MELBOURNE INSTITUTE
Applied Economic & Social Research

Housing Cycles and Housing Affordability

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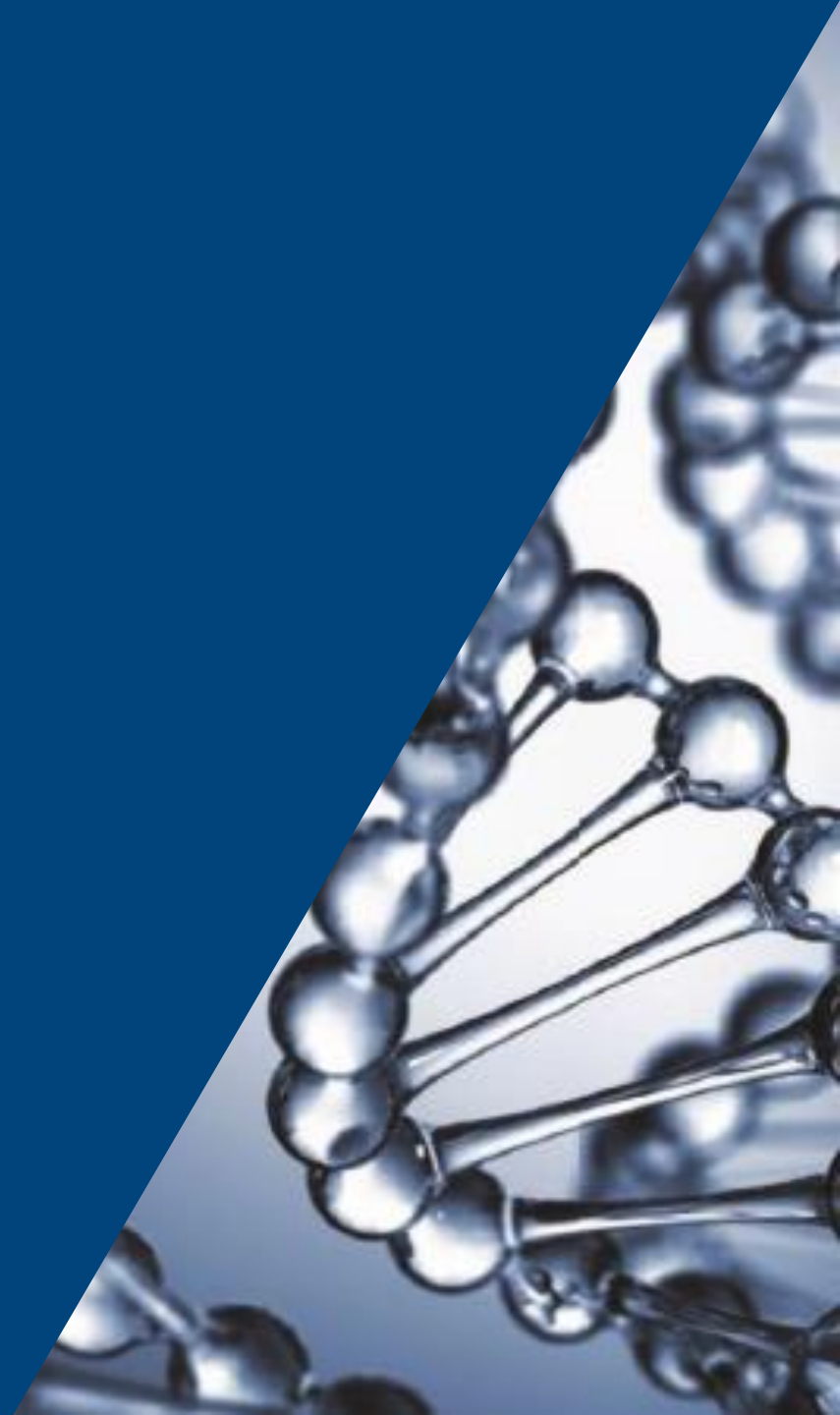
July 2024



Overview

Aims:

- Look at demand and supply factors in housing markets to understand underlying factors behind worsening housing affordability.

