BUILDING THE GOOD LIFE

RAI Discussion Paper: Meeting the demand for regional housing

REGIONAL AUSTRALIA INSTITUTE

Huggins Lookout, Bright, Victoria

ABOUT THE REGIONAL AUSTRALIA INSTITUTE

Independent and informed by both research and ongoing dialogue with the community, the Regional Australia Institute (RAI) develops policy and advocates for change to build a stronger economy and better quality of life in regional Australia – for the benefit of all Australians. The RAI was established with support from the Australian Government.

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REFERENCE

This report can be referenced as:

Hopkins, D., and Houghton, K. 2021, Building the Good Life: Meeting the Demand for Regional Housing, RAI Discussion Paper, The Regional Australia Institute, Canberra.

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SUMMARY

Regional Australia is seeing a surge of popularity. City-dwellers are moving to the regions and regional people are choosing to stay. Regional Australia offers the Good Life where community is strong, jobs are plentiful and housing – while currently under pressure – is still much more affordable and accessible than in the major capitals.

This discussion paper describes the current pressures across regional housing markets and the structural and cyclical drivers of these pressures. It outlines areas where policy should be considered and developed to support crucial additional (and appropriate) housing supply. The paper aims to lead and inform discussion among policy makers, industry participants and regional stakeholders to bring about action to restore balance in regional housing and boost supply. It is the beginning of RAI's deeper research into regional housing markets with research partner, UniSA. The overall research will delve more closely into regional housing literature and policy and develop a typology of regional housing markets to inform more detailed place-based responses.

Current pressures in housing markets are almost universal across regional Australia – in both rental markets and purchase markets. While these pressures are partly driven by cyclical and macroeconomic factors (largely stemming from the COVID-19 pandemic), they are underscored by a shortage of regional housing. That is, over the long term, regional home building has not kept pace with population growth. Regional Australia's population grew by an average of 76,500 people per annum in the decade to 2020. The number of homes approved for construction declined in five out of those 10 years. Supply has generally been meaningfully boosted only when federal governments have offered major housing stimulus. In that respect, the latest stimulus – HomeBuilder – has been especially important for regional areas.

The shortage in regional housing is constraining local economic growth and development, preventing regions from meeting their full potential and contributing to the post-COVID recovery. There are jobs going unfilled simply due to a lack of suitable housing. Local private enterprise is constrained in realising nascent opportunities and creating new jobs because of local shortfalls in the amount and mix of housing.

Communities are responding to meet their local needs for additional and more diverse housing. In Dubbo, apartment presales are currently underway in a 13-storey mixed-use development, No. 1 Church Street, while the majority of housing coming online in Wollongong and Newcastle over the past five years has been non-detached housing. In Port Hedland, a partnership between the Western Australian Government and a construction firm led to the provision of 293 apartments for key workers. Smaller inland local governments are also taking innovative steps. Temora Shire Council in New South Wales, for example, is explicitly seeking to free up local flexible zones for mixed-use and medium-density housing.

Regions, as always, are responding with local initiatives. But all levels of government need to address structural barriers, and industry has a role to play too. These structural barriers to home building in the regions are the key drivers of the long-term shortfall in housing. In seeking to understand (and thereby pave the way to address) these barriers to regional housing supply, this paper breaks down regional housing markets into two broad types, requiring different responses – noting that a more detailed typology is currently being developed under RAI's research program.

Regional Australia offers the Good Life where community is strong, jobs are plentiful and housing – while currently under pressure – is still much more affordable and accessible than in the major capitals.

In the first instance, there are high-growth regions where the barriers to home building are quite traditional – strong demand has run up against supply that is not adequately responsive due to issues with bringing shovel-ready land to market that will see the right mix of new housing added to local stocks. Housing supply levers in relation to planning (including planning controls), the provision of infrastructure, and incentives for development need to be set not only to ensure an appropriate volume of housing supply, but also an appropriate mix of dwelling types at appropriate (affordable) price points. In practice, these are a mix of public and private issues. Some high-growth regional places have plentiful supply of suitable land, but the pace and mix of development is inadequate.

Housing shortages are present not only in high-growth regions but right through to smaller (typically inland) areas where population growth has been minimal, if not negative. In this second type of regional housing market, activity has stalled because of the small scale of these markets and because local households face constrained access to housing finance. These regions also face issues with the overall quality of local stocks, again due largely to constrained access to finance. The RAI estimates this issue affects at least 20 per cent of regional (mainly inland) local government areas (LGAs). These LGAs aren't limited to just small and/or remote settings, but are a diverse set including Mount Isa and Rockhampton in Queensland, Glen Innes and Snowy Valley in NSW and West Wimmera and Pyrenees in Victoria. The key policy consideration here is how to address the underlying issue of constrained access to finance. The RAI's suggestion is to broaden existing government housing guarantees that aim to address similar problems.

House construction Mackay, Queensland

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POPULATION

Regional Australia has long been a desirable place to live. Over the past decade more capital-city people have been moving to regional areas than have moved in the other direction, as documented in the RAI's Big Movers report. COVID-19 has amplified this trend, particularly in relation to regional people choosing to stay in place. Since the pandemic, even fewer regional people have been moving to capitals.

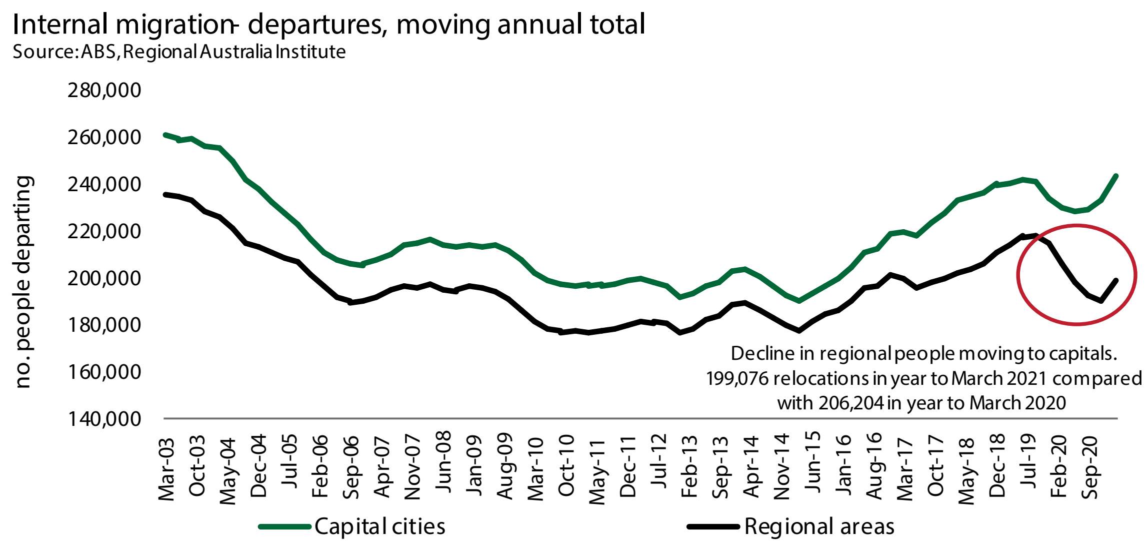
Key drivers of this movement – especially in this time of the pandemic – which are explored in more detail in this paper, are strong demand for labour and the affordability of housing in regional markets compared with the major capitals.

The latest population trends and dynamics are having a potent effect on regional housing markets. In particular, with more regional people staying in place, fewer homes are being listed for sale and vacated for rent, while demand for this limited stock has risen. Regional housing stocks were already lagging behind population growth and the pressures are being felt across many and varying regional communities, manifested in surging housing prices and very tight rental markets.

The key policy consideration here – for both local and state governments – is population growth forecasts and government roles in preparing for, and resourcing, anticipated population growth and the associated infrastructure and services.

Most state government planning departments are currently reviewing their population projections and this is timely. Widespread feedback to the RAI is that population projections for regional areas have frequently undershot actual population growth, leaving communities ill-prepared for the population growth that actually occurs.

At a regional and local government level, the policy consideration goes to scenario planning. Regional and local planning should include scenarios (and their implications) for higher and lower rates of population growth. There are examples of local governments that actively consider high-growth scenarios in their local plans. In particular, policy makers and planners at the local level should consider the pipeline of actions needed to cope with higher-than-usual housing demand and population growth.



