobs and have limited income earning capacity they tend to move back with their parents or look for cheaper shared living arrangements.

Anecdotal evidence suggests that, at the beginning of the pandemic, hundreds of thousands of (mostly younger) Australians moved back in with their parents after losing their jobs. But given the relative strength of the economy compared to the outlook in our first report, household formation is likely to have turned around in some areas as people regained employment.

Figure 2.2: Key components of population growth (actuals)

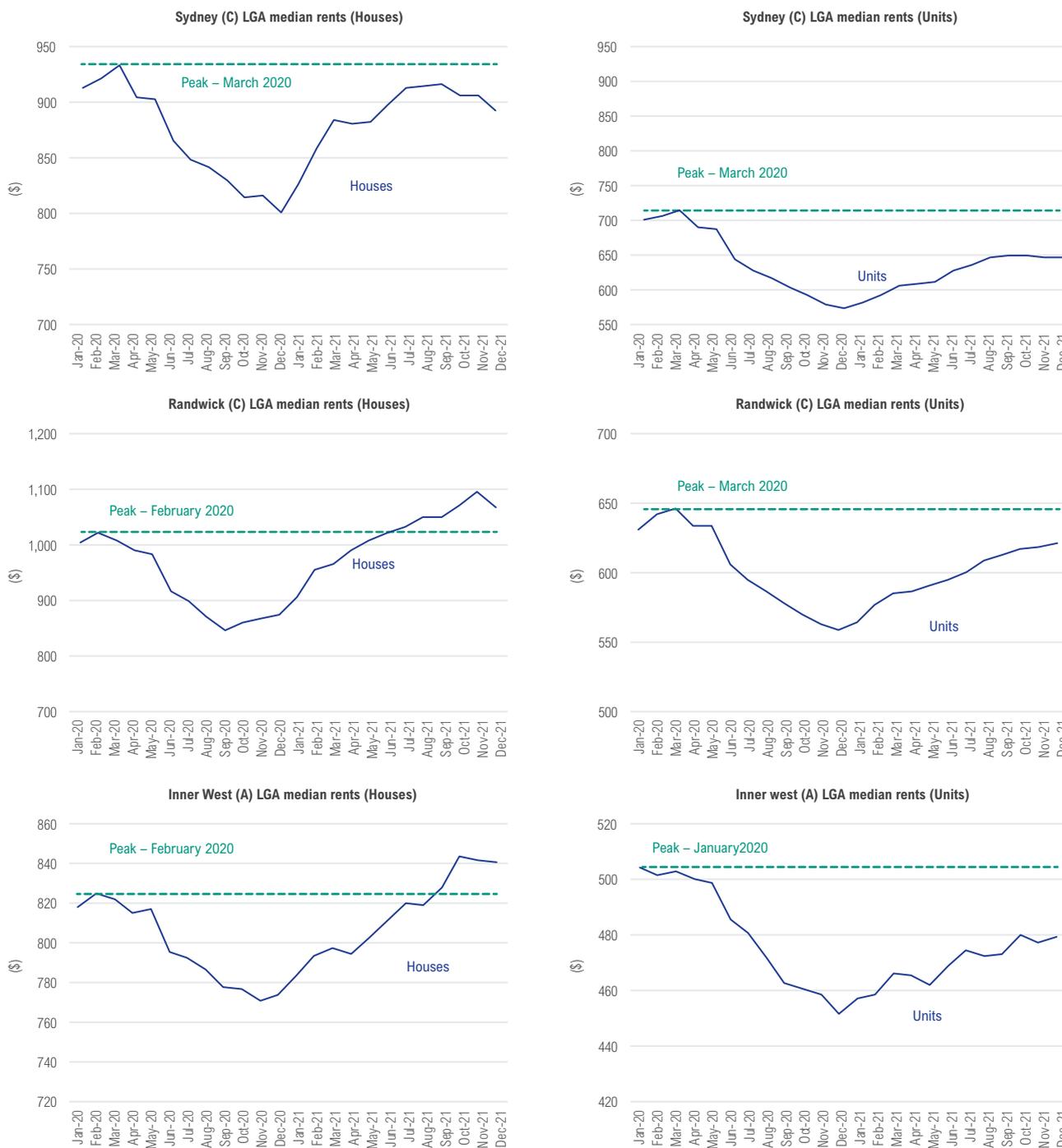


Source: ABS, NHFIC

Other economic variables, such as rents, can also affect the rate of household formation. If rents are falling, it increases the purchasing power of incomes for housing services. This allows more people to live on their own, decreasing average household size. Conversely, if rents are rising, fewer people are able to form new households. Inner city areas in Sydney and Melbourne, which are close to universities, saw large falls in asking rents following the onset of COVID-19 and the fall

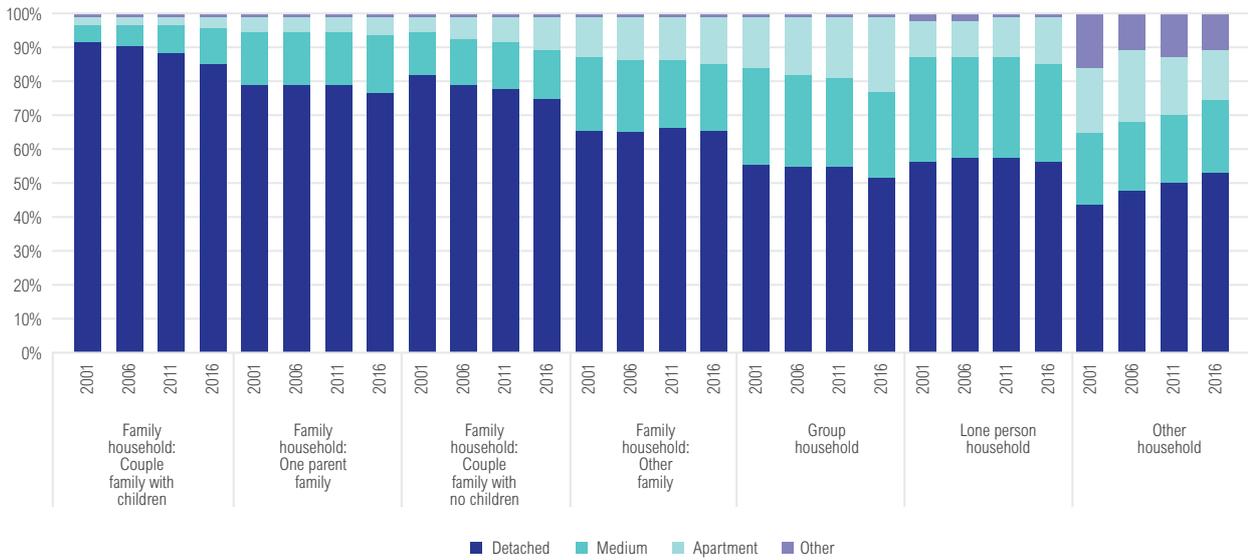
in NOM. But this has now reversed somewhat, suggesting the improved rental affordability and possible attractiveness of smaller household size during the pandemic has attracted some people back into the market (see Figure 2.3). It might also suggest some latent household formation (see below). As outlined in the ‘State of the housing markets’ chapter, the fall in vacancy rates (and rent increases) has also been driven by a withdrawal in rental listings.

Figure 2.3: Rents in Greater Sydney LGAs close to major universities



Source: CoreLogic, NHFC

Figure 2.4: Household and family type by dwelling structure, 2001–2016 – Australia



Source: ABS, NHFIC

### Housing preferences

As people move through life they have different preferences for different types of living arrangements.

Australia continues to be one of the least densely populated countries in the world. More than 80% of couples with children around Australia live in separate houses and detached dwellings.

However, in recent decades preferences have shifted as higher density living has increased in Australia’s major cities. The last few Censuses to 2016 show the most significant shift in dwelling demand has been toward semi-detached and low-rise apartment dwellings.

Household preferences are also affected by affordability and supply factors. The trend shown in Figure 2.4 reflects a combined supply and demand response: the combined expectation of residential developers with the preferences of the buyer/renter market.