- Assess the Federal Government's target in 2024-25 budget:

> *"…and we're building more homes for Australians.*
> *In the 5 years from this July, we aim to build 1.2 million of them."*

Treasurer Jims Chalmer, Budget Speech 2024-25, 14 May 2024

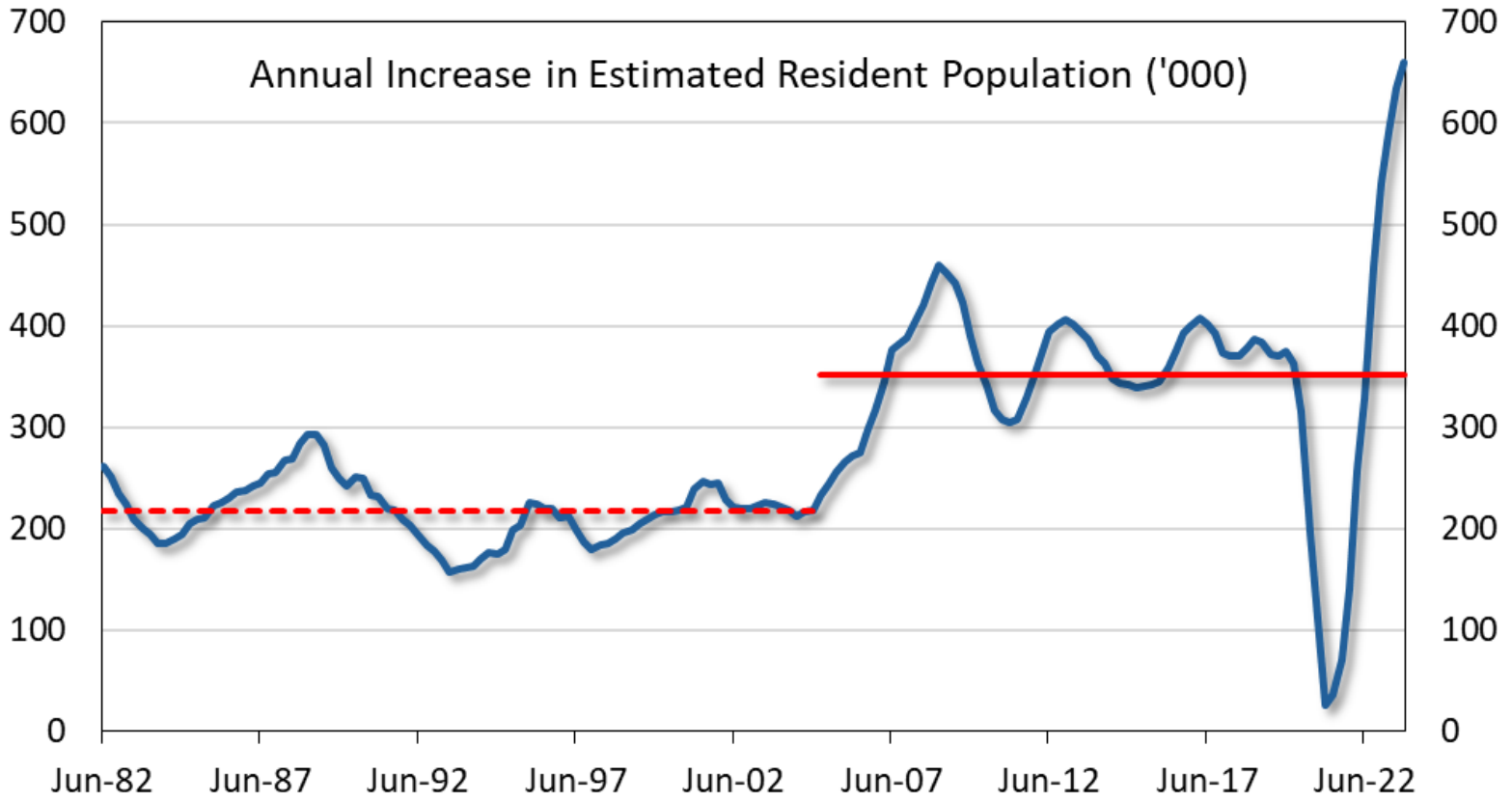
❑ *Is this ambitious? Will it be enough to ease the housing affordability issue?*

https://ministers.treasury.gov.au/ministers/jim-chalmers-2022/speeches/budget-speech-2024-25

Demand

Population increase as a proxy for increasing demand

- Huge population increase from 2005: average annual increase **220,000** → **350,000**

