

# EXECUTIVE SUMMARY

## Key points

- COVID-19 is expected to cause the largest negative shock to population growth since early last century, with almost one million fewer people (than previously) expected to be living in Australia by 2025. This will see new demand for housing fall by 286,000 dwellings between 2020 and 2025, compared with the pre-crisis outlook.
- The housing demand shock is large and unprecedented with the biggest impact to be felt in the apartment and rental segments. But the lower growth of new housing demand is likely to be temporary. From 2023 to 2025 on the back of a strengthening economy and a return to normalisation of Australia's migration program, new demand is expected to exceed new supply.
- Federal and state government stimulus is supporting supply by encouraging construction activity in the short term but the lower new demand for housing weighs on construction over the medium to longer term, with net additions likely to fall and then recover to around 148,000 in 2025. Weakness in net apartment additions will extend to 2025, when just 27,000 new dwellings are expected, similar to levels seen prior to the apartment boom.
- The demand shock will leave the housing market with new supply exceeding new demand for the next two years. We expect new supply to exceed new demand by around 127,000 dwellings in 2021 and 68,000 dwellings in 2022. Cumulative new supply is expected to be around 93,000 higher than new demand by the end of the projection period in 2025, after demand rebounds in 2023.
- This shorter-term period where new supply exceeds new demand can be seen as partial catch-up for much longer more protracted periods of undersupply. After a prolonged period of undersupply in the 2000s, there was a significant (albeit lagged) supply response in the period prior to COVID-19, but construction levels were the bare minimum to keep supply and demand broadly in balance.
- The projections in this report are sensitive to assumptions for net overseas migration (NOM) and population growth. Sensitivity analysis shows that under slightly more optimistic population assumptions, cumulative projected excess supply over the projection period halves from around 93,000 to 46,000 dwellings.
- If vaccines are forthcoming earlier than expected, resulting in international borders opening sooner and more Australians returning home, together with potential supply constraints, we would anticipate any cumulative excess supply over a medium-to-longer term horizon to be negligible.
- With new supply expected to exceed new demand over the near term, it is likely to put downward pressure on rents in Sydney and Melbourne where vacancy rates are higher. This could improve overall rental affordability, although the real impact will differ across geographies and household income distributions. Also, the impact of COVID-19 is disproportionately affecting industries where employees are more likely to be renting.
- Longer term trends of declining affordability, particularly for low-income households in the private rental market and the ability for prospective first home buyers to transition to home ownership are likely to persist, particularly if supply is not responsive to demand when it recovers.
- A lower period of housing demand due to the global pandemic presents an opportunity to reset policy frameworks to ensure that actual planning policies can accommodate future population growth without adverse consequences for affordability.



The focus of  
this report is on  
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in both supply  
and demand for  
housing.

## Introduction

# COVID-19 has brought an unprecedented negative shock to new demand for Australian housing, mainly via international and domestic border closures.

This has left some capital city rental markets oversupplied relative to the collapse in new demand and this is currently putting downward pressure on rents. The pandemic and uncertainty about the general economic outlook and employment has, at times, weighed on the broader housing market and affected the decision-making process of households in their purchase of property and developers in providing new supply to the market.

Despite these substantial headwinds, construction activity and house prices are holding up relatively well on the back of government and central bank stimulus, and pent up demand in jurisdictions that have successfully contained the virus. The private sector via banks and utility companies are also doing their part to support the recovery.

- The Federal Government eased fiscal policy taking the budget position from a forecast surplus of 0.3 per cent of GDP for FY20 at Mid-Year Economic and Fiscal Outlook to a deficit of 4.3 per cent of GDP in the same year and 11 per cent of GDP in FY21. There is already evidence that the Homebuilder program is supporting demand for detached dwellings. Furthermore, the JobKeeper program is continuing to provide vital support to the construction industry and the economy more broadly, with the construction industry the largest recipient of JobKeeper payments.
- Concessions on stamp duty for first home buyers purchasing a newly constructed dwelling has been extended in NSW. In Tasmania, stamp duty concession for first home buyers purchasing an established dwelling are introduced and concessions were also available for pensioners downsizing. WA introduced stamp duty relief late in 2019 and decided to extend this relief in response to the pandemic. WA also introduced a Building Bonus grant in June 2020. In the ACT, concessions were introduced for all home purchasers of detached homes, off-the-plan units and townhouses.