A longstanding problem in Australia has been the mismatch between housing preferences and where housing is located. Housing is often concentrated in city outer rings, away from CBDs where most of the jobs are.

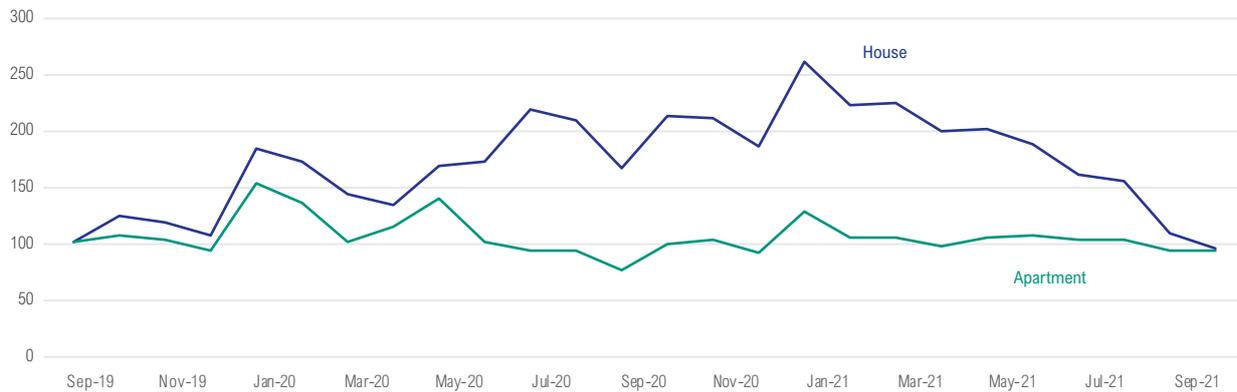
For example, the NSW Productivity Commission has noted that several of the innermost Sydney LGAs, including Woollahra, Randwick, and Mosman, which are close to the CBD are less dense than middle-ring areas such as Burwood and Canada Bay. The report notes only 20 per cent of new dwellings will be built in LGAs within 10 kilometres of the Central Business District<sup>5</sup>. This is despite research suggesting there’s an excess demand for higher density housing in inner Sydney<sup>6</sup>.

The pandemic has likely had an unusually large impact on housing preferences, given targeted stimulus primarily supported detached dwellings, the move towards lower density housing and (relatively inexpensive) properties in regional areas, together with cheaper inner city rental stock.

5 NSW Productivity Commission White Paper, page 269

6 The Apartment Shortage, RBA Research discussion paper, Tulip & Jenner

Figure 2.5: Changing housing search preferences before and during the pandemic



Source: Domain

Many people have been able to work from home, which has led to a stronger preference for larger houses with more bedrooms and more space (Figure 2.5). That said, early indications suggest some of these behaviours may be temporary.

NHFIC liaison also suggests there has been a marked change in preference for larger apartments up the eastern coastal seaboard, including people amalgamating two apartments for more space.

The pandemic has certainly produced a larger than usual increase in people preferring to live in less densely populated areas. A recent NAB survey suggests that up to 85% of people now see consideration of a move to a regional area an important factor when buying a home.<sup>7</sup>

This change in preferences is not unique to Australia. In other OECD countries, the pandemic also increased demand for houses located in areas with larger detached dwellings and more outdoor space.<sup>8</sup>

The stronger desire to live outside major cities has, in turn, likely opened up some more affordable rental stock in inner metropolitan areas. Given the falls in rents, this could have underpinned smaller household sizes in some areas. The 'State of the regions during COVID-19' chapter discusses these issues further.



Many people have been able to work from home, which has led to a stronger preference for larger houses with more bedrooms and more space.