POLICY CONSIDERATIONS

It is timely that state and local governments review regional and local population forecasts, and look to include high-growth scenarios

BACKGROUND

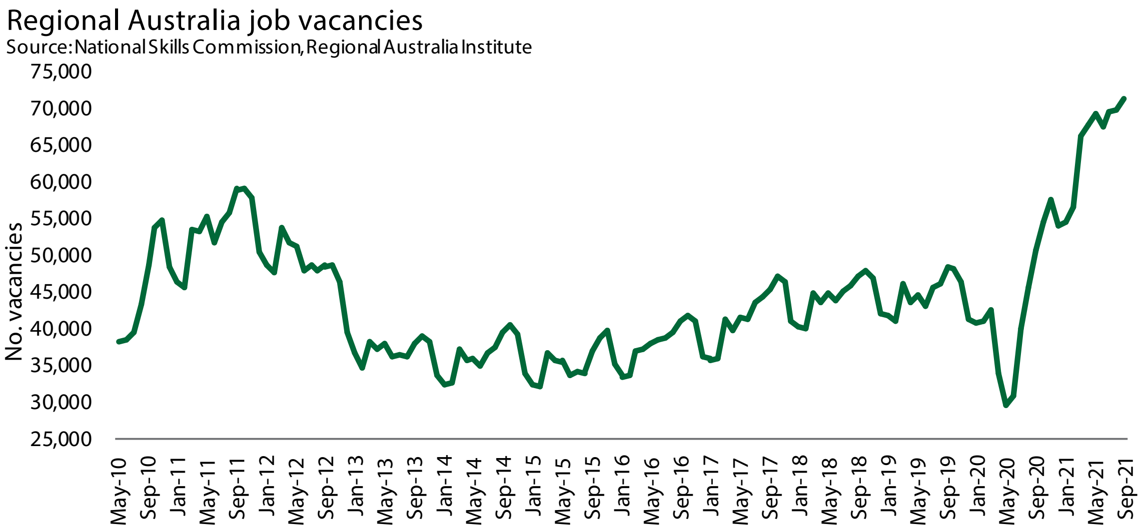
RECORD JOB OPPORTUNITIES

Record job opportunities due to improving economic conditions is a key attraction of regional areas.

Regional job vacancies were already gathering momentum prior to the pandemic and in March 2021 surpassed the previous record (associated with the mining-construction boom). Latest data show a fresh record in October – more than 74,000 jobs advertised. These job vacancies are widespread across the regional areas of all states and territories and across different occupations. Professional workers and skilled tradespeople are in especially high demand. This is very different to the last period of high regional labour demand (2011-2012), when the large number of job ads reflected the country's then two-speed economy – vacancies were narrowly based across the resources sector and states (mainly Queensland, Western Australia and the Northern Territory).

The widespread uptake of working from home since the onset of the pandemic makes a regional move easier still. This change in work patterns is in addition to the record number of existing positions that regional employers need to fill, suggests that there will continue to be a steady flow of workers from cities (and other places) to the regions.

Regional job vacancies were already gathering momentum prior to the pandemic and in March 2021 surpassed the previous record



BACKGROUND

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REGIONAL VS CAPITAL AFFORDABILITY

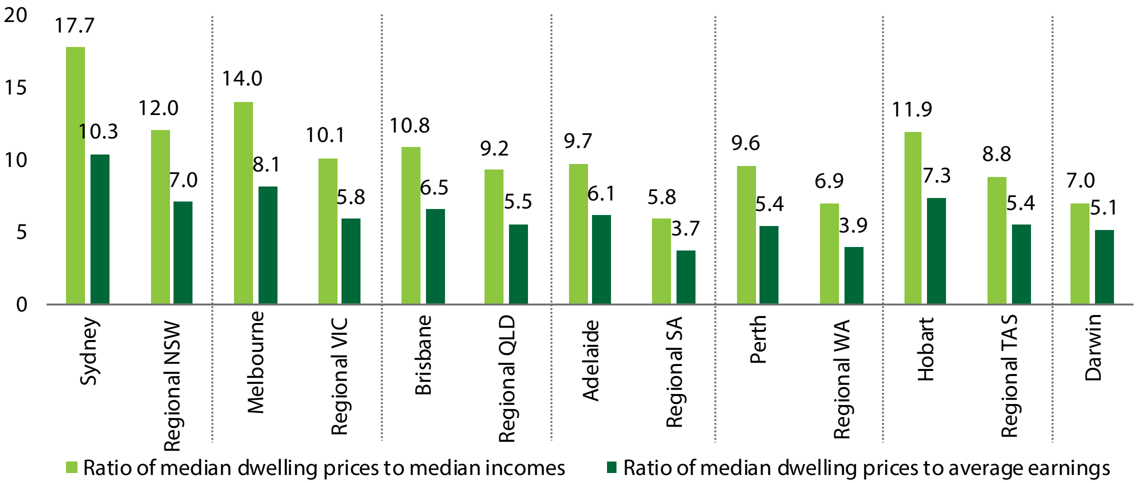
While this paper focuses on the pressures in, and disruption to, regional housing markets, these markets are still much more affordable and accessible than their capital city counterparts.

The chart opposite highlights this, using two slightly different measures of dwelling price to income ratios – the ratio of median dwelling prices to median incomes as well as the ratio of median dwelling prices to average earnings. The latter measure is more commonly reported on, while the former is what RAI's Move Tool assesses. Earnings tend to be higher than incomes, making the ratio lower (and thereby improving the measured level of affordability – a lower ratio indicates better affordability). Incomes – which include non-wage incomes such as any government support payments and superannuation returns for example – are lower than earnings, making the ratio higher. Irrespective of the particular measure used, regional areas are more affordable than the capitals.

For capital-city dwellers moving to regional areas and taking their jobs with them, those price-to-income ratios tend to improve further. That is, the ratio of regional dwelling prices to capital city earnings is lower still, adding to the attractiveness of regional areas to capital-city earners, from the perspective of home ownership.

Estimated Regional vs Capital Affordability, June 2021 – Price to income and price to earnings ratios

Source: ABS, CoreLogic, RAI



BACKGROUND

RENTAL MARKETS

Current rental market pressures are just about universal across regional Australia. Regional vacancy rates have more than halved in each state and territory from what were already tight markets in most states a year earlier. Western Australia is the only state in which the regional rental market could be considered as not tight. The median vacancy rate for regional markets across the other jurisdictions is far below the 3 per cent threshold (anything below this is considered tight).

The vast majority of regional LGAs (where data is available) had tight vacancy rates, and many of these are smaller inland areas:

80 out 86 LGAs in regional NSW – the three tightest LGAs in June 2021 were Edward River (0.14 per cent), Dungog (0.27 per cent) and Greater Hume (0.31 per cent)

All 46 LGAs in regional Victoria – Northern Grampians (0.15 per cent), Swan Hill (0.16 per cent) and Hepburn (0.22 per cent),

32 out of 45 in regional Queensland – the three tightest all had vacancy rates of 0.6 per cent: Charters Towers, Sunshine Coast and Cairns.

22 out of 28 in regional SA – the three tightest were Port Pirie (0.14 per cent), Clare and Gilbert Valleys (0.17 per cent) and Renmark Paringa (0.19 per cent).

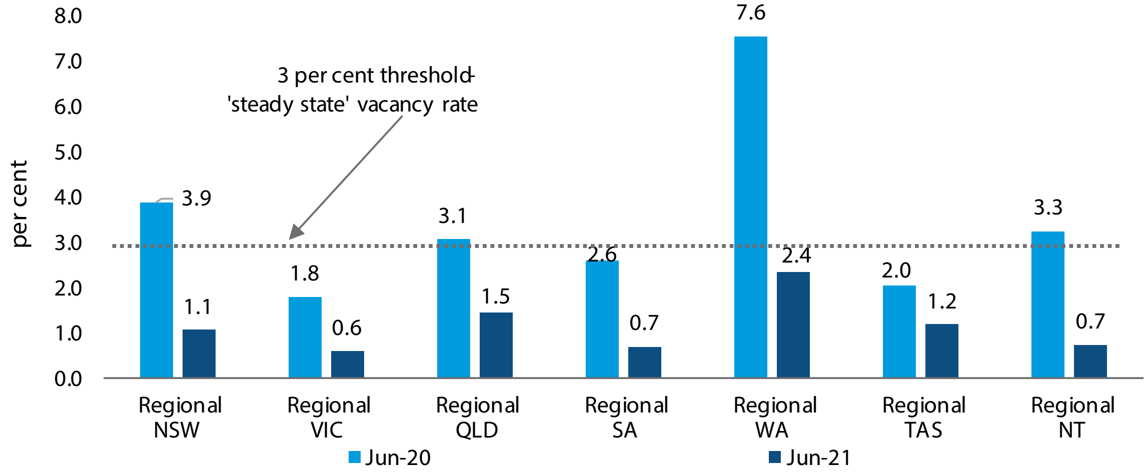
34 out of 58 in regional WA – the three tightest were Esperance (0.35 per cent), Broome (0.41 per cent) and Darandup (0.49 per cent).

18 out of 21 in regional Tasmania – the three tightest were Meander Valley (0.52 per cent) and Derwent Valley and Central Coast, both at 0.59 per cent.

6 out of 7 in regional NT – the three tightest were Litchfield (0.20 per cent), Katherine (0.68 per cent) and Alice Springs (0.71 per cent).