- Land tax relief was provided in New South Wales, Victoria, Queensland, South Australia, and Tasmania for those landlords with tenants impacted by income loss during the pandemic.
- The RBA eased monetary policy in March and again in November. By the end of November, the target cash rate was set at 0.1 per cent and similarly the yield target on the 3-year bond of 0.1 per cent. The bank also established a term funding facility for banks and other depository institutions to provide them with access to low-cost funding. At the November board meeting, a \$A100bn bond purchasing program was also introduced.
- The banks and utility companies have also provided households with support in 2020, with mortgage payment and service payment deferrals providing key support to both households and small business.

The short term period where supply runs ahead of new demand in our projections owing to the COVID-19 induced demand shock also needs to be considered in a broader historical context. Previous work undertaken by the former National Housing Supply Council (2011) estimated that in 2010 due to long and protracted periods where supply was inadequate to match demand, there had been a cumulative undersupply of housing of around 200,000 dwellings. And while Australia entered COVID-19 after a significant period of strong supply, construction levels were the bare minimum to keep supply and demand broadly in balance. Against that backdrop, the projections for supply to outpace demand over the next two years can be seen as partial catch up for longer more protracted periods of undersupply.

Moreover, the magnitude of the projected excess supply is relatively small, and could be negligible, particularly given that demand could surprise on the upside.

## Outline of the report

The focus of this report is on the path of recovery in both supply and demand for housing. This largely depends on the path of the COVID-19 virus, the reopening of international borders and broader economic recovery.

Control of the virus will clearly lead to fewer restrictions in the movement of people within Australia, a stronger economy and a solid, but not full, recovery in the demand for housing.

The Australian Bureau of Statistics Lending Indicators release provides a series on lending commitments for the established dwelling markets in each state, which provides a reasonably good snapshot.

Commitments were recovering during 2019 on the back of easier monetary and macro-prudential policy, but the spread of the virus caused a sharp drop between March and May in most states (Figure 1.1). The policy response has driven a strong rebound since then, with lending commitments increasing in each state and territory.

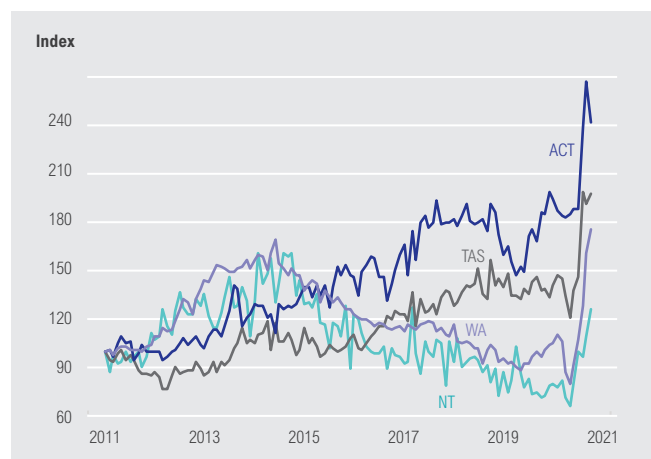
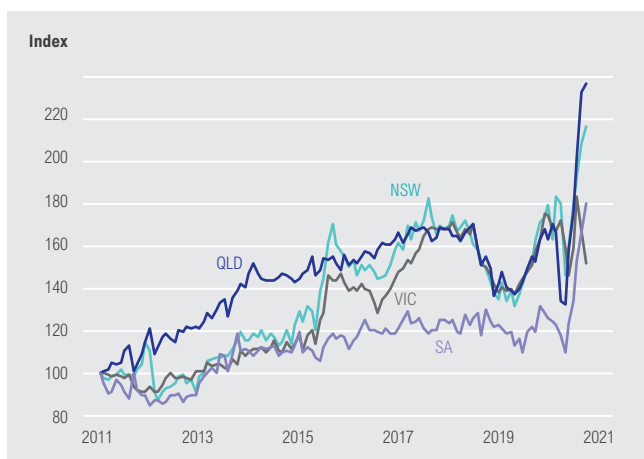
Open international borders have supported Australia's population growth model based around strong net overseas migration. However, their closure has effectively turned this model on its head representing a major challenge for policymakers. The 2020 Federal Budget forecasts negative net overseas migration in both FY21 and FY22 before a rebound in FY23. This means the anticipated excess supply and pressure on the rental markets, particularly in the large eastern state capital cities, will remain for some time.