<sup>7</sup> <https://www.news.com.au/finance/real-estate/buying/covid19-pandemic-causes-big-changes-in-house-hunters-preferences-nab-data-reveals/news-story/8c06ee791d8ba22120b8bf6e474e6b14>

<sup>8</sup> [https://ideas.repec.org/p/bdi/opques/qef\\_627\\_21.html](https://ideas.repec.org/p/bdi/opques/qef_627_21.html)

## Box 2:

## Latent household formation

Our State of the Nation's Housing 2020 report showed the falls in NOM due to closed borders generated spikes in vacancy rates and large falls in rents in inner city Sydney and Melbourne.

For example, rents in Sydney fell back to 2014 levels. But over the course of 2021 this was reversing, despite international borders remaining closed. Vacancy rates are now back to pre-pandemic levels in Sydney and Melbourne and rents are experiencing some upward pressure again (albeit off lower levels).

If the new supply coming into the market is outstripping new household formation, all other things being equal, vacancy rates typically remain elevated and rents fall. Conversely, when household formation is stronger than new supply, vacancy rates tend to fall and rents tend to rise.

As Figure 1.10 shows, some vacancy rate falls can be attributed to fewer rental listings, likely due to investors selling properties to first home buyers and other owner occupiers. But this is unlikely to explain all of these changes. The data suggests some latent pre-pandemic household formation could have been occurring over the course of the last year as rents in Sydney and Melbourne became more affordable.

Given latent household growth is difficult to measure, the sharply falling vacancy rates could mean that NHFIC's projections are underestimating recent household formation.

## Household formation during the pandemic

The current rate of household formation is difficult to assess. New household formation continues to be significantly affected by the lack of NOM since the beginning of the pandemic. A range of factors could also have affected the rate of new household formation over the course of 2020–21 and into 2021–22 (see Table 2.2).

- **Second homes** – Largely anecdotal evidence suggests more people have purchased second homes, but, putting a figure on the quantum – and establishing its materiality – is difficult to gauge. If more people buy second homes and leave city dwellings unoccupied it means more households are more spread over the existing housing stock.
- **Renovations** – The pandemic produced an unusually high degree of renovation activity (see 'State of the housing market' chapter). NHFIC liaison suggests that some people are renting second properties for the duration of the renovation, making vacancy rates lower than they otherwise would be.
- **Latent household formation** – Given borders were closed over most of 2020–21 through to late 2021, sharply falling vacancy rates across Sydney and Melbourne suggest some latent household formation could have occurred (see Box 2).

**Table 2.2: Positive and negative influences on new household formation since 2020 report**

Factor	Positive	Negative
Population growth and NOM	-	✓✓
Preference for living in open spaces during pandemic, including second properties	✓	-
Preference for smaller household size during pandemic	✓	-
Latent household formation due to improved rental affordability	✓	-
Lower rents	✓	-
Lower unemployment rate	✓	-
House prices	-	✓

✓✓ Strong ✓ Less strong or unknown impact

## Forecast methodology

### Definitions

This report uses the ABS definitions of dwelling type as the basis for its analysis, as detailed in Table 2.3.

**Table 2.3: Household formation categories**

Housing category	ABS structure dwelling types
<b>Detached</b>	Separate house
<b>Medium</b>	Semi-detached, row or terrace house, townhouse etc. with one storey
	Semi-detached, row or terrace house, townhouse etc. with 2 or more storeys
	Flat or apartment in a 1- or 2-storey block
	Flat or apartment attached to a house
<b>Apartment</b>	Flat or apartment in a 3-storey block
	Flat or apartment in a 4 or more storey block

Source: NHFIC, ABS. Non-private dwellings and other residential buildings have been excluded from the analysis. Non-private dwelling types include hotels, staff quarters, hospitals, hostels, nursing homes, certain types of welfare accommodation (i.e. group homes) and prisons. Other residential dwellings include caravans, houseboats and dwellings attached to commercial buildings.

Estimates for each housing type are then prepared at the national and state level, along with each state and the NT. Capital city forecasts are also produced, but Canberra and the ACT are grouped together.

**Table 2.4: Household formation locations**

Capital cities	Rest of state
Greater Sydney	NSW
Greater Melbourne	Vic
Greater Brisbane	Qld
Greater Adelaide	SA
Greater Perth	WA
Greater Hobart	Tas
Greater Darwin	NT
Canberra/ACT	

Source: NHFIC

### Household formation model

The household formation forecasts are based on estimating the total number of households by type for each year of the projections and for each geographic area, to accommodate the resident demographic. Like population forecasts, they are estimated as of 30 June each year.