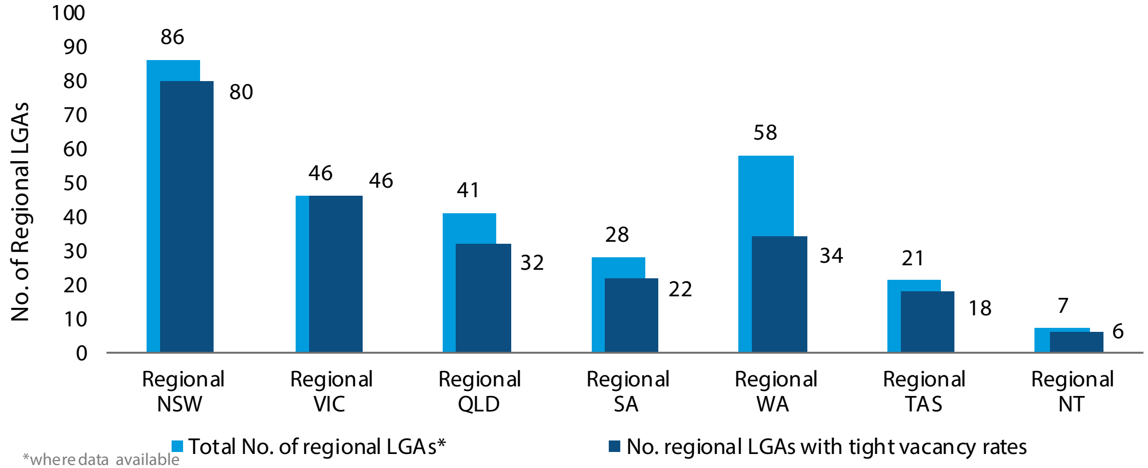
Regional LGA median rental vacancy rates

Source: CoreLogic, Regional Australia Institute



Regional LGAs with tight vacancy rates

Source: CoreLogic, Regional Australia Institute



*where data available

SIGNIFICANT PRESSURES BORNE BY MOST VULNERABLE

A key driver of current rental market pressures is diminishing availability of rental stock. Across regional Australia, rental listings have been declining for a prolonged period – for at least 18 months in most regions.

Prior to the current rental squeeze, regional rental markets had not performed as well as home-purchase markets in relation to affordability. That is, even prior to the effects of the pandemic, rental stress among regional communities was more prevalent than mortgage stress. The pandemic has amplified the issue of regional rental stress significantly.

As noted earlier in this paper, with more regional people staying in place, fewer homes are being listed for rent while demand for this limited stock has risen (in line with more capital-city people moving to the regions). CoreLogic data show the tightest rental markets are generally seeing double-digit growth in annual rental inflation, which would be pushing the most vulnerable – low-income earners who don't qualify for, or can't access, public housing and who rent privately – into housing stress. The RAI has received widespread feedback that it is these members of regional communities who are bearing the brunt of rental market pressures. There are extreme but not uncommon examples of regional people who were previously renting and are having to find emergency or even makeshift accommodation because they could not find an alternative affordable rental property.

The key policy (and program) consideration here – for local governments and local communities more broadly – is the increased need for community and social housing. Several states have recently embarked on programs to expand social housing, including Victoria's Big Housing Build, Queensland's $2.9 billion Social Housing Action Plan, Renewal SA's target of 15 per cent affordable housing and Western Australia's target of a 6 per cent increase in social housing. Nationally, the National Housing Finance and Investment Corporation's (NHFIC) Affordable Housing Bond Aggregator provides low-cost, long-term loans to registered community housing providers to support the provision of more social and affordable housing.[1]

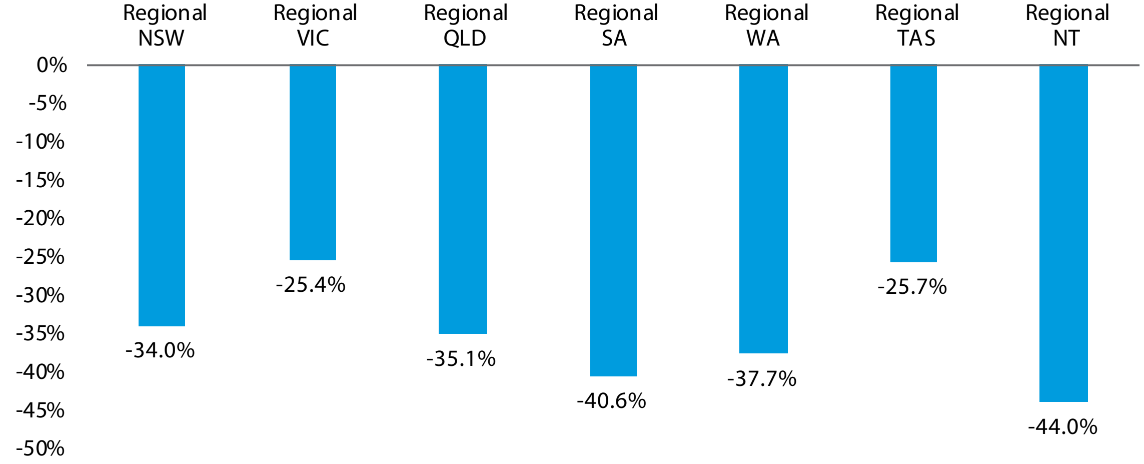
Some communities might find that local rental stress, homelessness and the need for community and social housing are new phenomena. These communities are likely to require further assistance in meeting this need and would also benefit from NHFIC's capacity building program which enables eligible community housing providers to access assistance on finance, business planning, property development and risk management, in and around NHFIC's existing programs.[2]

POLICY CONSIDERATIONS

Local governments and community housing providers should consider accessing NHFIC's affordable housing bond aggregator and its capacity building program to meet increased need for social and community housing

Combined regional LGA rental listings- Jun qtr 2021 vs Jun qtr 2020

Source: CoreLogic, Regional Australia Institute



1. https://www.nhfic.gov.au/what-we-do/affordable-housing-bond-aggregator/
2. https://www.nhfic.gov.au/what-we-do/national-housing-infrastructure-facility/capacity-building-program-grants/

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CURRENT REGIONAL HOUSING PRESSURES

PRICES

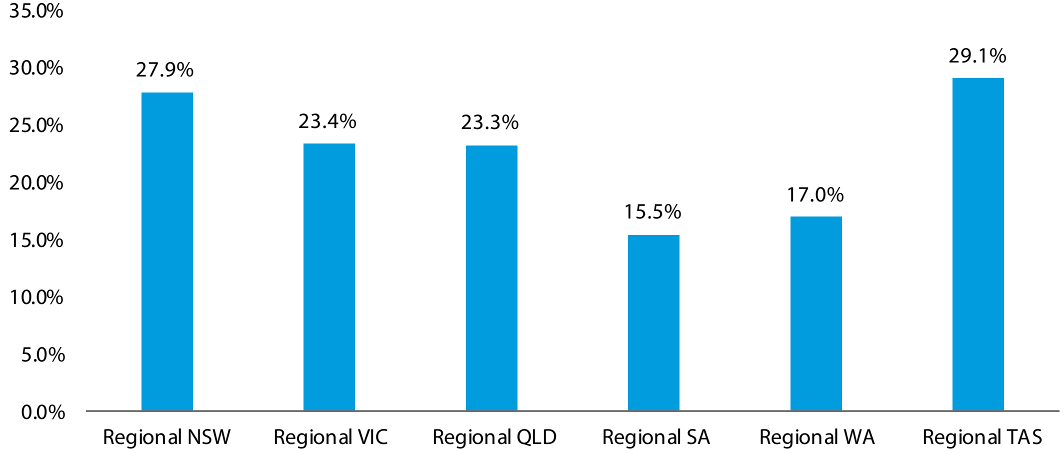
Housing prices across regional Australia have been growing strongly and for a prolonged period. According to CoreLogic, in October 2021 prices were 24.3 per cent higher than a year earlier. Underneath this aggregate measure there are places with much lower price growth, and others with much higher price growth. For capital cities, the growth over the same period was 20.8 per cent. The pace of this growth had been accelerating from late 2020 through until March 2021 (when the monthly price increase was 2.5 per cent, or an annualised rate of 30 per cent). While the pace of growth has since moderated, regional housing prices are still growing strongly – the annualised rate in October 2021 was around 20 per cent.

Prior to these latest increases, regional housing price cycles tended to be more muted than in capital cities, as outlined in the chart below. In particular, capital-city growth had generally outstripped regional growth. In that sense some of the latest growth in regional prices could be considered as catch-up growth.

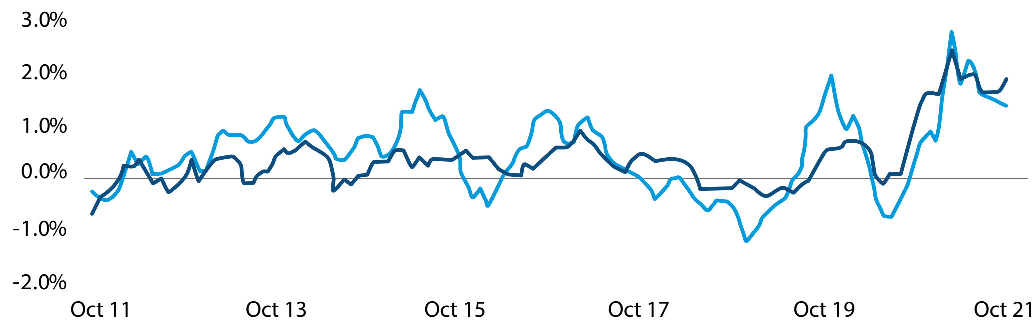
As highlighted earlier in this paper, despite the recent runaway price growth, housing affordability in regional areas is still more favourable than capital cities. Price-to-income ratios show that regional home ownership – whether on a regional or capital city income – is far more accessible than capital city home ownership.

