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Markets Stabilise in the Wake of Stricter Lending

At a time when uncertainty is affecting property markets, it is appropriate to review some factual information about influences driving demand for residential property. This newsletter looks at both the Gold Coast and Australia's East Coast markets.

Among the factors driving the uncertainty are elections, both here and overseas, Brexit, weak global growth and concerns about China's growth. Specific to the property market are influences related to lending to investors and fears of an oversupply of apartments.

Graph 1 on the next page provides comparative data on Other Dwelling* Building Approvals for the Eastern Seaboard capital cities and Gold Coast City over the past 15 years. The data for 2015/16 is an estimate, based on ten months' data annualised. Note that not all building approvals proceed to construction.

For Greater Melbourne, Graph 1 shows that the peak of activity in 2014/15, (33,519 other dwellings, including ones in non-residential buildings), was 124% above the previous peak of 14,952 other dwellings in 2010/11.

In the Greater Sydney region, there were eight years to 2011/12 when other dwelling approvals were below the levels of the previous peak (on average 12,631 approvals per annum, compared with an average of 19,964 approvals per annum in the early 2000s).

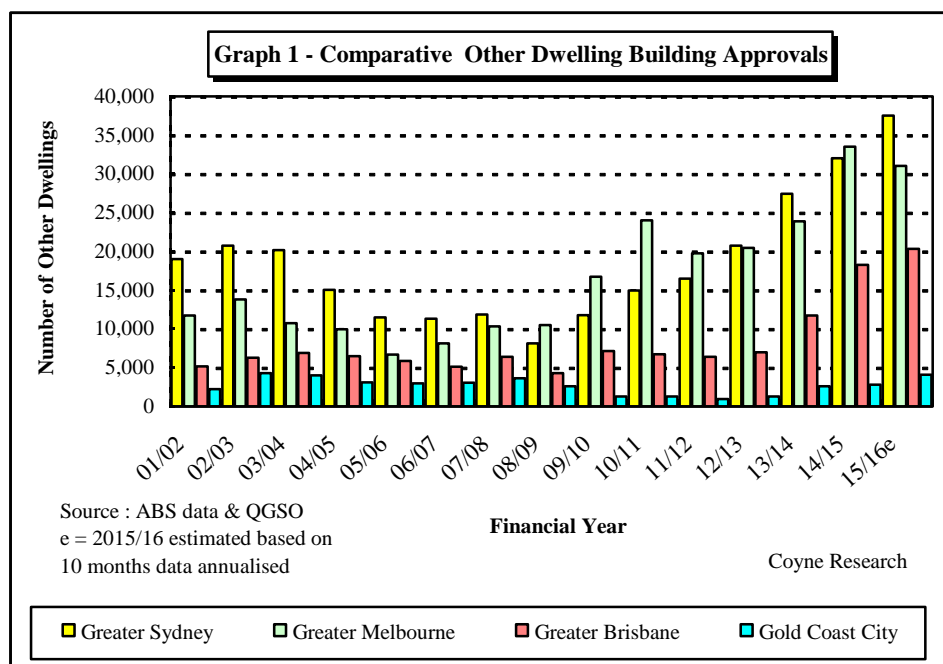
Since that time in the Greater Sydney region, approvals have risen sharply, to an estimated record of 37,523 other dwellings in 2015/16. Unlike Melbourne, these projects are more widely distributed across the Sydney region.

Graph 1 shows that other dwelling approvals also rose in the Greater Brisbane region over the past three years, reaching an estimated 20,312 approvals in 2015/16. This is more than three times the average of 6,150 other dwelling approvals over the previous 12 years to 2012/13.

* Other dwellings include residential units and townhouses.



View of the Parklands Village heart being developed by Grocon as the Athletes' Village for the Gold Coast 2018 Commonwealth Games (image courtesy of Grocon)



Although the peak of completions is yet to be experienced in the Greater Brisbane region, there is already evidence of lower take-up levels and a softer rental market. In some inner Brisbane suburbs, the median rent for two bedroom units fell by \$10 to \$15 per week over the year to March 2016 – source: Real Estate Institute of Queensland (REIQ).