A resurgence of case numbers, similar to that seen in Victoria during the September quarter, will clearly be a major setback, should it occur.

Over the longer term, COVID-19 has the potential to change the way we work and live.

Recent reports suggest around 40–60 per cent of the working population are still working from home. Early indications also suggest that demand has shifted away from inner-city dwellings to regional centres. But it will likely be some time before it will be clear whether COVID-19 induced working from home patterns and the recent uptick in more people choosing to move to the regions will endure. If these work arrangements become more permanent, the gap between housing affordability in the capital cities and the regions may narrow.

**Figure 1.1: Owner-occupier Lending Commitments (January 2011=100)\***



Source: ABS Cat No. 5601.0. \* value of lending commitments excluding refinancing

Housing preferences may also change due to COVID-19. The design of our dwellings may need to incorporate a home office if working from home becomes a necessity.

Workers in the CBD may also be more willing to live on the urban fringe within capital cities or further away from their place of work. These changes could then affect the distribution of demand for infrastructure within cities. Companies may also decentralise away from the CBD, which would enable people to work closer to home.

The development industry can have a delayed response to movements in underlying demand. In part, this reflects changing financial conditions and the nature of the industry, but it also reflects delays and costs associated with the planning system. This varies between states, but our industry liaison indicates NSW generally has the largest impediments.

Adding to this weight of evidence, the NSW Productivity Commission's recently released Green Paper indicated the average time taken for processing development applications in NSW was significantly longer than in other states for all development types.<sup>1</sup>

- For medium-density housing developments, development application determinations take an average of 200 days in New South Wales compared with 70 days to 105 days in other jurisdictions.
- In high-density housing developments (assessed by councils) development application determinations take an average of 190 days vs an average of 105 business days for other jurisdictions.
- In greenfield sub-divisions they take 130 days on average compared with 100 days in the second slowest state (Queensland).

This report contains four chapters, with Chapter 1 outlining the outlook for the demand for housing and Chapter 2 providing projections for supply. In Chapter 3, we bring together the interaction of both supply and demand.

The supply and demand outlook are detailed for Australia, capital cities and rest of state for each state and territory.

In Chapter 4, housing affordability is analysed by looking at social and affordable housing, the private rental market and first home buyers rather than just looking at the housing market in aggregate. Housing as a service is a vital requirement for all Australians, with around one-third of all households renting. Consequently, affordability at the bottom end of the rental market and in the rental market more broadly is important and is where the equity implications of housing affordability are more marked. The size of the financial step between housing as a service, and housing as both a service and financial asset, is also an important consideration.

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1 New South Wales Commissioner for Productivity (2020) [Productivity Commission Green Paper: Continuing the productivity conversation](#).