Regional dwelling values- Oct 2021 vs Oct 2020

Source:CoreLogic



Month-on-month change in dwelling values



Source:CoreLogic

DISRUPTING ACCESS TO HOME OWNERSHIP

High price growth is often couched as a marker of success of a local community. However, as outlined in relation to the pressures in rental markets, this runaway price growth presents a significant disruption to local communities, particularly for lower-income households in those small inland areas that had typically struck a sustainable balance between low incomes and low housing costs. Housing stress isn't typically a significant issue in these communities and homeownership has been quite widely accessible, including to local low-income earners. So while overall price-to-income ratios in regional areas still compare favorably with capital cities, the runaway price growth is reducing local low-income earners' access to local home ownership and creating inequality in these previously sustainable locations.

BIGGEST INCREASES

LGA-level data from CoreLogic shows the largest annual price increases in the June 2021 quarter across each of the states (aside from the smallest markets where transactions are few and prices very volatile) were generally in small, low-cost inland LGAs. These increases are well above the 20 per cent price increase across regional Australia as a whole:

In NSW: Moree Plains (up by 99 per cent to reach $265,000), Narrandera (+65 per cent to $236,000) and Temora (+47 per cent to reach $380,000).

In Victoria: Loddon (up by 76 per cent to reach $247,000), Moyne (+59 per cent to $570,000) and Towong (+49 per cent to reach $305,000).

In Queensland: Murweh (up by 39 per cent to reach $132,000), Burdekin (+34 per cent to $215,000) and Maranoa (+30 per cent to reach $250,000).

In SA: Whyalla (up by 34 per cent to reach $207,500), Wakefield (+30 per cent to $215,000) and Berri and Barmera (+29 per cent to reach $245,000).

In WA: Port Hedland (up by 74 per cent to reach $365,000), East Pilbara (+66 per cent to $365,000) and Collie (+29 per cent to reach $231,500).

In Tasmania: Central Highlands (up by 64 per cent to reach $234,000), Dorset (+66 per cent to $480,000) and Southern Midlands (+41 per cent to reach $480,500).

In the NT: Alice Springs (up by 10 per cent to reach $435,000).

AFFORDABLE PLACES

There were many LGAs with a median dwelling price of under $250,000 in June 2021 including

NSW	Leeton
VIC	Gannawarra
QLD	Hinchinbrook
WA	Collie
SA	Berri and Barmera
TAS	Central Highlands

And affordability also remains high in many LGAs, with dwelling price to income ratios low. In places like these, median dwelling prices are about three times median annual incomes

NSW	Warren
VIC	Yarriambiack
QLD	Cloncurry
WA	Dalwallinu
SA	Cleve
TAS	West Coast

TOP DOLLAR REGIONS

Median dwelling prices (for houses and units) in the top dollar regions – generally high-value coastal areas proximate to the capitals that are also growing quite quickly – have overtaken their respective capital cities.

Regional markets more expensive than their capitals, June quarter 2021

LGA	Median Dwelling Price
Byron	$1,550,000
Kiama	$1,310,000
Wingecarribee	$1,028,750
Greater Sydney	$994,298
Queenscliffe	$1,250,000
Surf Coast	$1,182,000
Macedon Ranges	$805,000
Greater Melbourne	$753,100

LGA	Median Dwelling Price
Noosa	$1,000,000
Sunshine Coast	$716,250
Gold Coast	$637,500
Greater Brisbane	$586,142
Exmouth	$576,750
Augusta-Margaret River	$560,000
Chittering	$550,000
Greater Perth	$526,166

Source: CoreLogic

LATEST POPULATION GROWTH AND DYNAMICS

As highlighted at the outset of this paper, the desirability of regional Australia has been growing for some years, evidenced by rising net migration (more people moving to regional areas than those moving in the other direction). Job opportunities had been growing prior to the pandemic and the barriers to moving are even lower now given the much greater uptake of working from home.

The RAI's own coverage of population flows between capital cities and regional areas, the Regional Movers Index (see appendix) – produced in partnership with the Commonwealth Bank – shows the particular regional destinations experiencing the largest shares of this movement. It also shows the LGAs experiencing highest growth. In the 2020-21 financial year, the LGAs that accounted for the largest share of capital-to-regional migration were the largest non-capital city destinations:

- Gold Coast (11 per cent share)
- Sunshine Coast (5 per cent)
- Greater Geelong (4 per cent)
- Wollongong (3 per cent)
- Newcastle (2 per cent)

The five highest-growth LGAs are mostly a two-to-four-hour drive from Melbourne and highlight the flow of people from Greater Melbourne looking to make a tree change during the pause in lockdowns in early 2021:

- Moorabool in Victoria (up by 68 per cent)
- Mansfield in Victoria (+62 per cent)
- Corangamite in Victoria (+52 per cent)
- Murray River in NSW (+48 per cent)
- Alpine in Victoria (+47 per cent)

EFFECTS OF COVID-19 PANDEMIC

In addition to driving population growth (and demand for housing) in regional areas, the pandemic has also produced other effects that generally add to the demand for regional housing.

In relation to lockdowns, regional living has become even more appealing compared with capitals that have disproportionately borne the brunt of these lockdowns and restrictions. There is also anecdotal evidence that Australians who would otherwise be holidaying internationally are diverting this expenditure into regional housing markets, allowing prices to be bid up.

The closed international border has had a number of consequences. On housing's demand side, Australians have diverted their international holidays to domestic destinations, generally favouring regional areas (as opposed to capitals either in lockdown or at greater risk of going into lockdown). Analysis from Tourism Research Australia shows that despite closed borders, travel spend in regional areas increased in the year to June 2021 (while there were large declines in the capitals). TRA has also found that Australians are spending longer in their regional destinations. Accordingly, demand for holiday accommodation in the regions is high and many of the popular regions are reporting the presence of investors keen to supply into the short-term holiday accommodation market. There are mixed views about the impact that these listings have on local rental markets. Some feedback to the RAI has been that in some popular tourism destinations, holiday rentals tend to be newer, more upmarket properties which are quite different from the stock of long-term more affordable rental properties. On the other hand, there is evidence that a fall in short-term listings is associated with a fall in local rents.

The pandemic is also having significant effects on the supply side of the residential construction sector. The closed international border has meant a virtual halt in skilled migration. Labour shortages are widespread including in the residential building industry which is in the midst of a home-building boom. Trade labour shortages have been a chronic problem for many smaller inland areas, so the current shortages will be exacerbating this existing issue. The pandemic is also disrupting international supply chains. The price of materials is increasing, especially for timber. Timber shortages are a global phenomenon that had started emerging even prior to the pandemic. These supply-side effects mean that it will take the industry longer to complete the very large number of homes in the pipeline in regional areas. Current housing pressures are therefore likely to persist and even worsen for some time yet.

Main commercial street, Beechworth, Victoria

REGIONAL ECONOMIC GROWTH

Improving economic conditions tend to drive demand in housing markets – and this is on display in regional Australia.

Prior to the onset of the COVID-19 pandemic, regional economic conditions had been gathering momentum due to the easing drought and high levels of public infrastructure spending. Regional labour markets are an indicator of this momentum – job vacancies during the period 2016-2019 were growing at an average annual pace of around 6 per cent (the fastest since the mining construction boom). The actual number of people employed in regional areas in the years immediately preceding the pandemic was also growing; at around 2 per cent per annum, a pace not seen since the mining construction boom.

While the COVID-19 restrictions of 2020 temporarily derailed this momentum, the subsequent recovery was swift, strong and widespread. Regional job vacancies surpassed previous records (associated with the mining construction boom) in March 2021, and the latest data show a fresh record in October – more than 74,000 jobs advertised.

The current strength in the regional Australian labour market (and general economic conditions) is widespread across the states and territories. This is very different to the last period of high regional labour demand in 2011-2012, when the large number of job ads reflected the country's then two-speed economy – vacancies were narrowly based across the resources sector and states (mainly Queensland, Western Australia and the Northern Territory). Total job vacancies in regional New South Wales and Victoria were at best holding steady during that time.

The jobs currently advertised are positions that regional employers need to fill and are predominantly in the high wage, high-skilled trades (especially engineering and construction trades) and professions. The record vacancies suggest that there will continue to be a steady flow of workers from cities (and other places) flowing into regions to take up these positions.

The record vacancies suggest that there will continue to be a steady flow of workers from cities (and other places) flowing into regions to take up these positions.

