HIA Housing Forecasts

Summary

Record Year of Home Building

Australia may not have managed the pandemic perfectly, but we are in a much better position than most economies. This will be important as it will assist Australia's ability to attract skilled migrants when international travel restrictions are eased.

Typically recessions cause lingering impacts on the economy and households. The impact of the 1990s recession was observed in the income and employment prospects of young workers for a decade. This economic recovery is unique due to its speed. A rapid return to economic growth minimises the long-term adverse impacts on employment, the participation rate and wage growth.

The residential building industry was also fortunate to experience less interruption throughout 2020 than many other industries. The ability to continue to operate as well as the incentives provided through HomeBuilder and other measures have produced a boom in detached home building.

Many leading indicators have reached record levels following the growth in demand for detached housing that followed the announcement of HomeBuilder in June 2020. New Home Sales peaked in the December 2020 quarter to be almost 100 per cent higher than for the same period the year before. A record quarter of loan approvals was also observed in the December quarter of 2020. Finally, building approvals are now starting to reflect this surge in demand for detached homes and will continue to increase in coming months as this exceptionally large flow of work enters the pipeline.

Access to finance was a major constraint on activity in recent years but this challenge appears to have eased and mortgage arrears is starting to return to pre-pandemic levels.

First home buyers have responded rapidly and account for 43 per cent of loans, the highest rate since the post-GFC stimulus measures. They not only accessed HomeBuilder grants, they also benefited from the National Housing Finance Investment Corporation guarantees, state government grants and a brief reprieve from house price growth.

Investor activity was very low in 2020 but they are starting to return as rapid rental price growth pulls them back to the market. Investors will be important for continuing demand for new homes once the HomeBuilder incentives end.

All this indicates a very strong level of new detached home construction through 2021 and into the first half of 2022.

There is, however, a dark shadow that sits behind HomeBuilder.

The lingering effects of this recession on home building will be due to the change in the rate of population growth and the geographic shifts in population. The impact of the cessation of overseas migration will eventually impact detached housing in the same way it has impacted multi-units.

There has also been a rapid demographic shift away from inner city living as commuting to the office becomes less frequent. School leavers have also remained in regional areas, rather than being attracted to cities for employment and education, adding to the increase in population across most of the country. A change in consumer preference toward lower density detached housing is also partly due to families seeking additional work-from-home spaces.

HomeBuilder and low interest rates facilitated this shifting of population away from Sydney and Melbourne. This has exacerbated the loss of overseas migration on these cities. The south east corner of Queensland, South Australia and Western Australia appear to be the beneficiaries of this demographic shift which has partially offset the loss of overseas migration.

Evidence of this geographic shift can be seen in the exceptionally tight rental market that exists across the country. New home building will not meet the increase in demand in the short term.

The exception to this tight market is the growth in the availability of units in Sydney and Melbourne. Rental vacancies in most cities have fallen below 1 per cent, the effective floor, as there are more renters than properties. This is also a driver behind the rapid house price growth.

A challenge for forecasting in the years ahead is determining if, when and how quickly the population will return to the multi-unit market in Sydney and Melbourne. This will partly be determined by businesses embracing working-from-home arrangements, once the world returns to 'normal'.

It is likely that much of the shift in population will be permanent, particularly from retirees. Some of the two years of school leavers that have remained in the regions will also have established households and careers and remain in the regions. When 'normal' does return, however, young students and workers will once again move to employment centres in capital cities. The urbanisation trend has occurred for centuries as higher wages attract workers and it will return when international travel restrictions ease. This could leave many regions that are currently experiencing an uncharacteristically strong economy, in a demand shadow.

The combination of the restrictions on migration, the post-HomeBuilder slump and changes in demographics are expected to lead to a decline in new home construction from 2022 and leaves a very pessimistic outlook for home building in 2023. An increase in interest rates is also possible from 2023 onwards and as was observed after the GFC, this will have an immediate adverse impact on housing.

Of course, the variables that will impact on housing demand in 2023 are significantly larger than usual for both the upside and the downside. The key policy decisions impacting this outlook is when and how quickly overseas migration will return to pre-pandemic levels.

We have a particularly pessimistic outlook for Victoria given their reliance on overseas migration to drive economic growth over the past decade. Evidence to date is that Victoria has also seen interstate migration decrease which will exacerbate this shortfall. Victoria is also very reliant on the construction sector as its employment base and as this slows, it will impede an economic recovery.

In this Outlook we are assuming overseas migration recommences in 2022 but does not return to pre-pandemic levels until the end of 2024. We also assume intrastate and interstate migration is once again able to occur unconstrained.

Detached starts rose to 27,173 in the September 2020 quarter, up by 4.8 per cent from the 25,936 recorded in the June 2020 quarter. These gains were relatively broad-based, with quarterly increases occurring in New South Wales, Victoria, South Australia, Tasmania and the Northern Territory. We forecast a national increase of 15.0 per cent in the December quarter on the back of the HomeBuilder stimulus, to 31,246, and will sustain this strong level for 12 months. This level of activity has not been seen since the single March 2000 quarter preceding the introduction of the GST.

In financial year terms, this will bring detached starts from 102,185 in 2019/20, up by 24.4 per cent to 127,143 in 2020/21 – the strongest 12 months for detached dwellings since 1994 – before declining back to 90,787 over the following two years to 2022/23, a level last seen in 2011/12.

Multi-unit starts declined by 7.2 per cent from 16,643 in the June 2020 quarter to 15,451 in the September 2020 quarter. Western Australia was the only jurisdiction to see an increase in this quarter. We forecast starts to bounce back slightly in the December 2020 quarter, up by 2.5 per cent to 15,842 before heading back down towards a late-2021 trough that will mark the weakest performance for this sector since 2012.

In financial year terms, multi-unit starts are forecast to decline by 15.7 per cent from 69,294 in 2019/20 to 58,416 in 2020/21, reaching a financial year trough of 50,619 in 2021/22 – the weakest year since 2009.

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