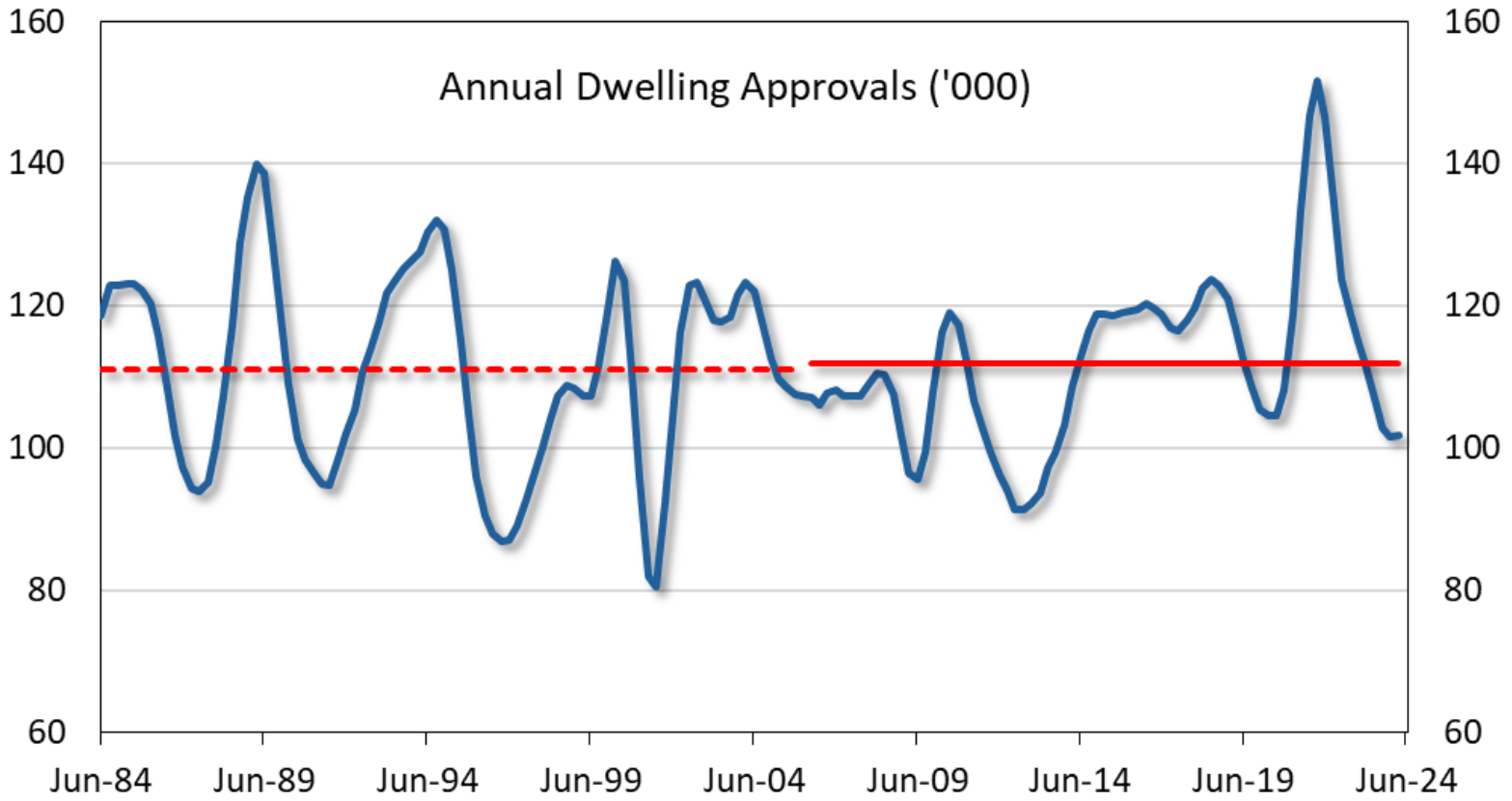


Source: ABS.