The Gold Coast – A Cautious Approach

The smaller and more volatile Gold Coast market experienced four years of subdued activity to 2012/13, during which oversupplies of apartments were absorbed (an average of 1,185 other dwellings approved per annum, compared with the average of 3,241 approvals per annum over the previous eight years).

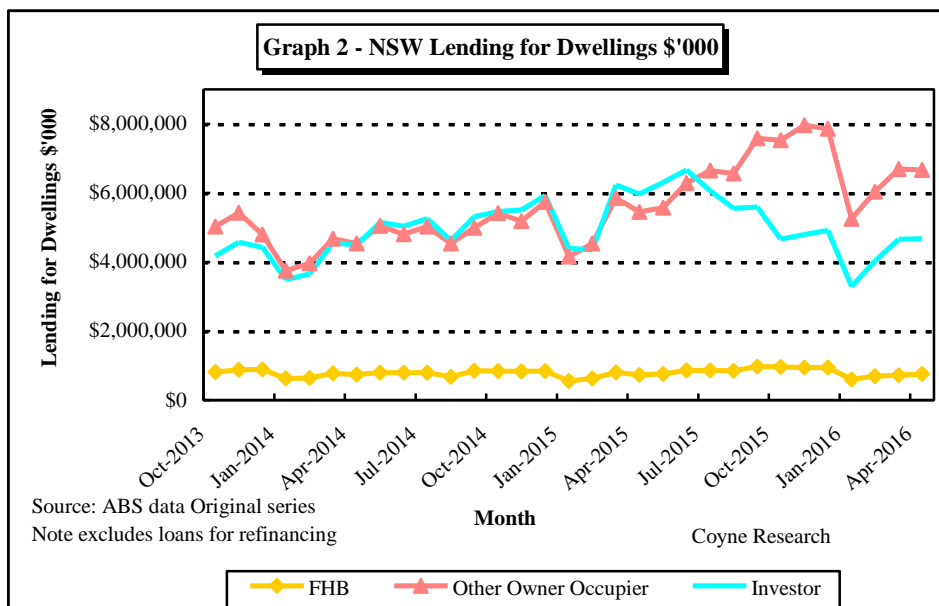
It is only over the past year that other dwelling building approvals have exceeded 4,000 dwellings, close to the previous peak reached in 2002/03 and 2003/04 (on average 4,158 other dwellings per annum). This can be attributed to a more cautious approach by developers and lenders to the Gold Coast market.

Although there are very large numbers of apartment projects with development approvals, especially along the Light Rail route from Southport to Broadbeach, only a small number have commenced construction and marketing.

The recent peak of other dwelling building approvals would have included the two largest Gold Coast projects: Grocon Limited’s \$550 million Parklands Residential Village, with 1,252 apartments and townhouses; and Wanda Ridong (Gold Coast) Development’s \$970 million Jewel, with 171 hotel rooms and 512 apartments. Note that Grocon plans to rent the Parklands apartments after their use as the Athletes’ Village during the Gold Coast 2018 Commonwealth Games.

Given the extent of potential new apartment construction, particularly in the southern capitals, it is not surprising that banks have altered their lending policies towards investors. This has been partly driven by actions of the Australian Prudential Regulatory Authority (APRA), which moved in late 2014 and 2015 to restrict the rate of increase of lending to investors and to increase capital adequacy requirements for banks.

Graph 2 on the next page shows that in New South Wales (NSW), loans to investors peaked at \$6.6 billion in June 2015. Such loans fell to a seasonal low in January 2016, before stabilising at \$4.7 billion in April 2016. This was 30% below the peak and in line with the average of \$4.8 billion per month over the 12 months to December 2014.



Investor Lending Stabilises Near Long-term Averages

During the upswing period in 2015, loans to investors in NSW reached a peak of 50% of all loans for dwellings. The long-term average (since 2007) was 37%, with 39% in April 2016.