RECORD-LOW INTEREST RATES, ULTRA-LOW FIXED RATES

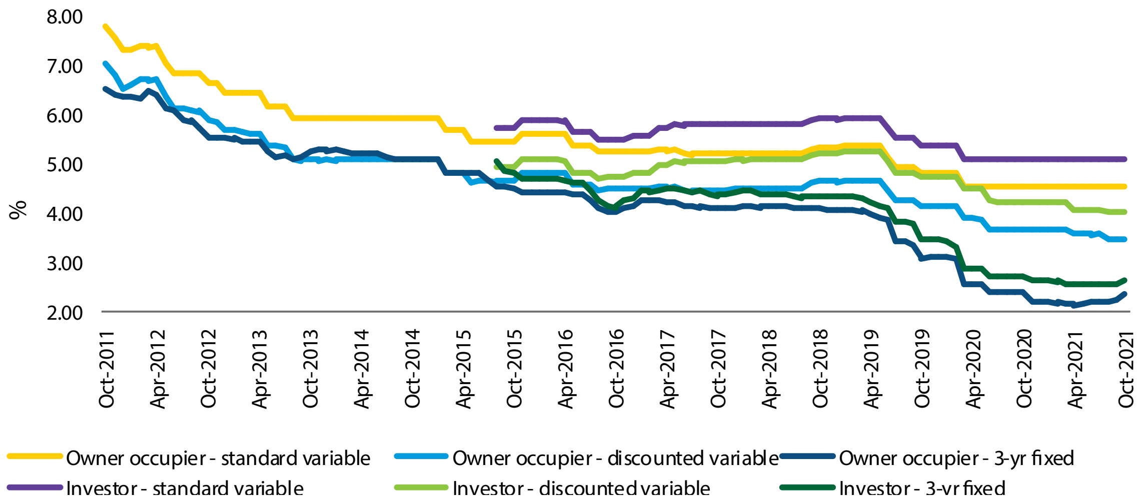
Housing markets generally are also very sensitive to interest rate settings, and this is applicable to regional Australia's housing markets. In particular regional housing prices have moved virtually in tandem with monetary policy settings in the most recent COVID-triggered loosening cycle. The RBA's loosening of monetary policy (including a raft of measures in addition to lowering the official cash rate) began in March 2020, with further 'unconventional measures' taken in November 2020. Regional housing price growth – after very little contraction – accelerated alongside these measures.

While current settings are still strongly expansionary, the degree to which they are expansionary is already starting to wind back. The RBA is starting to wrap up its unconventional monetary policy measures, including closing new drawdowns of the Term Funding Facility (in June 2021). This has already nudged fixed mortgage rates higher (average 3-year fixed rates to owner occupiers edged higher from a low of 2.14 in May reaching 2.36 in October), taking some steam out of the growth in housing prices. While regional housing prices are still growing, the pace of growth has been moderating since July 2021. Looking ahead, so long as interest rates remain low, this will keep the pressure on demand for housing and housing prices. More recently the Council of Finance Regulators has introduced macroprudential measures to cool the housing market – adding a higher serviceability buffer requirement on new loans issued. Borrowers will now need to demonstrate that they have sufficient incomes to withstand their mortgage rates increasing by 3.0 percentage points.

Regional housing prices moved virtually in tandem with monetary policy settings in the most recent COVID-triggered loosening cycle.

Mortgage rates to owner-occupiers and investors

Source:RBA



DECADES-LONG UNDERSUPPLY

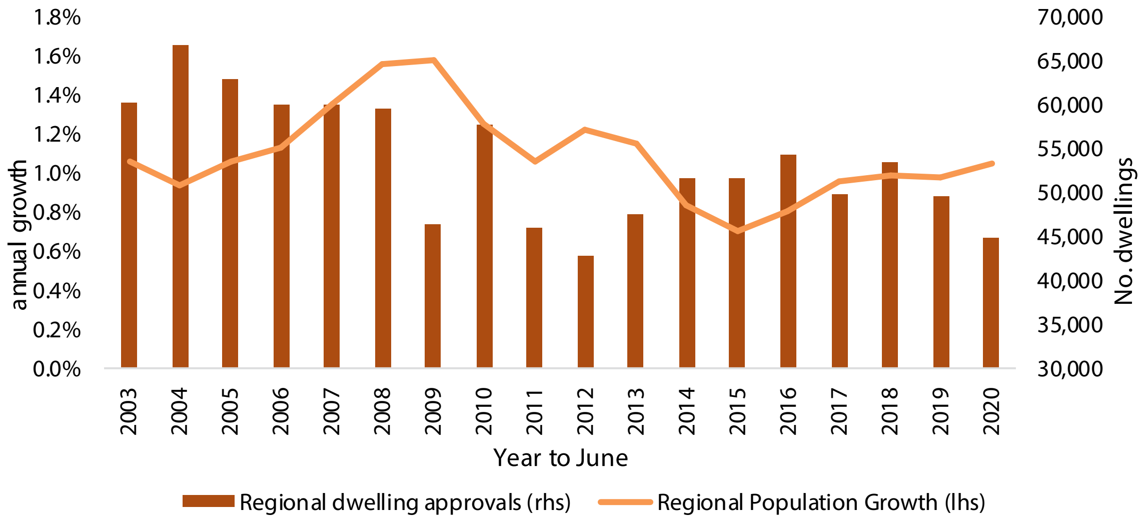
New home building in regional Australia has not kept pace with population growth over the long term. As a result, a regional housing shortage has been accumulating over several years.

In the most recent decade, regional Australia's population grew by an average of 76,500 people per annum. Yet the number of homes approved for construction declined in five out of those ten years. The absolute level of approvals during this decade has been low – about 50,000 dwellings per year, a level that is materially lower than in previous decade, when the annual average was closer to 60,000 dwellings.

Looking at that previous decade, the decade to 2011-12, regional Australia's population grew by an average of around 85,000 people per annum, while the number of dwellings approved for construction declined in eight of those ten years.

Australian regional population growth and annual dwelling approvals

Source: ABS, Regional Australia Institute



Report lead author Diwa Hopkins in Longreach Qld

SUPPLY GROWTH PERIODS

In the past two decades regional housing supply has only been boosted (in any meaningful way) by temporary housing stimulus measures brought on by economic crises. In response to the global financial crisis (GFC), the then Federal Government introduced the First Home Owner Boost. This grant – which was to the tune of $14,000 for new and substantially renovated homes – saw annual regional home building approvals rise to 54,394 dwellings in the year to June 2010.

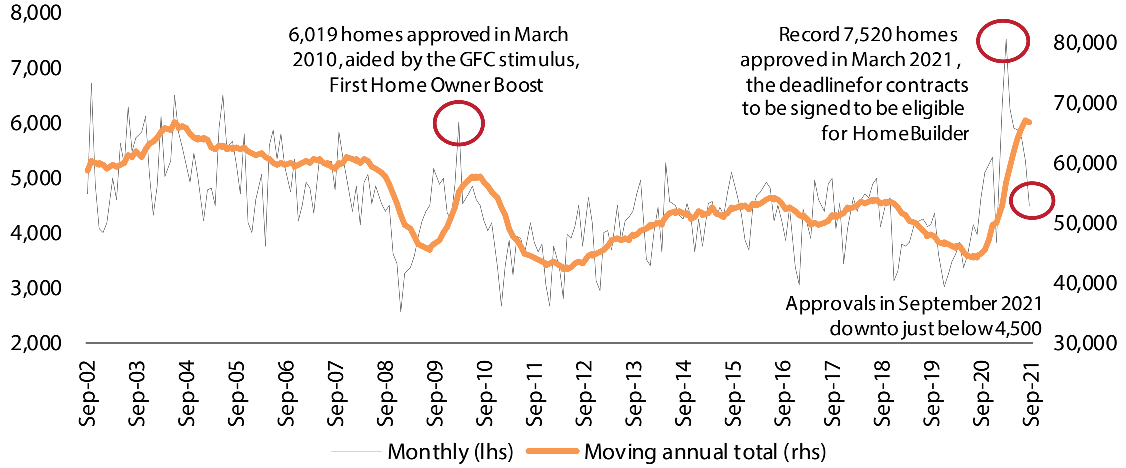
More recently, in response to the economic fallout of COVID-19, the Federal Government introduced the HomeBuilder scheme. HomeBuilder has been uniquely beneficial for many regional markets as the price caps on eligible projects rule out those in more expensive markets, including in capital cities where land values are high. Eligible new home projects must have a value that does not exceed $750,000, while a substantial renovation project contract must be between $150,000 and $750,000 on an existing property which has a value of no more than $1.5 million. The grant – which was to the tune of $25,000 for new or substantially renovated homes – has driven regional home building approvals to a new record.

This latest boost to supply will help to ease the current pressures in regional housing markets. As these homes get built and regional residents move into them, the churn will free up additional housing in both the home-purchase and home-rental markets.

While these temporary measures do help to alleviate years of accumulating shortages, the past two decades have shown that apart from times of crisis, regional housing supply is just not responsive to changes (namely increases) in demand, without government intervention.

As homes get built and regional residents move into them, the churn will free up additional housing in both the home-purchase and home-rental markets.

