

REGIONAL AUSTRALIA INSTITUTE

Submission to
Standing Committee on Tax and Revenue

INQUIRY INTO HOUSING AFFORDABILITY AND SUPPLY

September 2021



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KNOWLEDGE POLICY PRACTICE

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

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EXECUTIVE SUMMARY

Housing markets are universally tight across regional Australia – both home-rental and home-purchase markets. These pressures have their origins in both the supply and demand sides of housing.

On the supply side, **decades-long underinvestment is the key driver of the current pressures in regional housing markets**. The number of new homes approved for construction in regional Australia over the past two decades has either been falling or small. This is despite regional Australia's population growing consistently over the same period and despite a national record home building boom in the latter half of the last decade. Strict lending conditions in low-volume markets have also made it difficult for borrowers to access the debt finance they need.

On the demand side, **regional population growth** and dynamics are key factors driving demand for regional housing. Many regions are underprepared for population growth and regional population projections have not been updated to ensure that much-needed infrastructure can be programmed. Additionally, **buoyant economic conditions in regional areas and record-low interest rates are fuelling high demand** for regional housing.

Housing shortages are a constraint on regional economic performance. Economic growth in many regions is being held back now by the lack of available accommodation for workers. Regional employers are advertising record numbers of positions, but in many regions there is simply no suitable accommodation for these much-needed workers.

While **regional dwelling approvals have risen sharply**, signalling additional supply to be brought on to the market, labour and materials shortages will delay the arrival of this new supply.

The **Regional Australia Institute recommends changes in policies at the federal, state and local levels**, designed to ease the current housing shortages in regions and address longer-term market failures. The RAI recognises that regions need to be resourced for population growth, and supports the new emphasis in Infrastructure Australia's recent *2021 Australian Infrastructure Plan* on dedicating resources to the provision of infrastructure and services in regional Australia.

DRIVERS OF REGIONAL HOUSING PRESSURES

PRICE GROWTH

1. **Growth in demand in regional areas has outstripped supply** – listings of properties for sale have been at historic lows at the very same time that interest in regional housing has increased. These low listings are partly due to regional people staying in place and not moving to capital cities as in the past.
2. **The increase in demand and capacity to pay has been driven by:**
 - An increased interest in and preference for regional living, enabled by widespread job opportunities (through record regional job vacancies) and further magnified by a greater ability to work from home.
 - Some price growth reflects 'catchup growth' in 2020 following years of regional price growth generally lagging metro market price growth.
 - Low interest rates, including ultra-low fixed interest rates. These have increased buyers' capacity to pay.
 - Additional demand has arisen out of COVID-19 – with funds diverted into regional housing instead of activities like for example for overseas holidays.

RENTAL PRESSURE

1. **Regional rental stocks have been declining** over the long term, in part due to local regional residents staying put rather than relocating to capital cities in the same numbers as in the past.
2. There is some evidence that **residential rental properties are being diverted to the holiday rental** market in tourist destinations amid the strong demand for domestic holidaying while international borders remain closed.
3. There is little commercial incentive to build for rent in many small, low-growth regional markets.
4. Investor activity is returning nationally, but it is unclear whether this is occurring in regional markets.

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RECOMMENDATIONS

MEASURES TO SUPPORT REGIONAL HOUSING AFFORDABILITY AND SUPPLY

NATIONAL MEASURES

1. **Introduce a 'Regional Home Guarantee'** – the housing shortage in regional Australia can in large part be attributed to barriers to finance which are specific to regional communities. In regional areas, financial market regulation often conspires with low valuations for home building and renovation projects to significantly reduce regional households' access to finance. The funding of such projects typically requires far more than a 10-20 per cent deposit/equity required of city borrowers – tipping the affordability/financial feasibility out of reach of the regional household. The Regional Home Guarantee would cover this significant finance gap faced by households seeking to build or substantially renovate a home in a regional area. It would play the same role in addressing this equity issue for regional buyers as it currently does for First Home Buyers and Single Parents.
2. **Target NHFIC's Capacity Building Program grants to regional community housing providers** – with a view ultimately for a larger amount and share of the Affordable Housing Bond Aggregator's loans directed to social and community housing in regional housing markets. Currently such providers and housing tend to be concentrated in metro markets.
3. **Targeting Commonwealth support for infrastructure to enable regional housing** – balancing the Commonwealth's big project infrastructure investments with funding to enable regional councils to get more land 'development ready', as local infrastructure costs are often a barrier to land release. NHFIC has a lending facility available for this and the RAI recommends that this be targeted to regional areas, especially those where there has been very little new building due to land supply constraints.
4. **Introduce a Regional Trade Placement Incentive** – another key barrier to housing supply in regional areas is a severe shortage in skilled trade labour. A regional trade placement incentive equivalent to what is offered to medical professionals placed in regional areas would help address this key barrier to housing supply.
5. **Invest into skills training providers – TAFEs and RTOs** – to build on the expansion of JobTrainer and the rapid uptake of subsidized apprenticeships. What's needed now is investment in 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.
6. **Restart skilled migration with specific targets/incentives for regional areas** – 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.
7. In addition to the above housing measures, the RAI is calling for **support for regionalisation** – a key strategy enabling regional Australia to reach its economic potential. Support would include measures that aid regional communities' liveability, enabling them to attract and grow their population. This could be done through business incentives, co-investment in regional working hubs or employment targets.
8. **Slow down public capital works to ease trade shortages** – so long as skilled migration is constrained, trade labour shortages will persist at least over the medium term (additional investment into training takes a number of years to result in additional trade labour availability, given the time it takes to educate and train). Slowing down growth in the record level of public capital works in regional Australia would ease current trade shortages.