Supply

Dwelling approvals as a proxy for increase in housing stock

- Not much change in the annual number of dwelling approvals in the last **40 years**

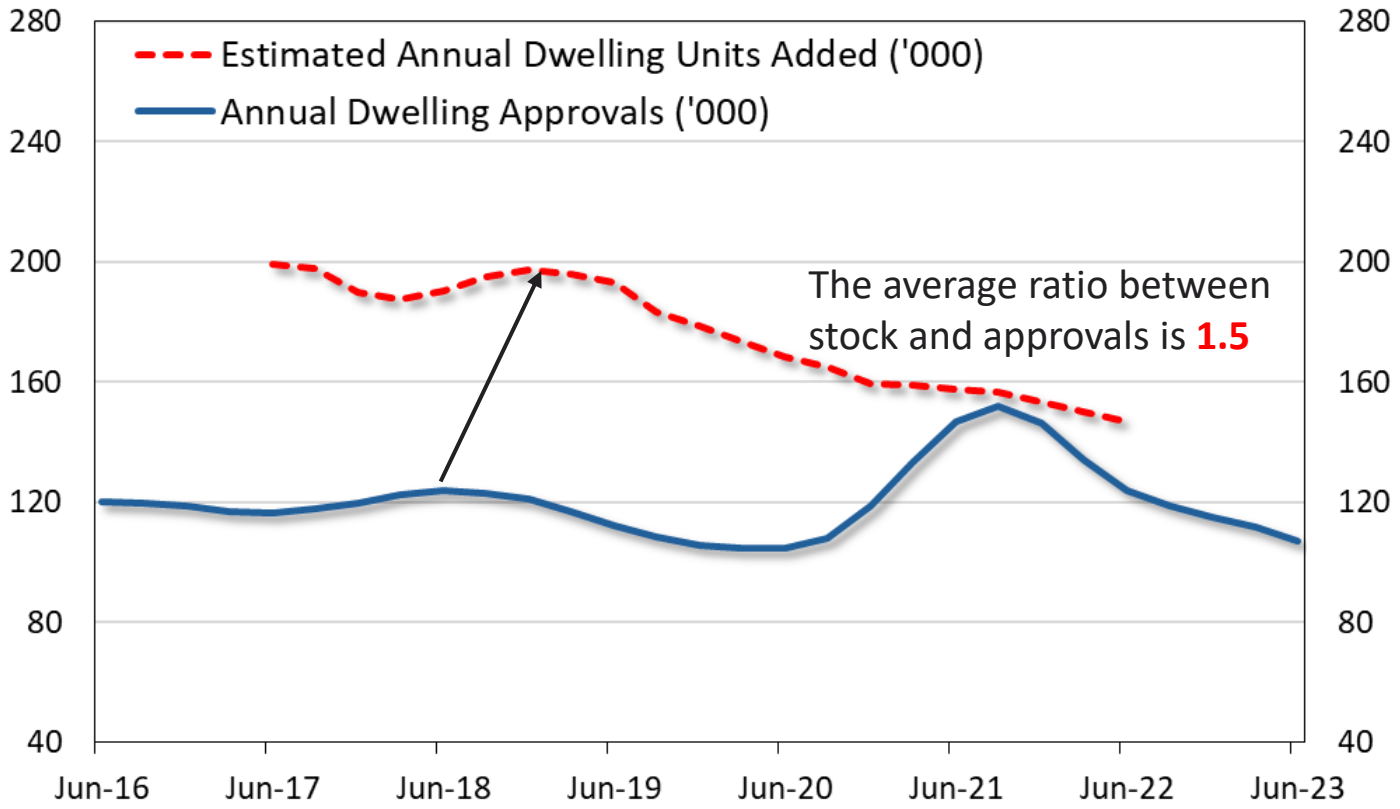


Source: ABS.