The model is not a measure of observed transactions in the market in any one year. In the current period of low population growth, positive market sentiment and considerable home purchases could support higher levels of actual demand for new housing.

Given recent falls in vacancy rates, the model suggests some latent household formation could have occurred after the shock in 2020. However, this is difficult to assess until the 2021 Census data are released. Nonetheless, the household formation approach developed here is of benefit because it incorporates the impacts of some key macroeconomic variables on demand and builds on the work of the former Housing Supply Council.

### Methodology for projecting new household formation

- Population projections are based on data provided by the Centre for Population and are consistent with the population figures in the 2021 Population Statement.
- These projections allocate the forecast population by 5-year age group into family and household living arrangements. This allocation is based on long-term drivers, namely population growth and broader demographic changes. This allocation is done with regard to the past demographic trend identified through Census and calibrated to the Australian Bureau of Statistics' Household and Family Projections, Australia 2016 to 2041 Series I ratios for future living arrangements (which is based on living arrangements fixed to the 2016 Census ratios).
- From the Census data, the ABS provides estimates of propensity for each of the age cohorts in the resident population to form, or belong to, a family or non-family household, or to live in a non-private dwelling. These living arrangements are applied at the state, capital city and regional level to the changing population size and age profile to estimate the number of households each year.
- The number of households by type includes estimates for family households, such as couples with children, couples without children, sole parents and other family households. The number of group households and lone person households is also estimated. The changing trends in the preferences of different household types are applied to provide estimates of trends in demand by dwelling type.

- Finally, the number of dwellings demanded is estimated for each state, capital city and regional area, including by type of dwelling, and aggregated to the national level over the projection period.

Importantly, the model takes into account far more than population forecasts. It considers:

- Changes due to the ageing population, changing average number of children per family household and other compositional changes in the ways people form various living arrangements
- The impact that economic factors can have on people's living conditions including the effect of changes to incomes, rents and unemployment
- An allowance for vacant and unoccupied dwellings due to dwellings that are temporarily vacant, holiday homes, permanently vacant (including abandoned) and used by temporary visitors rather than 'residents'.

### NOM and household formation

The most consequential assumptions for household formation in the model are NOM and the changing age structure of the existing resident population. NOM figures provided by the Centre for Population have been downgraded in the short term but upgraded from 2022–23. These expectations of NOM have worsened/improved since our State of the Nation's Housing 2020 report (Table 2.5).

### Impact of economic variables on household formation

The household formation projections are adjusted by drawing on empirical assessments of how key macroeconomic variables – unemployment, income and rents – affect living arrangements and demand for dwellings.

The following assumptions have been made to estimate household formation and are broadly in line with the Mid-Year Economic and Fiscal Outlook (MYEFO) budget estimates:

- The unemployment rate was expected to be at 7.25% in June 2021, before steadily falling to a plateau of 5% in June 2026 in our last report. But with unemployment now around 4.25% – much lower than anticipated – and projected to remain at this level by 2023, this will provide a more substantial boost to household formation in the short term.
- Following the significant boost to incomes from JobKeeper in 2019–20, in 2020–21 and 2021–22 the boost to income reverses. From 2022–23 it returns to growth and, compared with our last report and reflecting lower unemployment (stronger demand for labour), wages and incomes are now projected to show higher growth in real terms.
- Rents fell sharply in real terms in 2020–21 but, while the story is quite varied across markets, in line with stronger economic conditions and reflecting internal migration in response to COVID, rents have returned to positive growth in 2021–22 (on average). Going forward, rents are expected to continue showing rises broadly in line with historical trends but, with incomes also rising, affordability could improve modestly (on average) which would be positive for household formation.