ADDITIONAL MEASURES

State and regional

9. State governments should **review and revise regional population growth forecasts**. Widespread feedback to the RAI is that these population projections consistently undershoot actual population growth, leaving communities ill-prepared for the population growth that actually occurs.
10. State governments should **review stamp duty and development costs**. These place additional costs on housing. Stamp duty is an inefficient tax that is levelled only on households that transact on the housing market – typically those who are moving. The increasing numbers of capital-city dwellers moving to (and buying in) regional areas will face this additional transaction cost.
11. Regional groupings of councils should be determining the scale of local undersupply and look to translating this into local investment opportunities.

Local

12. Local governments – especially the governments of areas that are experiencing strong population growth – need to **bring more shovel-ready residential land to market and hasten the processes** for this to occur.
13. Local governments should **review and make any necessary revisions to local planning and zoning to enable an appropriate mix of dwellings** – many regional areas have an inadequate stock of attached and medium-density dwellings.
14. Local governments should **review and revise local regulations that may be limiting the ability for temporary or relocatable housing** to be part of the local housing mix.

TWO TYPES OF REGIONAL HOUSING PROBLEMS, TWO SETS OF RESPONSES

Regional Australian housing markets can be categorized – according to population growth – into two broad types which require two sets of responses.

HIGH GROWTH AREAS

In high-growth areas, the housing market pressures are quite traditional – strong demand has run up against constrained supply that is not adequately responsive to this demand. This dynamic has driven overall housing market pressures in these regions. This is most evident in 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 overall supply constraints in high growth regions partly reflect natural geographical restrictions but also inadequate planning for growth. Responses need to address the mix of housing as well as total availability – there is scope for more supply of medium density and more affordable housing.

Housing underinvestment in regional Australia is not limited to high-growth areas.

RAI has been receiving widespread feedback on local housing issues from a variety of regional communities across the country whose populations are growing slowly or even declining. In particular these communities are reporting that local underinvestment in housing – whether this be in new home building or renovation work – is constraining growth in local populations, employment and business activity.

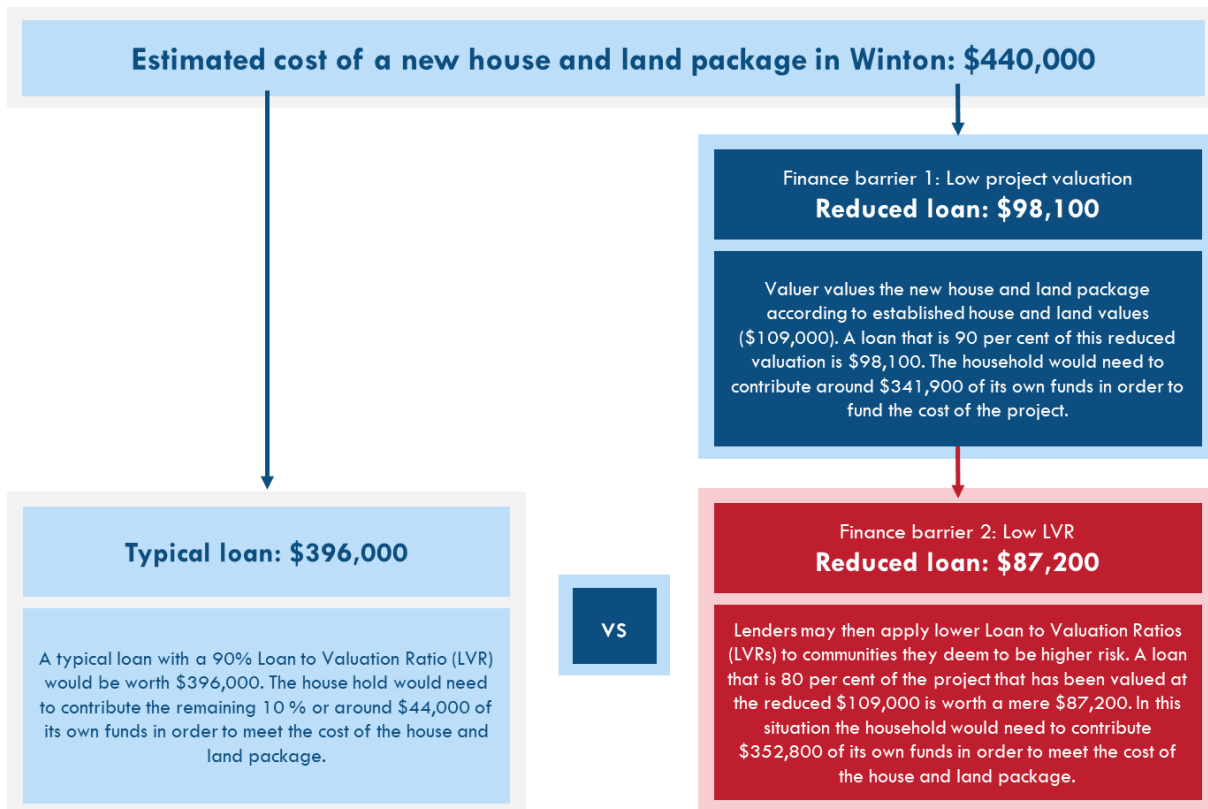
An indication of the underinvestment in housing is the very low levels of approved home building and renovation work per capita. The most extreme cases are LGAs – generally those with inland and remote locations – that have seen less than \$500 per capita per annum of approved home building and renovation work during the three years to June 2020. This compares with other areas – including capital cities – that have experienced well in excess of \$3,000 of approved home building and renovation work per capita, per annum over the same period.