Supply

Dwelling approvals vs dwelling stock

- There is no official **ongoing** estimate of dwelling stock

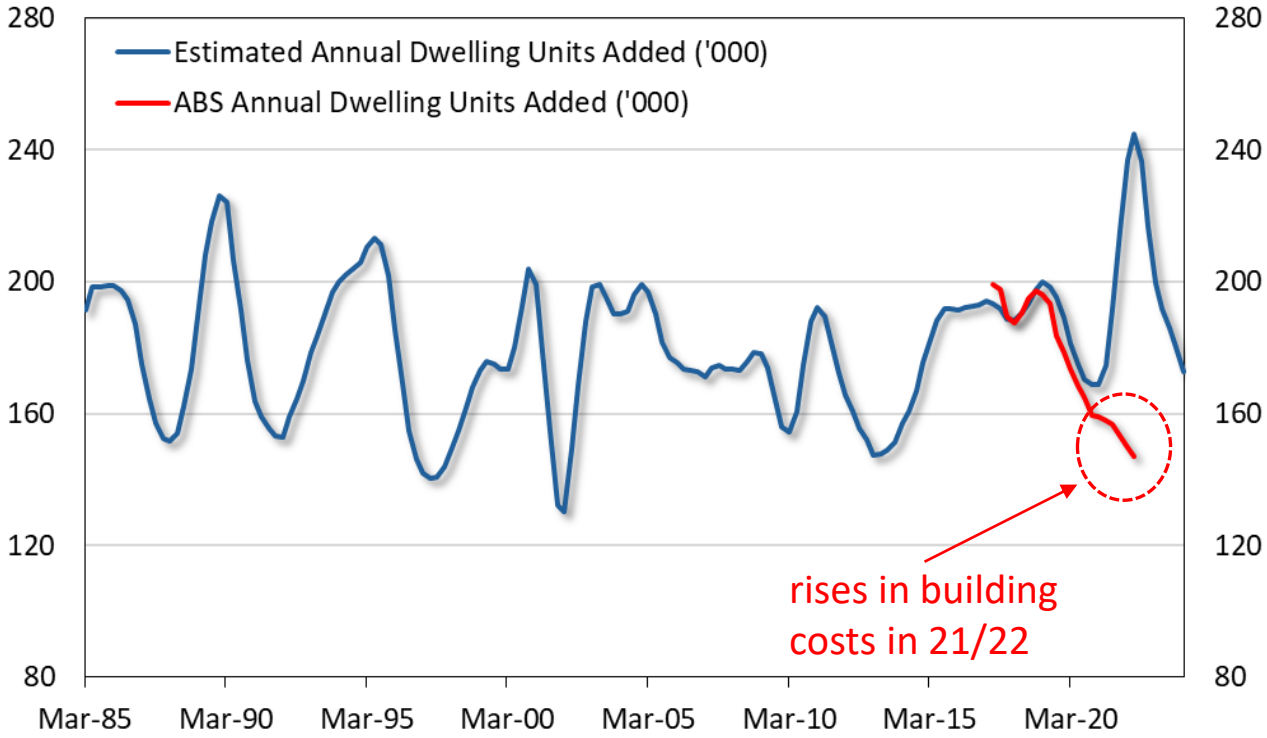


Sources: ABS; Dwelling stock estimates are based on the 2021 Census of Population and Housing.

Supply

Approximating increase in dwelling stock over time by dwelling approvals

Annual Increase in Dwelling Stock (**t**) = [**0.95** * *Annual Dwelling Approvals* (**t-3**)] * **1.7**



Assumptions:

- **95%** of dwelling approvals will be converted into housing stock within 9 months - a construction lag of **3 quarters**
- Ratio between actual stocks and approvals (to account for multiple-occupancy permits) is **1.7**