Regional home building approvals monthly and moving annual total
Source: ABS building approvals, RAI



NOT JUST HIGH GROWTH AREAS

As highlighted earlier in this paper, regional areas are almost universally experiencing housing pressures stemming from housing shortages. While media reporting has focused on the usual suspects – high-growth coastal areas – acute housing shortages are being experienced right through to small inland communities as well. For example, RAI research found that the shortfall of dwellings across the twenty-two LGAs that make up Western Queensland was about 1,480 dwellings.

POLICY CONSIDERATIONS

Local governments should consider accessing funds from NHFIC's National Housing Infrastructure Facility to assist bringing shovel-ready residential land to market.

UNLOCKING SUPPLY – LAND AND HOUSING INFRASTRUCTURE

This paper describes two overall housing market types that have very different challenges requiring different responses. Nevertheless, there are also policy settings that should be widely considered by state and local policy makers, irrespective of the market type in question. One widespread issue affecting both market types is the timely provision of shovel-ready land for residential housing.

In some growth markets, particularly those where the Commonwealth has made big project infrastructure investments which have boosted local economic growth and development, these investments have also had the side effect of contributing to local 'growing pains', particularly in respect to housing.[3]

Local infrastructure costs are often a barrier to land release. Bringing shovel-ready land to market in a timely way to meet the additional demand would help alleviate such growing pains. Smaller local governments (in areas where private development isn't occurring) often lack the financial capacity to invest in local housing infrastructure. Local governments should consider accessing funds (concessional loans, grants and equity investments) from National Housing Finance and Investment Corporation's (NHFIC)'s lending facility, the National Housing Infrastructure Fund, for local housing infrastructure to accelerate new housing supply.

3. https://www.nhfic.gov.au/what-we-do/national-housing-infrastructure-facility

REGIONAL AUSTRALIA INSTITUTE

UNLOCKING THE RIGHT SUPPLY

Another issue that is widespread is the nature of the shortage which is concentrated in non-detached housing. Regional housing stocks are disproportionately detached homes (see charts below) but needs and preferences are changing. The RAI has received widespread feedback from communities of varying sizes who report that the key segment of the market where demand is going unmet is non-detached or medium-density dwellings – the 'missing middle'.

The RAI's Western Queensland research found that even the smallest and most remote communities' local housing stocks need to be more diverse in order to best meet the needs and preferences of the people these regional and remote communities want to attract to fill local jobs: often young, single professionals and skilled tradespeople. Smaller dwellings are also often sought by long-term residents looking to downsize, even in smaller regional and remote communities. The local councils of Western Queensland estimated that nearly half of the additional 1,480 dwellings required by their communities should be non-detached housing, with nearly a quarter of those needing to be units or apartments.

In this respect, the flow of new housing (which only changes the mix of overall housing stocks at the margins) is still weighted to detached housing. State and local policy makers should consider how to facilitate bringing more non-detached product onto the market. There may be lessons to be gleaned from NSW and Queensland, the states which have the highest building approval rates for non-detached housing in their regions. Regional Victoria stands out with its very low share of non-detached housing being approved for construction, suggesting that planning and regulation at a state level could be a driver of this outcome.

As always, regions are responding with innovative local solutions. In Newcastle and Wollongong for example, the majority of new homes that have been approved for construction over the past five years are non-detached homes.

POLICY CONSIDERATIONS

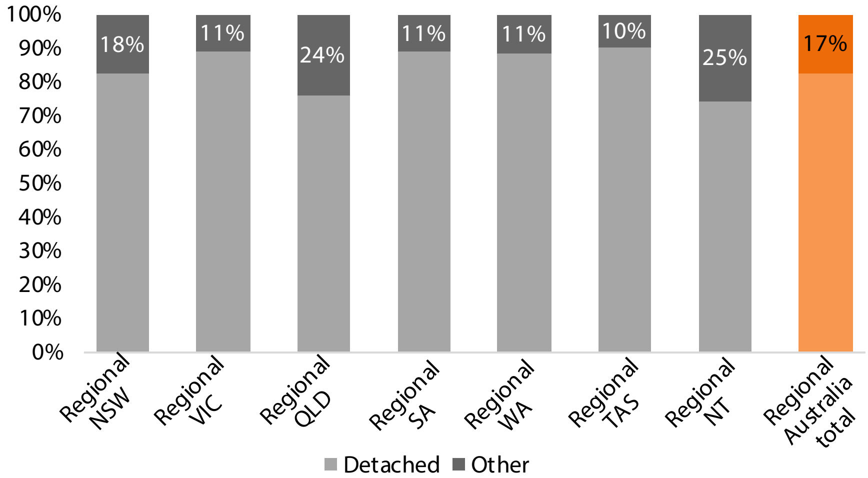
Review policy, planning and zoning settings – at state and local levels – to enable a greater share of non-detached housing to be built in a timely way.

Coffs Harbour recently approved a 13-storey mixed-use development in the CBD without controversy. Port Hedland has the Osprey Village which provides 293 affordable rental homes and community facilities for key workers through a partnership between the WA Government and a construction company. In Dubbo, apartment presales are currently underway in a 13-storey, mixed-use development, No. 1 Church Street. Even smalller inland local governments are taking innovative steps locally.

Temora Shire Council in NSW, for example, is explicitly seeking to free up local flexible zones for mixed-use and medium-density housing.

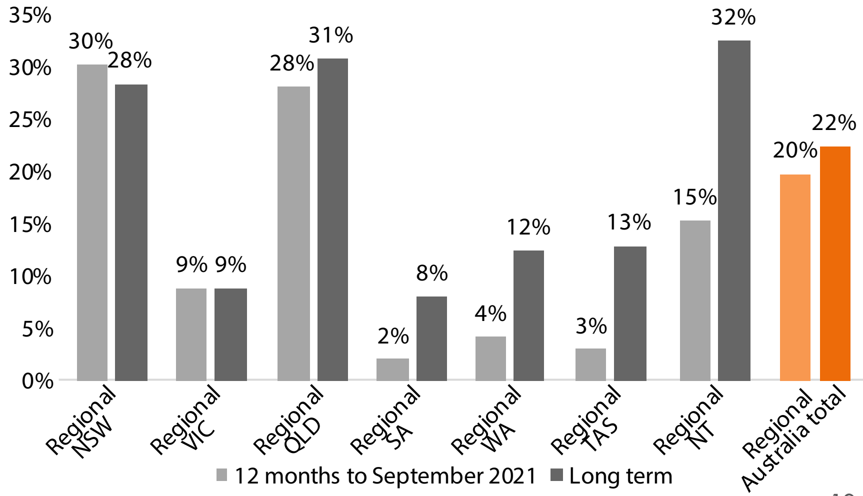
Regional housing stocks

Source: Census 2016, RAI



Non-detached housing share of all new housing approvals

Source: ABS Building Approvals, RAI



TRADITIONAL HOUSING SUPPLY CHALLENGES

In areas of high population growth, the housing market pressures are quite traditional – high demand has run up against constrained supply that is not adequately responsive to this demand. In these areas, supply may not be responsive to demand because of natural geographical restrictions, state government constraints, inadequate planning and zoning, or slow and onerous approvals processes. But even where the supply of suitable land is adequate, the market rarely capitalizes to provide the right mix of housing in regional places, and these dynamics are as important as land supply itself.

Supply challenges are contributing to housing-market pressures in these regions. The regions highlighted earlier in this paper as having the highest growth in migration from capital cities, along with those regions receiving the largest shares of population inflows, will be experiencing major stresses on their local housing markets. For example, those high-growth Victorian LGAs within two to four hours driving distance of Melbourne, all experienced price growth in the vicinity of 15 - 30 per cent in the year to June 2021.

Moreover, it's not surprising that the Gold Coast and Sunshine Coast LGAs have median dwelling prices ($637,500 and $717,250, respectively) that are higher than Brisbane's, as these LGAs are receiving the largest share of total capital city population outflows.

There are also the high-amenity, high-price regional LGAs including: Byron, Kiama and Wingecarribee in NSW; Queenscliffe and Surf Coast in Victoria; and Noosa in Queensland – each of these LGAs had a median dwelling price above $1 million in June 2021. While these markets are at the more extreme end of regional market trends, they represent the consequences of rapid increases in demand.

The key policy considerations in these types of markets need to address the issues of regulation, planning, approvals and shovel-ready land. Increasing total supply is essential, but so is working with builders and developers so that land is turned into dwellings, and that diversity increases to help ensure that new housing remains affordable. In high-growth places, especially those with severe shortages of accommodation for much-needed key workers, it is essential that a diversity of housing is provided including housing that offers a lower entry cost. In many LGAs there are restrictions on the approval of prefabricated and relocatable homes and these regulations need to be reviewed to enable some short-term responses to accommodation shortages. Medium-density developments need to be a prominent part of the planning scheme, even in regional areas, and in the longer-term, responses need to include the means to build a better business case for developers/ investors – local policy makers may even consider aggregating demand and offering a suitable structure such as a regional housing trust in order to bring about this supply.

In areas of high population growth, the housing market pressures are quite traditional – high demand has run up against constrained supply that is not adequately responsive to this demand.