LOW VOLUME AREAS

In low population growth areas the volume of trade in housing markets is generally very small. These low volume markets do not provide a vibrant enough local market to enable banks to provide finance on the same terms as provided to borrowers in more active markets.

In these low volume markets, underinvestment into housing is due largely to constrained access to finance. The constraints are most acute in places where the cost of a new home or renovation project is well above the value of the housing that is traded in the local housing market. Home building and major renovation projects in these settings will typically receive a valuation that is below cost and this in turn, weighs significantly on the household's access to finance. In small towns where there is no local building industry – no property development or spec-building – the burden of housing investment falls solely on local households. These households that do have the appetite to build or renovate face lopsided financing requirements – whereby in order to obtain any loan, the household will often have to provide a significant amount of equity, much more than the typical 10-20 per cent deposit. The RAI's recent

research into housing in Western Queensland illustrates the mechanics of this constrained access to finance with respect to a hypothetical new house and land pack in Winton.



A REGIONAL NEW HOME GUARANTEE

The RAI is recommending the Federal Government introduce a Regional New Home (and major renovation) Guarantee to address this structural barrier to finance. This would represent an additional category of homeowners eligible for a government guarantee of part of their home loan. Currently a limited number of guarantees of up to 18 per cent of the value of an eligible property are available to first home buyers, those building new homes and single parents, through the First Home Loan Deposit Scheme, the New Home Guarantee and Family Home Guarantee programs respectively.

For the Regional New Home Guarantee to work effectively, it would have to guarantee a larger portion of a home loan (than the currently-available guarantees worth up to 18 per cent). It is also critical that this guarantee is based on the cost of construction rather than the *value* of the property. 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 the guarantee 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 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, the financing constraint makes it hard for homeowners to raise the debt finance they would need for refurbishments and renovations.

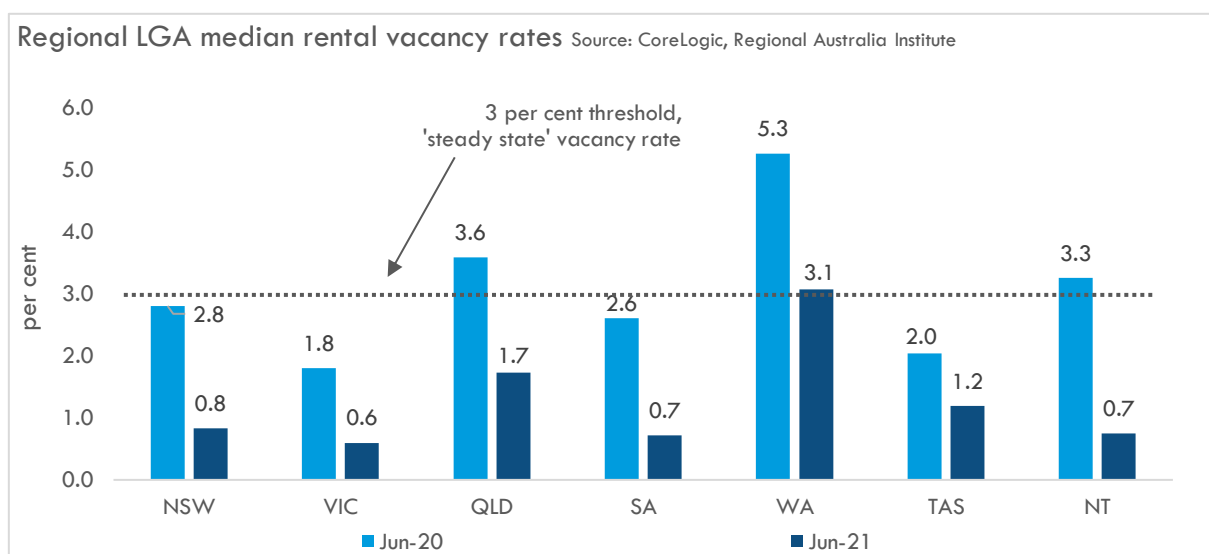
The Regional New Home Guarantee should also apply to loans for substantially renovating a property. Eligible households should be those seeking to build or substantially renovate a home in a market where there is a significant difference between the cost of a new house and land package and the prevailing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

CURRENT PRESSURES IN REGIONAL HOUSING MARKETS

Housing markets are tight across regional Australia – both rental and home-purchase markets. This tightness is reflected across numerous indicators across the regional areas of each state and territory.

REGIONAL RENTAL MARKETS

In regional rental markets, vacancy rates have more than halved in each state and territory – from what have already been tight markets in most states a year earlier. The chart below shows the median rental vacancy rate across regional LGAs is well below the three per cent threshold (considered to be a steady-state vacancy rate – anything less than this considered a tight rental market). Western Australia is the only state where the median regional rental market could be considered as not tight. The median vacancy rate for regional markets across the other jurisdictions is far below this threshold.