Over the past year, loans for owner occupiers in NSW have risen, particularly for upgrade buyers. These reached \$8 billion in November 2015, or 58% of all loans, before stabilising at \$6.6 billion in April 2016 (55% of all loans). Lending to first home buyers (FHB) remains flat in NSW at 6% to 7%, compared with the long-term average of 11%.

In contrast with NSW, Graph 3 shows that lending to investors in Queensland rose briefly in early 2015, reaching \$2 billion in March and June (37% of all loans).

This compares with the average of \$1.5 billion per month in loans to investors during 2014. By April 2016, loans to investors in Queensland had returned to \$1.5 billion, or 31% of all loans, in line with the long-term average.

The graph shows that loans to upgrade owner occupiers in Queensland rose to a peak of \$3 billion in December 2015 and March 2016, easing to \$2.8 billion in April 2016. This level of activity, at 59% of all loans for dwellings, was slightly higher than the long-term average of 56%.

Loans to FHB in Queensland have remained in the 9% to 10% range over the past two years, below the long-term average of 12%.

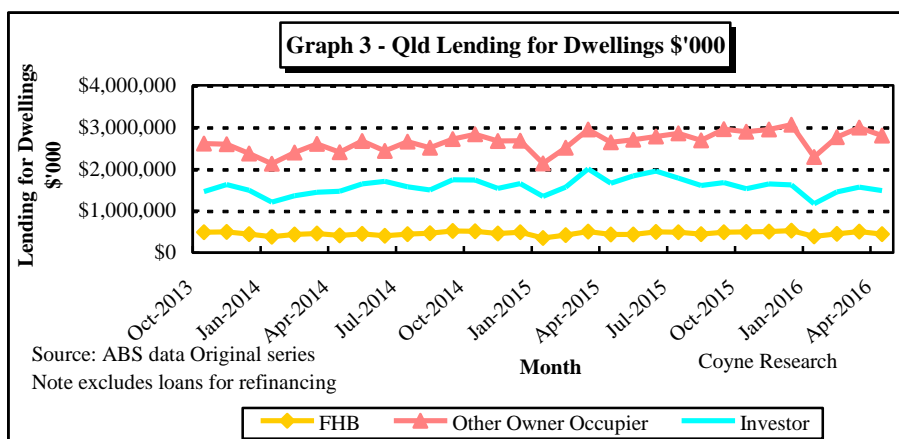


Table 1 – Comparative Home Value Index Changes

Location	Sydney	Melbourne	Brisbane	Gold Coast
Houses				
Month	3.6%	1.8%	-0.1%	-
Quarter	6.9%	2.4%	1.1%	-
Year-on-year	12.5%	14.6%	7.6%	7.2%*
Units				
Month	0.7%	0.5%	1.3%	-
Quarter	5.3%	-0.4%	0.8%	-
Year-on-year	15.5%	7.9%	2.4%	4.8%*

Source: CoreLogic RP Data *Hedonic Home Value Index* & CoreLogic RP Data *Regional Market Update* * year to March 2016

The data in Graph 3 suggests that the investor driven acceleration in residential markets that has seen significant price increases in southern capitals, has not influenced Queensland markets to the same extent. In fact, data from CoreLogic RP Data to the 31st May 2016, shown in Table 1, indicates Brisbane price increases have been subdued, compared with the southern capital cities.

Despite the changes to lending practices, a recent report from the Reserve Bank of Australia found off-the-plan sales to foreign buyers have remained high, especially in Sydney and Melbourne. However, developer incentives are being offered for some projects.

CoreLogic RP Data has raised the issue of settlement risk. This is exacerbated by the changes in bank lending practices and the likelihood of lower valuations at settlement than at the time of the off-the-plan sale. To date however, developers are reporting minimal numbers of units that have failed to settle, with such units being readily resold.

This partly reflects the motivations of foreign buyers, including a desire to invest capital in a stable country with a well regulated titles system, with the possibility of potential residency in future years.

Another consideration is that Australian apartment prices are lower, especially as the \$AUD has fallen.