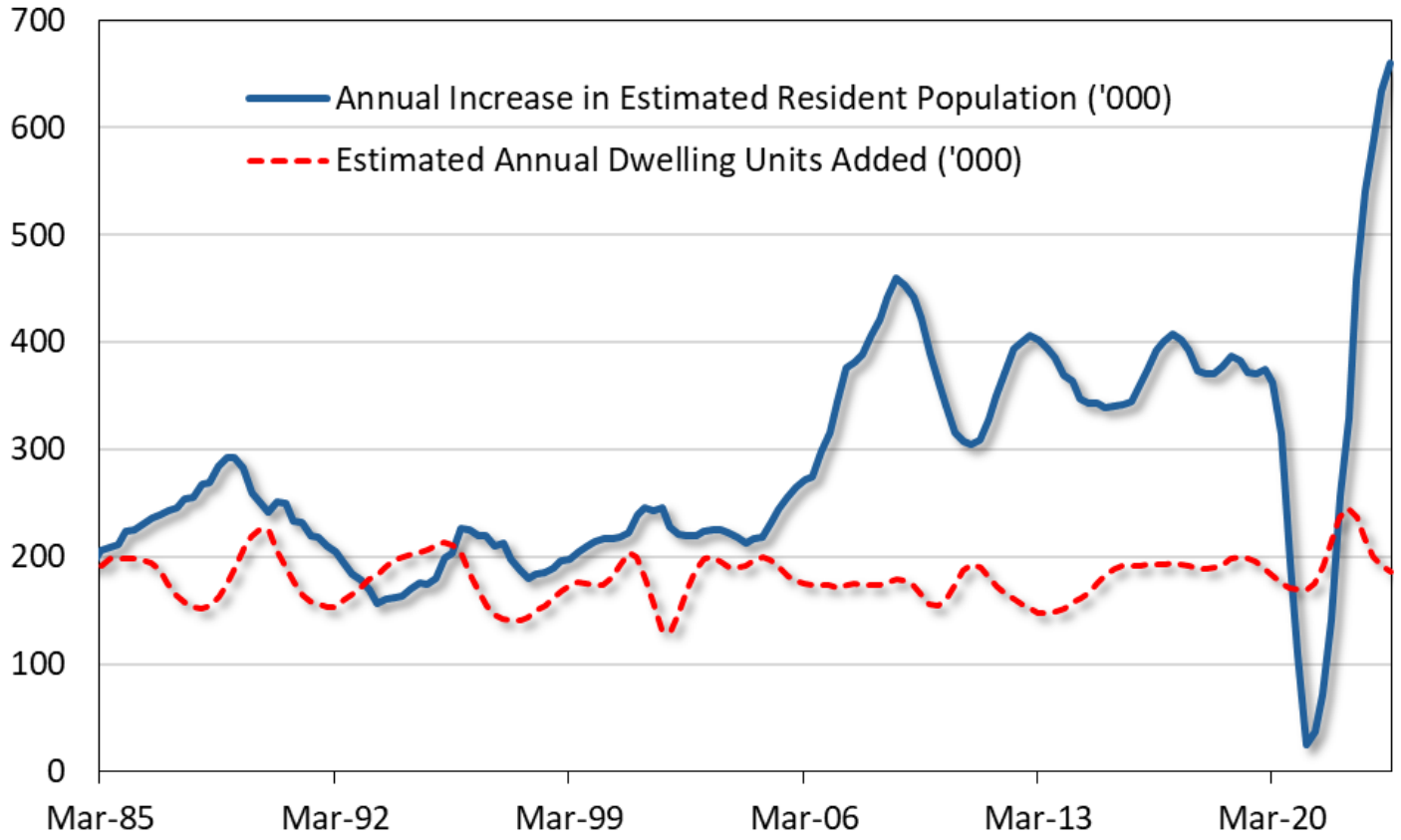
A Relatively Optimist Estimate

Sources: ABS; Dwelling stock estimates are based on the 2021 Census of Population and Housing; author's calculation.