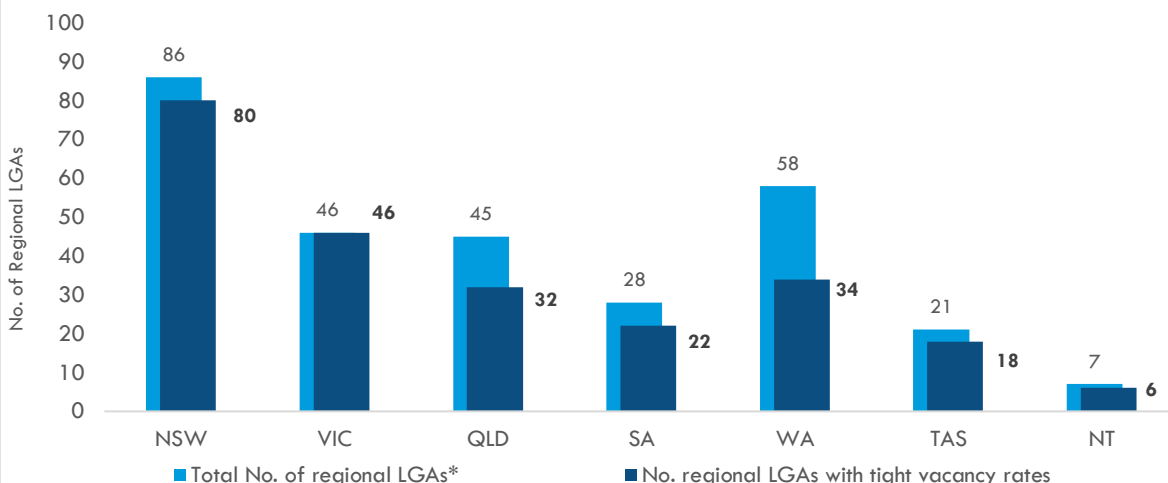


More specifically, the vast majority of regional LGAs (where data is available) had tight vacancy rates:

- **80 out of 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** – the three tightest were **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 LGAs with tight vacancy rates - June 2021

Source: CoreLogic, Regional Australia Institute



*where data available

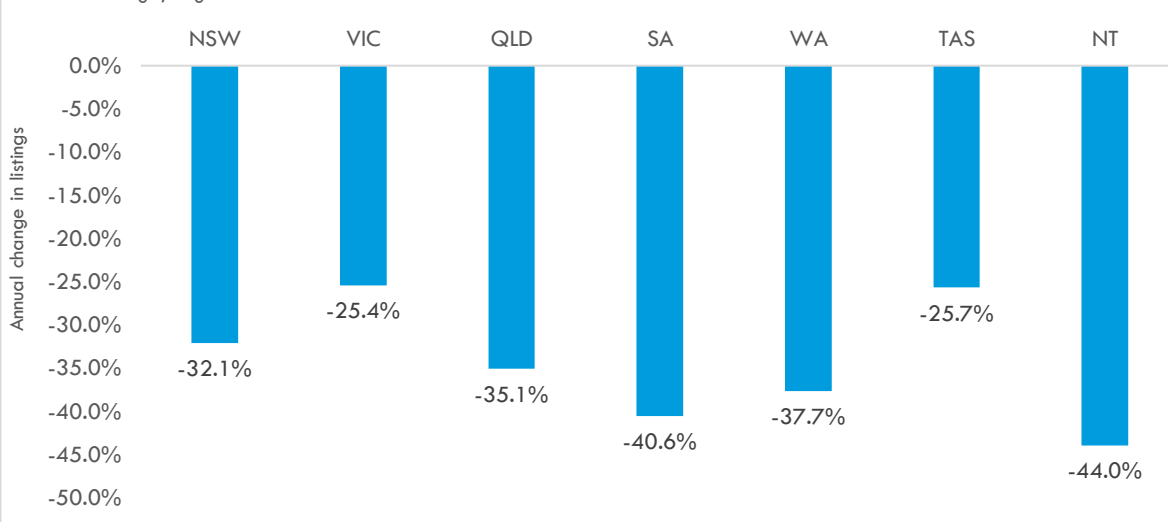
Driving this tightness is a low supply of rental stock. Across regional Australia, rental listings have been declining for a prolonged period – for around, if not more than, 18 months for most regions. The chart below shows the annual decline in total listings across the regional LGAs in each state and territory during the June 2021 quarter. The reductions have all been significant, ranging from 25 per cent to 44 per cent.

There are some signs that in some popular tourism regions some properties have been taken off the long-term residential rental market and converted to short term holiday rentals, contributing to long term rental stock shortages.