Market Outlook

In summary, it is considered likely that many of the proposed apartment developments in the Eastern Seaboard capital cities will not proceed, or will be delayed. APRA and the banks have acted to reduce the level of lending to investors, so that such lending has stabilised in line with long-term averages. There are now more sales to owner occupiers, although lending to FHB is still low.

It is nevertheless considered that many apartment owners and buyers, who have committed to buy off-the-plan in these cities, may experience difficult conditions over the next few years, as a result of the level of new supply and the inability of the rental market to absorb this new supply.

Some apartments may not be placed in the rental market. Inner Melbourne has already seen evidence of this.

Sydney may be an exception to this, since the market was undersupplied for several years. As at April 2016, the Inner Sydney vacancy rate remained low at 1.3% and the overall metropolitan area 1.7% (source: REI NSW).

Gold Coast A Bright Spot

Following the end of the construction phase of the resources economy and lower commodity prices, Queensland, particularly central and northern Queensland, has been adversely impacted. In Brisbane, there has been an impact upon office markets, as resources companies downsized.

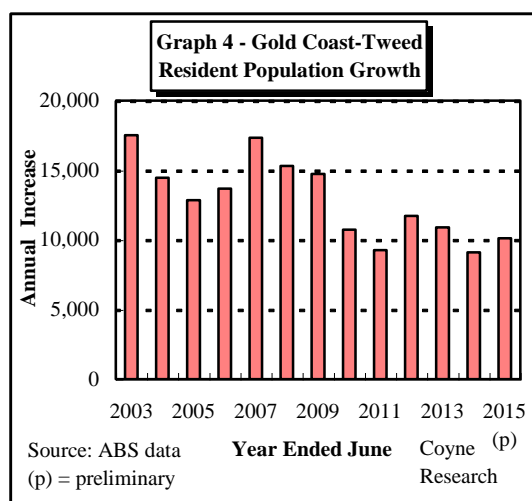
On the Gold Coast, the past few years have seen a strengthening of the local economy. This has continued in 2016, with an April 2016 unemployment rate of 5.3% and creation of 15,500 jobs for the year. This compares with the Queensland unemployment rate of 6.2%.

The improvement in the Gold Coast economy dates from the completion of two major infrastructure projects in 2014: the Gold Coast University Hospital and Stage One of the Light Rail.

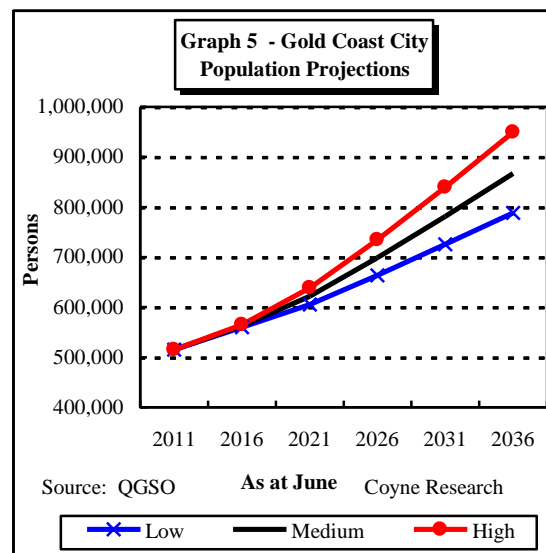
In the lead-up to the Gold Coast 2018 Commonwealth Games, there is ongoing construction activity on roads and venues, as well as the commitment to Stage Two of the Light Rail. While some have expressed concern about the Gold Coast economy after the Games, it seems unlikely the \$420 million Stage Two of the Light Rail would have occurred to the current schedule without the Games. Furthermore, as indicated on page 2, there is little evidence of an oversupply of apartments at this point.

In fact, the rental market on the Gold Coast has been experiencing record low vacancy rates – 1.1% in the December Quarter 2015, easing to 1.5% in March Quarter 2016. Over the year to March 2016, the median rent for two bedroom units rose by \$25 per week and by \$20 per week for three bedroom houses (source: REIQ).