Table 2.5: NOM – 2020 versus 2021 assumptions

	2020 report	2021 report	Change
2020–21	-72,000	-100,500	-28,500
2021–22	-22,000	-40,900	-18,900
2022–23	95,900	180,100	84,100
2023–24	201,100	212,600	11,500

Source: NHFIC, Centre for Population

## Household formation projections

The population shock is still influencing rates of new household formation, but this is expected to reverse strongly over the course of the next few years. New household formation is expected to remain low at around 60,000 in 2021–22, but then rise strongly to 182,000 in 2024–25 and then settle at around 175,000 to 180,000 new households a year.

As international borders reopen and NOM resumes, new household formation will recover over the coming years, climbing back towards pre-pandemic levels.

The fall in NOM had a stronger adverse effect on the multi-unit market given the drop off in migrants and students. As NOM rebounds, new household formation for multi-unit dwellings is expected to get back to close to pre-pandemic levels over the next 3 years.

When assessing these projections, it is important to distinguish between expected household formation and demand. People typically purchase detached dwellings when they are already renting, which means most purchases of new detached stock do not necessarily result in a new additional household forming. While household formation for detached dwellings is expected to gradually recover after falling to 26,000 dwellings in 2021–22, given the current low interest rates, demand for (particularly detached) dwellings is likely to remain strong.

The household formation projections also include a breakdown of dwellings by household and family group. This shows that of the 1.7 million plus new households expected to form from 2022 to 2032, the strongest growth is expected to be from lone person households at 595,000 (or over a third of all new households) (See appendix).

**Table 2.6 Expected household formation**

	2020–21	2021–22	2022–23	2023–24	2024–25	2025–26
<b>2020–21 forecasts</b>	54,200	91,600	144,700	178,800	175,300	na
<b>2021–22 forecasts</b>	103,300	60,400	158,600	166,600	181,500	177,800

Source: Macroplan, NHFIC. (e) net estimate using actual completions less estimated demolitions.

**Table 2.7 Expected household formation by dwelling type**

	2020–21	2021–22	2022–23	2023–24	2024–25	2025–26
<b>Detached</b>	56,100	25,900	92,100	95,100	105,200	100,900
<b>Medium density and apartments</b>	49,400	37,200	68,600	73,900	78,500	79,100
<b>Other</b>	-2,200	-2,700	-2,100	-2,400	-2,200	-2,200
<b>Total</b>	<b>103,300</b>	<b>60,400</b>	<b>158,600</b>	<b>166,600</b>	<b>181,500</b>	<b>177,800</b>

Source: Macroplan, NHFIC. (e) net estimate using actual completions less estimated demolitions.  
NB: Numbers may not add due to rounding

## Sensitivity analysis

Table 2.8: New household formation

	2020–21	2021–22	2022–23	2023–24	2024–25	2025–26
<b>Net Overseas Migration (NOM base)</b>	-100,500	-40,900	180,100	212,600	235,000	235,000
Household formation (central forecast)	103,300	60,400	158,600	166,600	181,500	177,800
<b>Net Overseas Migration (upside scenario)</b>	-100,500	78,500	235,000	235,000	235,000	235,000
Impact on household formation (relative to base)	-	50,600	24,600	11,300	2,700	2,400
<b>Net Overseas Migration (downside scenario)</b>	-100,500	-77,400	95,900	201,100	235,000	235,000
Impact on household formation (relative to base)	-	-15,500	-35,900	-6,300	-1,800	-1,300

Source: Macropian, NHFIC.

The Centre for Population has updated its NOM forecast by 132,000 from 2022 to 2024 due to high vaccination take up rates and a substantial relaxation of international border restrictions earlier and faster than envisaged at the 2021–22 Budget.

But the pace of the recovery of NOM will remain highly uncertain due to the unpredictability of COVID-19 and measures to contain it, together with the desire of people migrating as international borders are relaxed. Given this uncertainty, additional household formation scenarios are provided based on the Centre for Population's NOM upside and downside case scenarios.

The scenarios show that under an upside NOM scenario, its expected net new household formation would be 92,000 higher to 2025–26 relative to the central forecast. Under a downside scenario, its expected household formation would be 61,000 lower to 2025–26 relative to the central forecast.