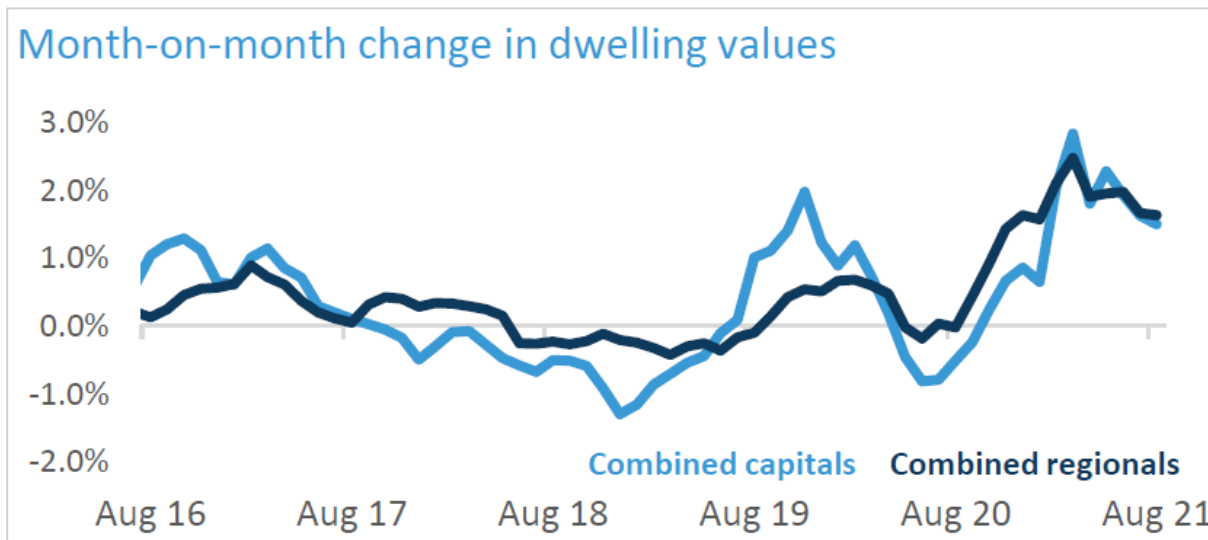
ABS and RBA data show that investors are coming back into the market nationally – the RAI believes that it is vitally important that regional investors return as well to lift the stock of rental properties. In many regions the yields are good (reasonably high rents and relatively low capital costs) so some of the commercial drivers are in place.

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

Source: CoreLogic, Regional Australia Institute

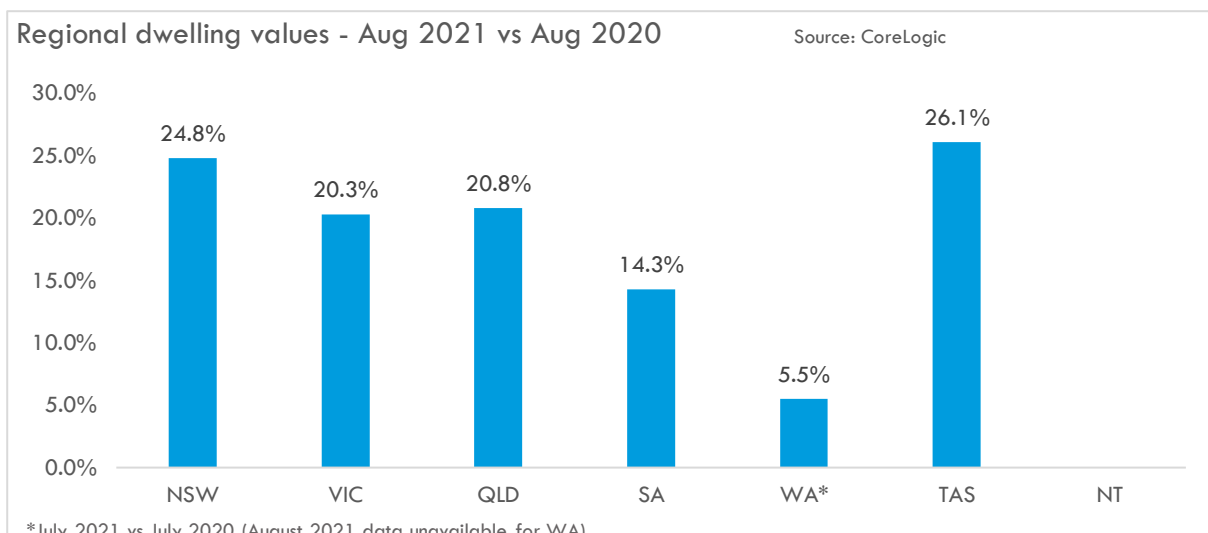


Housing prices across regional Australia have been growing strongly and for a prolonged period. According to CoreLogic, in August 2021 they were 21.6 per cent higher than a year earlier. For capital cities, the growth over the same period was 17 per cent. The pace of this growth had been accelerating 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 August 2021 was just shy of 20 per cent.



Source: CoreLogic

The growth in the aggregate is widespread and reflected in each of the jurisdictions. The chart below shows that in August 2021 dwelling values for each of the jurisdictions were substantially higher than a year earlier: up by 24.8 per cent in regional NSW, 20.3 per cent in regional Victoria, 20.8 per cent in regional Queensland, 14.3 per cent in regional SA, and up by 26.1 per cent in regional Tasmania. No data is available for regional WA and NT.