This trend partly reflects the Gold Coast’s relatively strong population growth. Graph 4 shows that the Gold Coast-Tweed region saw an increase of 10,124 persons in 2014/15, based on preliminary data from the Australian Bureau of Statistics (ABS). This is in line with the previous five years.



The Queensland Government Statistician’s Office (QGSO) recent population projections envisage continued strong growth.



Graph 5 shows that Gold Coast City is expected to see an average increase of 14,000 people per annum over the 20 years to 2036 (under the medium series projection).

Tourist Demand for Apartments

These population projections reflect growth in the resident population. The Gold Coast has always accommodated a visitor population on top of this. It is estimated that visitors add over 80,000 people to the Gold Coast-Tweed population of over 600,000 residents. This increases in peak periods to over 100,000 extra people.

The increased capacity of flights has seen a significant lift in international visitors to the Gold Coast. In the year to March 2016, 949,000 international visitors spent 9.8 million visitor nights, while 3.68 million domestic overnight visitors spent 13.4 million visitor nights. International visitors, lead by China, accounted for 20% of overnight visitors, 42% of visitor nights and 30% of regional expenditure. Daytrippers added a further 8.3 million visitors and spent \$885 million (source: Tourism Research Australia).

Many of the proposed new apartments along the Light Rail corridor will be targeting southern state and international investors, who will use their apartments for holidays and put them into the holiday letting pool for the rest of the year. This is an essential part of the continual upgrading of our tourism accommodation stock.

Insufficient Broadhectare Land

Over recent years, the number of vacant land sales has increased on the Gold Coast. Some developers over the past year have had trouble keeping up with demand.

The recent population projections for Gold Coast City show a total 2036 population of 866,634 residents (an increase of just over 300,000 residents over the next 20 years).

This 2015 medium series projection is only 4.3% below the 2013 medium series projection. At that time, the QGSO, in its Broadhectare Study for the Gold Coast, estimated there was about nine years' supply of land available.

This included a potential yield of 20,730 dwellings from 1,927 hectares of broadhectare land suited to standard urban densities (4-20 dwellings/hectare). The majority of the anticipated dwelling yield of 52,557 dwellings for Gold Coast City (58%) was expected to be on 567 hectares at higher densities (>20 dwellings/hectare).

The most recent QGSO quarterly report to September 2015 indicates that the supply of broadhectare land on the Gold Coast had fallen to 3,650 hectares (8% down on the 3,964 hectares of 2013). It is likely that the current supply of broadhectare land is now below the nine years' supply of 2013.

For planning purposes, in the past it has been considered appropriate to have sufficient zoned broadhectare land for 15 years. This is intended to meet sudden upswings in demand and put downward pressure on prices.

Since the Gold Coast has insufficient greenfield land for future population growth, it is likely there will be more pressure to release land currently protected, such as the cane fields.

Alternatively, over the medium to longer term, future prospective Gold Coast residents may be living in the adjoining Tweed Shire or Logan City.

The need to address the future broadhectare supply on the Gold Coast is reinforced by the stability of the median land price over several years at around \$230,000 to \$240,000. This is despite an increased number of smaller lots seeking to provide affordability, especially to FHB.

Recent Trends

Over the year to September 2015, the QGSO report identified 2,525 lots were registered (up by 73% on 2014). This was the highest number since 2008. The three dominant size categories were 350<450 m² (33%), 450<600 m² (34%) and 600<800 m² (17%).



Houses on 250 m² lots (10 metre frontages) at Highland Reserve at Upper Coomera

The increase in potential availability has mirrored the increase in demand. In the year to September 2015, there were 2,603 lots consumed on the Gold Coast (based on a lagged series of house building approvals).

This compares with the 3,455 uncompleted lots[#] in the pipeline with operational works approvals (1.3 years' supply) and with all uncompleted lots[#] in the pipeline – 8,595 lots, or 3.3 years' supply (source QGSO).

[#] uncompleted lots have development approval, but have not proceeded to survey plan certification.

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