POLICY CONSIDERATIONS

Issues around commercial feasibility, infrastructure provision, and planning controls (at local and state levels) that may be hindering the supply of shovel-ready residential land, along with mechanisms to encourage builders and developers to provide timely supply of a diverse mix of new housing stock.

Regulations (at each level of government) that may be limiting the ability for temporary or relocatable housing to be part of the local housing mix.

SMALL SCALE MARKETS, LITTLE 'DYNAMISM'

As highlighted earlier in this paper, current housing market pressures are being experienced by not just high-profile regions, but across all regional communities, right through to small inland areas where population growth is often weak or even non-existent. Inadequate housing in these communities is constraining local economic growth and development – jobs are going unfilled and nascent opportunities that would create more jobs are going unrealized due to insufficient housing for new workers.

In these markets, there is a broader issue of overall underinvestment in housing – whether new home building or the renovation of existing stock. This issue of housing underinvestment is widespread – a total of 184 out of 407 regional LGAs experienced an average level of annual housing investment that was less than $1,000 per capita over the three years to June 2020 (latest population data only go to June 2020). To put this in perspective, the regional LGAs receiving the largest investment see well above $4,000 per capita per annum. The chart opposite shows these low-investment LGAs are concentrated in the large states that have a higher prevalence of small, inland and remote areas – NSW, Queensland and WA and, to a lesser extent, SA.

In these areas, the housing market pressures are not immediately intuitive but have nevertheless arisen out of local housing supply being largely unresponsive to any underlying (incremental) increases in demand. Housing demand has slowly accumulated over many years, leading to shortages.

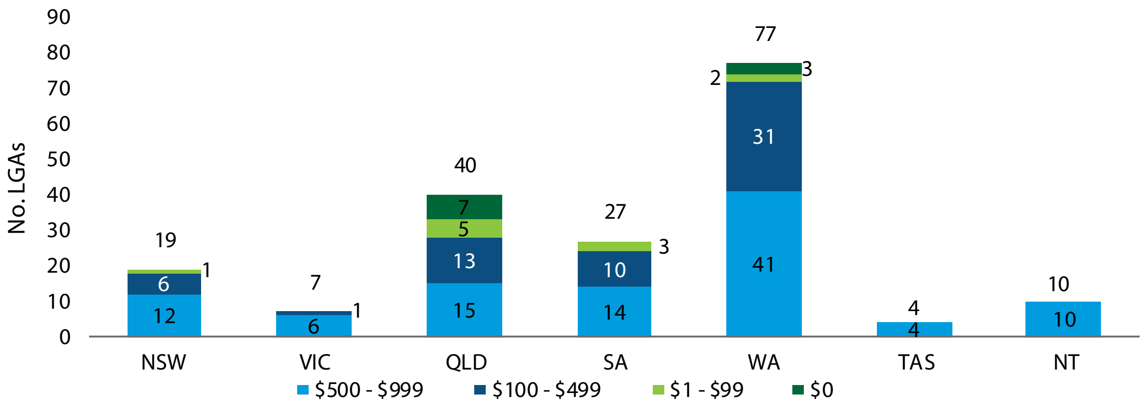
The unresponsiveness of local supply is due to these markets being small and having little 'dynamism' – there is no systematic property development (the development of new housing estates for example), while small-scale 'spec' home building that is regularly traded is also not a meaningful feature of these markets. The onus of all residential building work therefore falls on local households which face significant barriers to finance, as outlined further below.

POLICY CONSIDERATIONS

Regional groupings of councils to determine the scale of local undersupply and look to translating this into local investment opportunities through aggregated demand.

Regional LGAs with housing underinvestment (<$1,000 per capita per annum)

Source: ABS Building Approvals, RAI calculations



CREATING SCALE, ATTRACTING INVESTMENT

Regional communities can take action locally to overcome this issue of small scale. Groupings of regional LGAs can aggregate new housing demand across their regions to create scale that may be sufficient to attract commercial housing investment and development.

Specifically, aggregated demand for housing can be translated into an investment opportunity through an appropriate investment vehicle. Australian Housing and Urban Research Institute (AHURI) research suggests that an unlisted residential property fund is one such vehicle to attract institutional or private-equity investment. Institutional and private equity investors are increasingly open to investing in housing as the returns (the rents) have the potential to provide a sufficient and stable income stream. In attracting this type of investment, the structure of the fund is critical, as well as its management (it must be managed by an experienced fund manager). The actual properties and tenancies borne out of the investment need to be managed by an experienced property manager. Finally, the returns – the rental yields – must also be sufficient.

STRUCTURAL BARRIER TO FINANCE: BELOW-COST VALUATIONS

In low-growth areas, households that do have the appetite and financial capacity (under typical market settings) to undertake a new home build or major renovation project will face significant barriers to finance. Projects often don't materialize because of these barriers. The residents who are able to build or do major renovations are those who have deep pockets – they have significant cash to draw upon to make up the difference between the small amount they can borrow and the project cost.

Specifically, a home building or major renovation project slated to take place in a low-volume and low-price market will have its valuation weighed down, often to the point where the project is valued at below cost. This is because valuers must assign projects a market value based on recent comparable sales. Valuers are only able to draw on very few (if any) transactions, and the transactions that do occur are generally low-value housing compared with the cost of a new build or major renovation.

The table on the next page shows the largest LGAs that see the least amount of investment into local housing – measured by home building and renovating work approved by local councils on a per-capita basis in the year to June 2020 (latest population data only goes out to this date). Despite these particular LGAs being underpinned by relatively large populations, the small number of transactions that are occurring are at a low value and this is weighing on overall local housing investment.

Even the most expensive transactions of the few that are taking place (the 75th percentile) are still low in value. Critically, they can be lower than what might be considered the cost of a typical regional house and land package – for the purposes of this paper, this is taken to be about $450,000. This is the threshold for the 75th percentile price of these small-scale markets. That is, if the most expensive package traded is less than this threshold, it is likely that local households seeking to build or renovate will struggle to obtain typical mortgage finance for their project, and a large deposit will be required to offset the risk to the bank of lending for a project worth more than average dwelling values..

In the year to June 2020, across regional Australia, there were at least eighty LGAs where this was an issue; specifically, there were eighty LGAs where the 75th percentile dwelling price was less than $450,000 and the local level of housing investment per capita was less than $1,000 per annum. These LGAs obviously include small, remote locations but also major centres such as Armidale in NSW; Greater Geraldton in WA; and Townsville, Rockhampton, Gladstone, and Western Downs in Queensland, in addition to those in the chart opposite. While dwelling prices have obviously increased since June 2020, so too have building costs, so the issue of below-cost valuations is likely to still be pervasive.

Urban development, Lightning Ridge, New South Wales

A TYPICAL REGIONAL HOUSE AND LAND PACKAGE

$450,000 could be considered as the cost of a typical regional house and land package. While building costs are often higher in more remote locations, land values tend to be quite low and offset the higher local build costs such that total house and land costs are relatively modest. RAI research into housing in Western Queensland found that in Winton, while average build costs were high – some $2,000 per square metre – the average unimproved residential land value in 2020 was just $15,000 per block.

State	Region (LGA)	Estimated Resident Population (no.)	Value of approved residential building work per capita ($)	75th Percentile sales price ($)	Volume of sales (no.)
		Jun-20	Avg 3 yrs to June 2020	3 months to June 2020	3 months to June 2020
QLD	Western Downs	34,579	417	283,750	122
SA	Whyalla	21,506	201	247,500	58
SA	Port Pirie City and Districts	17,576	394	216,250	51
NSW	Broken Hill	17,269	357	173,750	60
QLD	Burdekin	16,953	932	250,000	47
SA	Port Augusta	13,697	569	246,500	25
NSW	Moree Plains	13,077	411	262,500	28
QLD	Maranoa	12,688	427	290,000	36
SA	Wattle Range	12,060	969	295,000	55
VIC	Ararat	11,965	824	285,625	42
VIC	Northern Grampians	11,403	973	290,000	43
WA	East Pilbara	10,921	244	253,750	-
SA	Berri and Barmera	10,836	762	277,500	33
QLD	North Burnett	10,656	643	240,000	31

Source: ABS, CoreLogic, Regional Australia Institute

STRUCTURAL BARRIER TO FINANCE: UPSIDE DOWN LOANS

RAI's recent research into housing in Western Queensland illustrates the actual mechanics of constrained access to finance. The diagram opposite shows the barriers that a hypothetical household will encounter in seeking to build a new home in Winton at locally estimated prices.

In this scenario, a typical loan – covering 90 per cent of the cost of the project – would be worth $396,000. The household would have to finance the remaining $44,000 with its own funds.

The first barrier is a low valuation. If the project was valued at Winton's median house price ($109,000 in the year to June 2020), rather than the build cost, then a typical loan (covering 90 per cent) on this value would only finance $98,100 of the project, leaving the remaining $341,900 to be financed from the household's own funds.