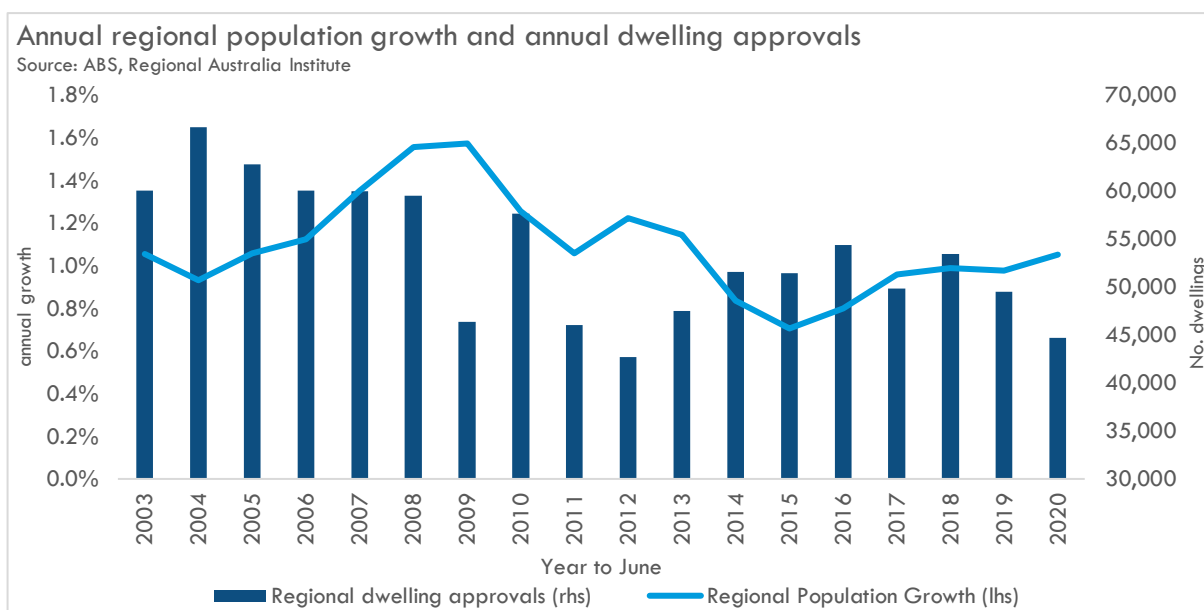
CAUSES OF REGIONAL HOUSING MARKET PRESSURES

SUPPLY-SIDE: DECADES-LONG UNDERINVESTMENT

Pressures in regional home-rental and regional home-purchase markets are underscored by a weak flow of new housing that has not kept pace with a growing population over the past two decades. As a result, regional housing demand has been accumulating over several years.

The chart below shows that since 2003-04 the number of dwellings approved for construction across regional Australia declined in each year out to 2011-12 (except for the during the stimulus-aided year of 2009-10). Meanwhile the population of regional Australia grew at an average rate of 1.2 per cent per annum (or around 85,000 people per annum) over this same period.

Since 2012, the number of dwellings approved for construction each year has remained anaemic relative to what was typical prior to the Global Financial Crisis (GFC). Between 2003 and 2008 regional Australia was approving on average slightly more than 61,000 dwellings for construction each year. In the decade to 2020, approvals were down to an average of 50,000 dwellings per year. This is despite regional Australia's population continuing to grow throughout that entire period. This is also despite home building nationally experiencing a record boom in the latter part of the decade (in terms of both duration and volume of building).

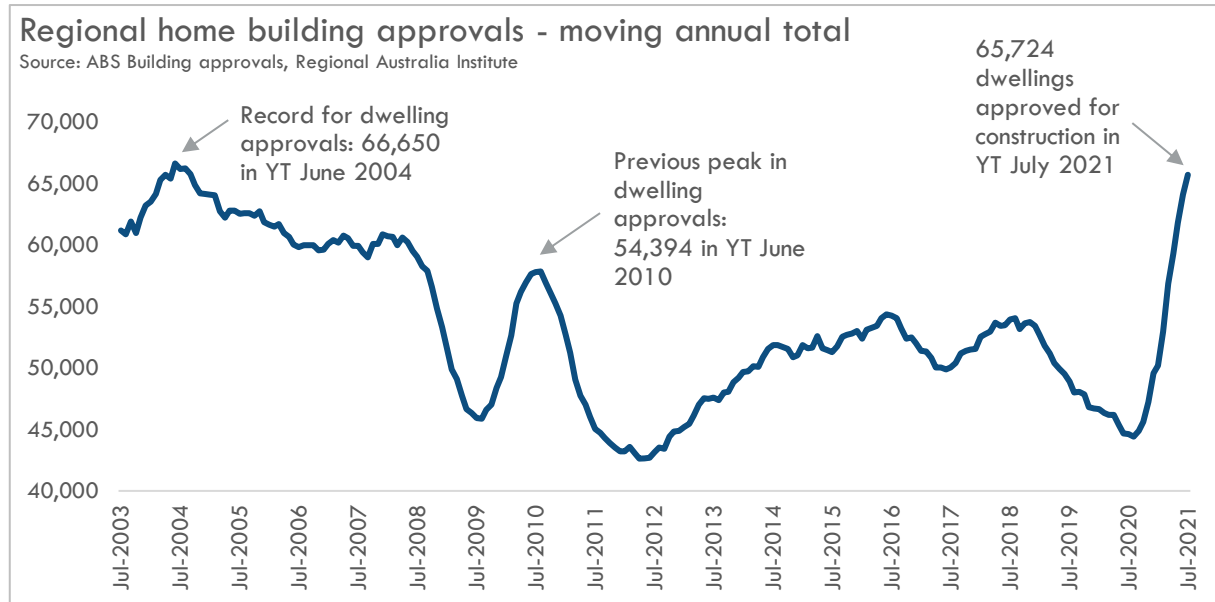


In the past two decades regional housing supply has only been boosted (in any meaningful way) by temporary housing stimulus measures brought on by economic crises. In response to the GFC, the then-Federal Government introduced the First Home Owner Boost. This grant – which was to the tune of \$14,000 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 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 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 annual regional home building approvals to

reach 65,724 homes in the year to July 2021. 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.