## Demand

- Over the period 2020 to 2025 (inclusive), the COVID-19-induced shock will see new demand for housing fall by a total of 286,000 dwellings relative to the pre-crisis outlook, with the impact largely felt in Australia's rental markets over the short to medium term.
- The projections show new demand for housing falling sharply in 2021 and 2022 from pre-COVID levels of 176,300 and 186,900 to post-COVID levels of 54,200 and 91,600 respectively, mainly due to the sharp falls in net overseas migration (NOM).
- The sharp fall in new demand is being felt largely in the rental housing segment given the composition of NOM, particularly lower demand from international students, and that households most affected by the recent rise in unemployment are more likely to be renters. Lower interest rates and government stimulus are also encouraging renters to buy, given mortgage costs are more on par with renting in some locations.
- From 2023, on the back of positive NOM and a strengthening economy, housing demand will lift to 144,700 dwellings in 2023 and move back close to pre-COVID levels to around 178,800 dwellings in 2024.
- New housing demand is extremely sensitive to changes in population growth and Australia's migration intake. Sensitivity analysis shows that under a slightly more optimistic scenario where NOM is negative in 2021 but recovers earlier and returns positive in 2022, this would boost new demand for dwellings by around 86,000 dwellings over the period to 2025.
- The projections indicate lone households with residents aged 70+ will grow strongly (+23 per cent) over the period 2019 to 2025, and couples without children are expected to also grow strongly over the same period (+9 per cent).
- Demand for detached and medium-density dwellings will recover to pre-crisis levels by 2024, while demand for apartments will fall to around 16,200 dwellings in 2021 before gradually recovering to around 31,700 in 2025, still well below pre-crisis demand (47,600 in 2019).

## Supply

- A recovery in construction activity from the COVID-19 recession is underway, led by detached housing. We expect total net additions to rise to 181,000 in 2021 from 170,000 in 2020 on the back of the monetary and fiscal stimulus put into place this year.
- In 2022, some withdrawal of fiscal stimulus seems likely to make room for a recovery in parts of the economy most affected during the COVID-19 recession. Over the longer term, the lower population growth outlook highlighted in the demand chapter will weigh on construction, with net additions likely to be only 148,000 in 2025.
- The detached housing market is clearly responding to the fiscal and monetary stimulus and we expect net additions to rise to 108,000 in 2021 from 90,000 in 2020. However, the withdrawal of stimulus and relatively weak population growth outlook means that by 2025 net new detached housing additions are likely to be only 97,000.
- The downturn has weighed more on apartments than detached or medium-density dwellings because of international border closures. Furthermore, federal and state government stimulus packages thus far have been more targeted towards the detached dwellings. We expect net apartment additions to fall to 45,000 in 2021 from 55,000 in 2020.
- Lower population growth means that net additions for new apartments in 2023 are likely to be 58 per cent below those seen just prior to the COVID-19 recession. Even by 2025, we still expect them to be 51 per cent below this benchmark and only 27,000 dwellings, levels last seen prior to the apartment boom. But net additions to the apartment market were already 15 per cent below their peak before the COVID-19 recession.
- More positively, credit availability doesn't appear to be limiting construction activity, with lending to developers broadly tracking building approvals. However, credit could tighten in pockets such as capital city CBD apartment markets if growth in NOM remains sluggish.
- The State of Housing Supply-Demand Balance Chapter brings both supply and demand together, with the net supply and demand balance having implications for rental price pressures and vacancy rates.

## Affordability

- There is likely to be downward pressure on rents (on average) in Sydney and Melbourne which could improve overall rental affordability in the short term—but the impact of COVID-19 is disproportionately affecting industries where employees are more likely to be renting.
- Lower income households in the private rental market are more vulnerable to rental stress. The proportion of private renters in the bottom two income quintiles spending more than 30 per cent of their disposable income on housing costs has increased almost 10 percentage points since 2008.
- As a result of rents being set as a fixed proportion of income, affordability for state social housing tenants have mostly been unaffected by the pandemic. However, given the pandemic's impact on jobs and the wider economy, it is likely the significant existing waitlists for state social housing will increase.
- First home buyers have been taking advantage of the recent softness in dwelling prices, low interest rates and government stimulus, accounting for more than 40 per cent of total new housing loans—10 percentage points higher than the long-term average.
- Over the longer term, NHFIC's projections see housing demand bouncing back and will exceed housing supply between 2023 and 2025. Affordability for renters and prospective first home buyers could deteriorate if supply is not responsive to the strong rebound in demand.