The next barrier is lenders' practices of lowering their exposure to more remote areas by applying lower Loan to Valuation Rations (LVRs). This practice stems from financial market regulation that requires banks to hold greater amounts of capital against their assets. The level of capital required depends on the riskiness of the assets held – the greater the risk, the greater the capital lenders are required to hold. Lending to borrowers in more risky markets is now more costly for banks than a decade ago because of the additional capital they must hold. Accordingly, banks tend to limit their exposure to regional and remote markets by restricting the LVRs of mortgages in those areas.

This Winton scenario considers a case where a lender would provide only 80 per cent of the value of the project. The ultimate loan amount – a loan that is 80 per cent of the reduced-value project – would be worth a mere $87,200. The household would then have to fund $352,800 – the vast majority of the cost – from its own finances for the home to be built.

The quality of the housing stock in these finance-constrained markets is of great concern to people in these communities. The driver is the same as for the lack of new builds – major renovation projects are likely to receive below-cost valuations and banks are similarly likely to apply stricter LVRs such that major renovation projects become financially out of reach. The cumulative effect is an overall deterioration in these communities' housing stocks.

Estimated cost of a new house and land package in Winton: $440,000

Finance Barrier 1: Lower Project Valuation

Reduced Loan: $98,100

Valuer values the new house and land package according to established house and land values ($109,000). A loan that is 90% of this reduced valuation is $98,100. The household would need to contribute around $341,900 of its own funds in order to fund the cost of the project.

Typical Loan: $396,000

A typical loan with a 90% Loan to Valuation Ratio (LVR) would be worth $396,000. The household would need to contribute the remaining 10% or around $44,000 of its own funds in order to meet the cost of the house and land package.

←Vs→

Finance Barrier 2: Lower LVR

Reduced Loan: $87,200

Lenders may then apply lower Loan to Valuation Ratios (LVRs) to communities they deem to be higher risk. A loan that is 80% of the project that has been valued at the reduced $109,000 is worth a mere $87,200. In this situation the household would need to contribute $352,800 of its own funds in order to meet the cost of the house and land package.

POLICY CONSIDERATIONS

Address severely constrained access to finance for households seeking to build new housing or do substantial renovations in small, low-value markets – consider expanding existing programs that address similar issues of access to finance such as the First Home Loan Deposit Scheme, the New Home Guarantee and the Family Home Guarantee programs.

A REGIONAL NEW HOME GUARANTEE

The Federal Government may consider a Regional New Home (and major renovation) Guarantee as a measure to reduce these significant barriers to finance, likely faced by households in at least 20 per cent of regional LGAs. It would be a response to two key problems in these low-volume markets: the availability of local housing AND the quality of the local stock.

This form of support already exists for some home buyers – providing access to finance for eligible borrowers who would otherwise face prohibitively large deposits. The Federal Government currently provides guarantees of up to 18 per cent of a home loan (allowing buyers to take out a home loan with a deposit as small as 2 per cent) for first home buyers, single parents and people looking to build through the First Home Loan Deposit Scheme, the New Home Guarantee and Family Home Guarantee programs.

A Regional New Home (and major renovation) Guarantee would have to guarantee a larger portion of a home loan. It is important that this guarantee reflects the cost of construction, while the loan would still be based on the project's valuation, usually already some discount on the actual construction cost. This would be to address the key barrier to accessing finance – low valuations. In very extreme cases, the financing gap is in the order of 70 per cent of a house and land package:

Using the Winton example, a 10 per cent deposit on a Winton house and land package costing $440,000 would be $44,000. The cascading effects of financial barriers mean that a bank might end up requiring a deposit (equity) of $352,800. The difference between $352,800 and $44,000 – the gap this scheme would seek to narrow or even close – is $308,800, or 70 per cent of the cost of the house and land package.

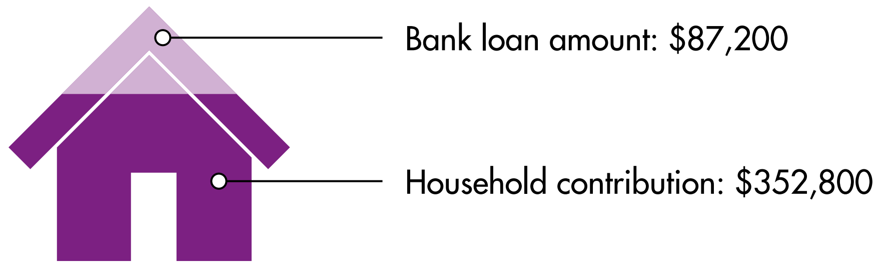
This is an extreme case – a more reasonable share could be 30-40 per cent of the cost of the house and land package. In the Winton scenario, a 30 per cent guarantee would be worth $132,000 – which is actually less than the maximum value of guarantees currently on offer: 15 per cent of the value of a $950,000 new-build property ($142,500).

Under this scenario the Winton household would be required to fund $220,300 of the $440,000 house and land package. $132,500 would be covered by the Regional New Home Guarantee, and the remaining $87,200 would be covered by the bank loan.

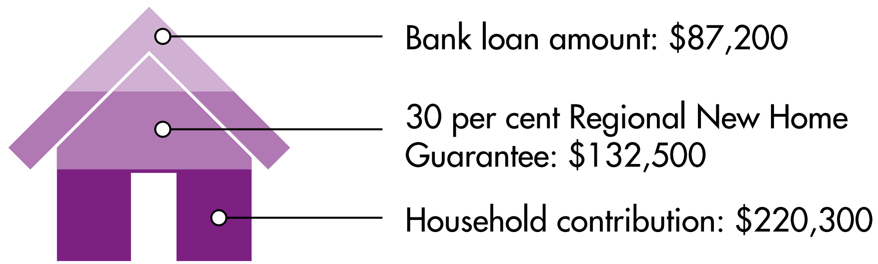
The Guarantee should also apply to loans for substantially renovating a property. Eligible households should be those seeking to build or substantially renovate a home in a market where there is a significant difference between the cost of a new house and land package and the prevailing prices at which homes are being traded. Eligible households should also be those who can comfortably service the loan.

WINTON $440,000 HOUSE AND LAND PACKAGE SCENARIO

CURRENT SITUATION: LARGE (PROHIBITIVE) HOUSEHOLD CONTRIBUTION



REGIONAL NEW HOME GUARANTEE: REDUCED FINANCIAL BURDEN



TRADE LABOUR SHORTAGES

Skilled trade labour in the residential construction sector has generally been in tight supply. With the pandemic causing a virtual halt in skilled migration, this tight supply has developed into a shortage, particularly at a time when a large volume of home building is in the pipeline.

While the RAI is mindful of the current national biosecurity aspects of allowing skilled workers into Australia, worker shortages in regions are becoming critical and migrant worker flows need to be re-established for the recovery to continue. Policy makers should consider these factors and potential timelines as Australia now begins to open its international borders.

Policy makers should also consider the level of investment in, and the availability of, quality post-school training and learning across regional Australia, as recommended by the National Regional, Rural and Remote Tertiary Education Strategy adopted by the Government in 2020. JobTrainer and expanded apprenticeship places will increase take-up by employers, but it is vital for regional communities that the pattern of this training being centralized is reversed, so that training can once again be done in region, to maximise the likelihood of qualified workers continuing to provide their skills in regional markets.

As long as skilled migration is constrained, trade labour shortages will persist, at least over the medium term, as any additional investment in training takes a number of years to result in more trade labour workers. The record level of public capital works in regional Australia is adding to current trade shortages and is creating cost increases due to excess demand.

Finally, trade labour shortages tend to be most significant (and chronic) in small and remote communities. Policy-makers might consider what incentives could be deployed to encourage tradespeople to practice their trades in regional and remote settings where the shortages and severe and ongoing.

Policy-makers might consider what incentives could be deployed to encourage tradespeople to practice their trades in regional and remote settings where the shortages and severe and ongoing.

POLICY CONSIDERATIONS

The role of incentives for tradespeople to practice their trade in regional and remote settings.

Building on the expansion of trade training places to increase trade training in smaller communities across regional Australia.

Processes to enable safe reopening of international borders for skilled migrants.

Using record levels of public capital works spending to stimulate expansion of regional trades training

CONCLUSION

Regional affordability – while still very attractive to capital-city movers – is being challenged, as regional home values have risen by an average of more than 20 per cent during 2020-21 alone. Regional rental housing has almost evaporated.

In high-value regional markets, essential workers are being priced out of the market. This leads to labour shortages and diminished amenity for residents as services become restricted due to a lack of workers.

Many small, low-cost regional communities are seeing significant disruptions to their local housing markets and it is likely that rental stress is becoming a greater problem and access to home ownership is narrowing.

Supply is not keeping up with demand in many parts of regional Australia, and the mix of housing being supplied is generally not meeting the needs of existing and new residents. Underinvestment in medium-density housing in regional Australia is particularly acute.

The RAI has outlined areas for policy consideration and development for all levels of government – federal, state and territory, and local governments – as well as investors and developers.

This discussion paper highlights the different drivers of housing problems in different parts of regional Australia. These different drivers mean that the responses, too, need to be tailored to each region if they are to be effective.

Bauhinia St, Blackall, Queensland

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