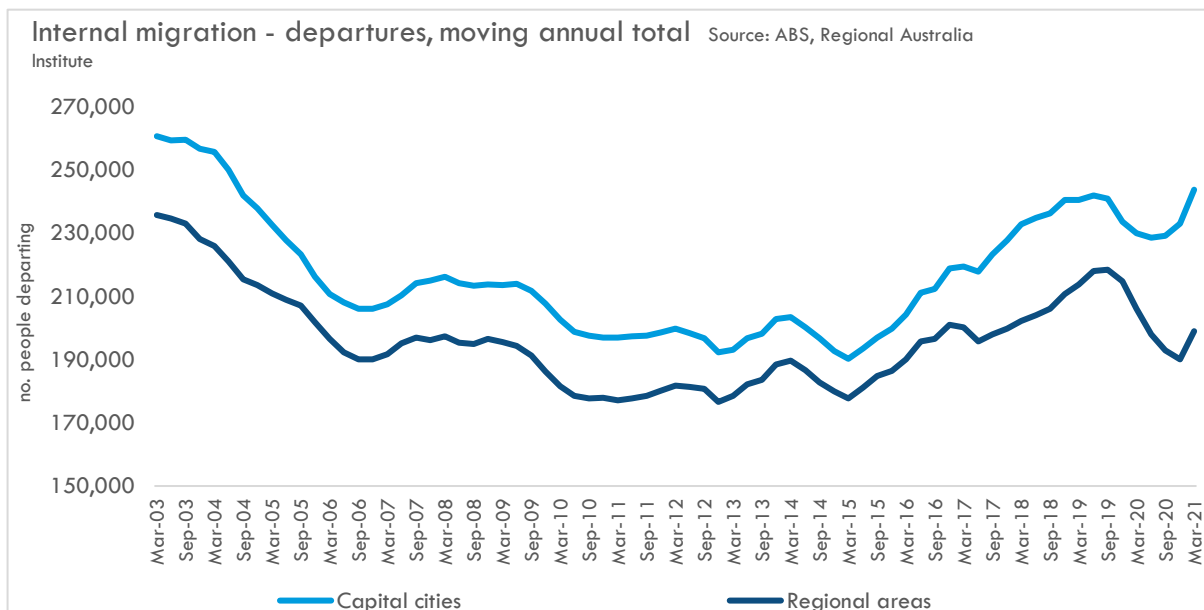
These temporary measures however do not overcome the underlying and ongoing structural barriers to regional housing supply and investment.



DEMAND-SIDE: REGIONAL POPULATION GROWTH AND DYNAMICS

The COVID-19 pandemic has accentuated a long-standing feature of Australia’s population dynamics – that population flows from capital cities to regional areas are larger than in the other direction. In particular, against the backdrop of the pandemic regional people have been staying in place in regions in far great numbers.

The chart below illustrates how departures declined amongst both capital-city dwellers and regional people, but the magnitude of decline was far greater for regional people. That is, in 2020 a total of 190,151 people departed regional areas (for capital cities) - this is far fewer (down by 11.5 per cent) than the 214,875 people who made such a move in 2019. For capital-city dwellers moving to regional areas, the decline was marginal: 233,122 in 2020 compared with 233,779 in 2019.



This has driven net migration to regional areas to record levels. This net migration outcome is also a key driver of regional housing market pressures. As regional people stay in place, fewer dwellings are coming up for sale and rent. Meanwhile, for those dwellings that do become available for sale or rent, there is strong demand, given the still-strong numbers of capital-city dwellers making a regional move. No data is available for investors in regional housing markets, but there is widespread anecdotal evidence of strong investor demand for regional housing.

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 and also the LGAs experiencing strongest growth. In the 2020-21 financial year, the LGAs that accounted for the largest share of capital to regional migration were:

- 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 LGAs that experienced the largest increases in migration from capital cities were:

- 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)

The five highest-growth LGAs are mostly 2-4 hours' drive from Melbourne and highlight the outflow from Greater Melbourne of people looking to make a tree change once the lockdowns eased in early 2021.

Population inflows of the scale seen in these LGAs in 2021 will be having a major impact on housing shortages. Increasing supply is essential, as is increasing diversity to ensure that new housing remains affordable. In high growth places, especially those with severe shortages of accommodation for much-needed 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 part of the planning scheme, and in the longer-term responses need to include the means to build a better business case for developers/investors by aggregating demand and offering suitable structures such as a regional housing trust.