Demand vs Supply

Increase in supply has not kept up with increase in demand

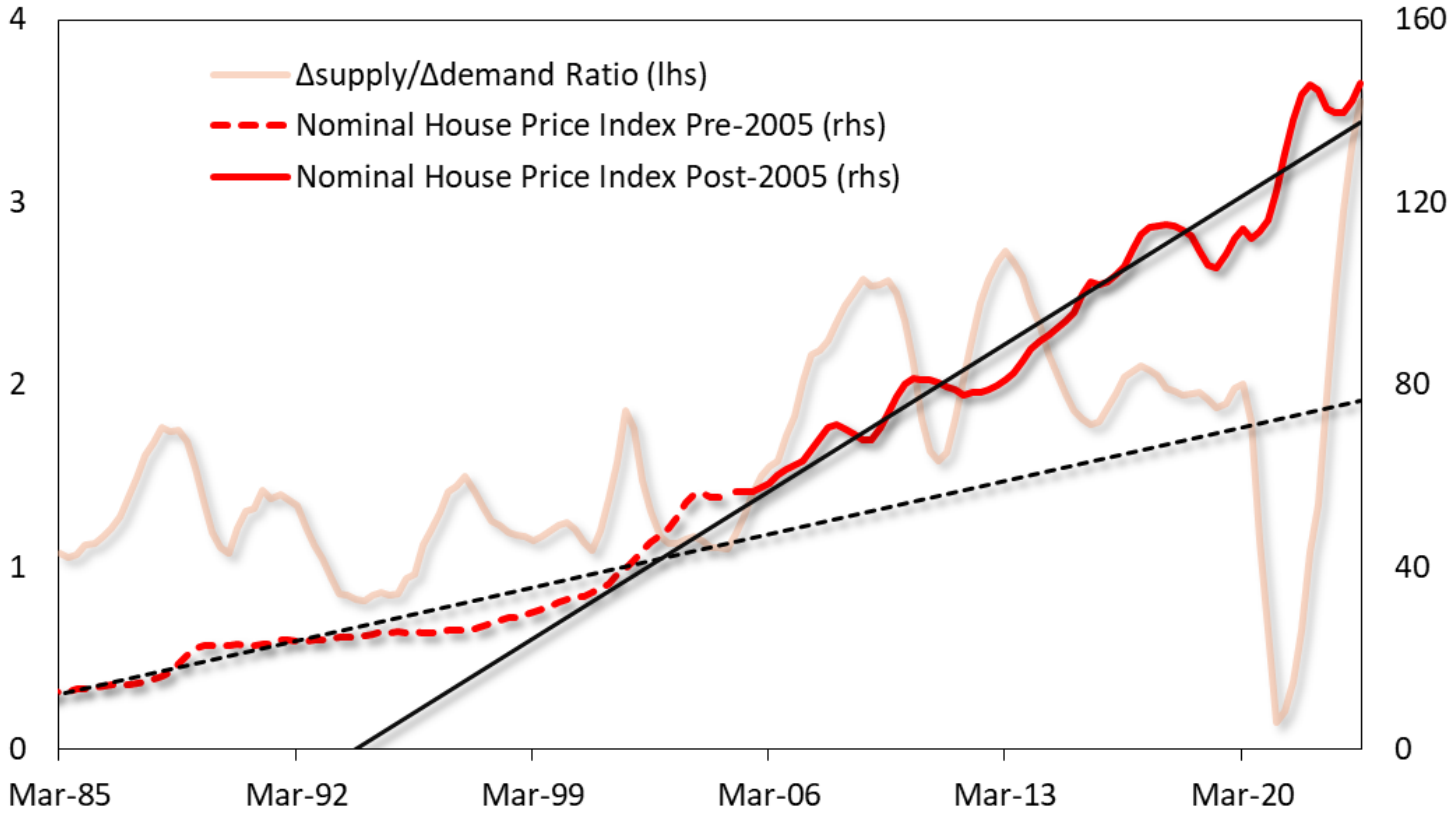
- **Δdemand/Δsupply ratio** increased from an average of **1.2** before 2005 to **2.0** after 2005



Sources: ABS; author's calculation.

House Prices

- Nominal House Price Index has a steeper trend post-2005



Sources: ABS; OECD; author's calculation; Nominal House Price Index (2015=100).

Federal Budget Target: is 1.2 million ambitious and enough?

- According to ABS estimates, in 6 years from June 2016 to June 2022, we added **a total of 1.2 million** new dwelling units, or around **200,000 new dwelling units per year**.
- Interest rates were lower and building costs were lower over that period.

❑ *Q: **Is the target of 1.2 million new homes in 5 years from July 2024, or 240,000 new homes per year, ambitious?*** Probably, YES.

- ❑ Higher interest rates
- ❑ Higher building costs
- ❑ Less saving in the population
- ❑ The fact that we have not built 240,000 new homes per year yet (based on existing estimates), or at least not consistently

❑ *Q: **Will this target, if achieved, ease the housing affordability issue?*** It depends on "excess" demand over this period.

- ❑ Population growth over this period is critical

Will the targeted new homes ease the housing affordability issue?

- Current average annual population increase since 2005: 350,000
- Long-run average annual dwelling units added : 180,000
- **Δstock** = *(new dwellings – dwelling removals)*

Key Assumption:
- Keeping annual population increase at **350,000 p.a.**

Δpop/Δstock ratio	Corresponding **Δstock** p.a.	Estimated **new dwellings** p.a. **(Δstock * 1.1)**
1.9 (current)	180,000	198,000
1.8	190,000	209,000
1.7	210,000	231,000
1.6	**220,000**	**242,000**
1.5	230,000	253,000
1.4	250,000	275,000
1.3	270,000	297,000
1.2 (historical)	290,000	319,000

Sources: author's calculation.