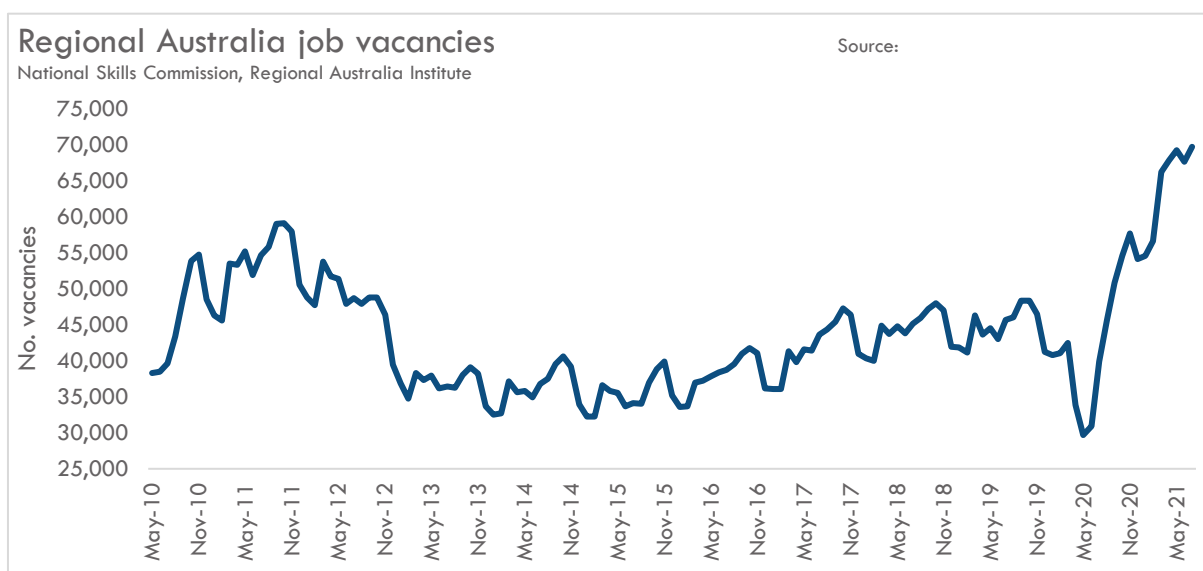
DEMAND-SIDE: STRONG REGIONAL ECONOMIC CONDITIONS, LOW INTEREST RATES

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

REGIONAL ECONOMIC GROWTH

Prior to the onset of the COVID-19 pandemic, regional economic conditions had been gathering momentum at the behest of easing drought conditions and strong 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 similarly growing at around 2 per cent per annum, also a pace not seen since mining construction boom times.

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, with the latest data showing a fresh record in July – some 69,700 jobs advertised.



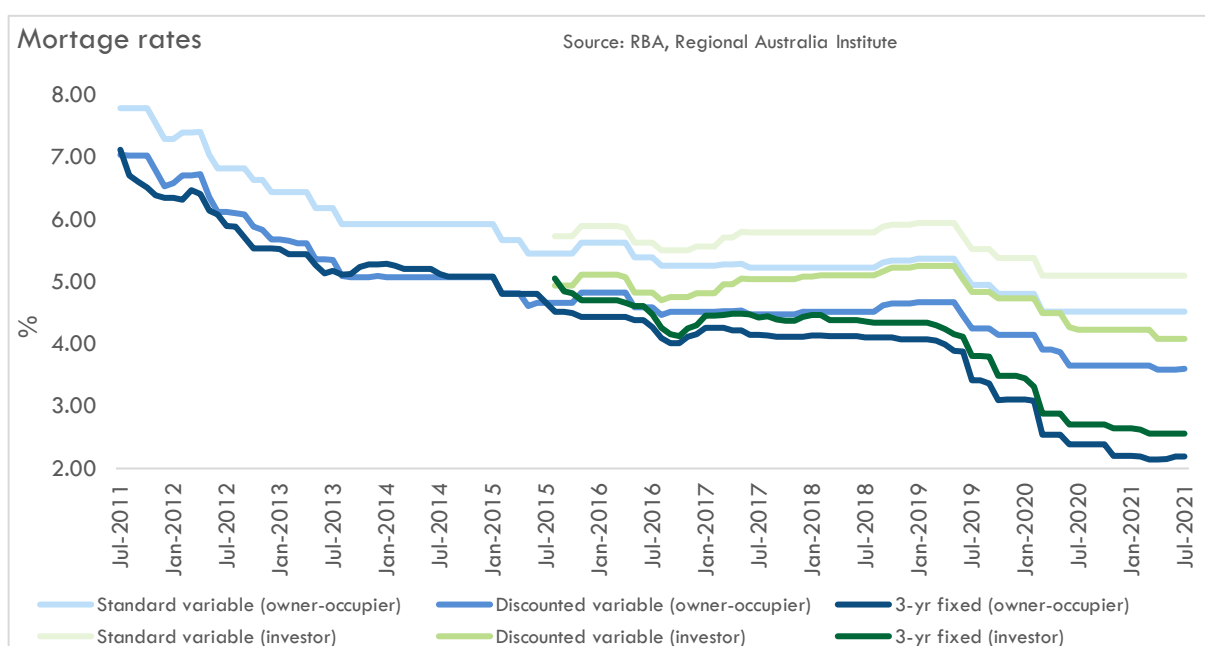
The current strength in the regional Australian labour market is widespread across the states and territories and across different occupations. This is very different to the last period of strong labour demand 2011-2012, when the large number of job ads reflected the country’s then two-speed economy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

The jobs advertised are positions that regional employers need to fill, and the record numbers 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.

Most state government planning departments are currently updating their regional population forecasts to take account of the changes in the scale of growth seen in recent years in regional Australia.

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 – as outlined further above – 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 settings are still very 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 (on June 2021). This has already nudged fixed mortgage rates higher (average 3-year fixed rates to owner occupiers edged higher from 3.59 per cent to 3.6 per cent in July), 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.



CONCLUSION

The RAI welcomes this inquiry into housing affordability and supply. Both are very important concerns in regional Australia in 2021.

Affordability is being challenged as regional home values have risen over 20% through 2020-21, and in particularly 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 lack of workers.

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 proposed responses to these challenges for consideration by the Commonwealth Government, State and Territory Government, and Local Governments.

The RAI has pointed out the different drivers of the 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. The RAI is keen to assist the Inquiry with further analysis or information if required.