

# PROPERTY INVESTMENT MARKET REPORT

- MARKET INTELLIGENCE FROM FORRESTER COHEN



*This is an image of a typical boutique townhouse development in Pascoe Vale, Melbourne.*

## MELBOURNE, VIC AUGUST 2017

This report examines the considerations for investment in Melbourne for houses, townhouses and apartments. The report uses metrics developed by Forrester Cohen to correlate local market conditions with factors that have historically driven capital growth.

**Melbourne** has experienced unprecedented population growth over the last decade. ABS statistics show that the Victorian population has increased from 2005 to 2015 by about 1M people<sup>1</sup> with most settling in Melbourne.

Net overseas migration was 54,052 people in 2014-15<sup>2</sup> with another 10,190 moving from interstate<sup>3</sup>. This was a decrease in numbers due to lower migration to Australia overall.

One top of this there were 401,423 student visas on issue in Australia at June 2016<sup>4</sup>. Lodgments were up 7.8% on the previous year while granted visas were up 3.8%<sup>5</sup>. Juwai.com tells us 46,000 Chinese students are currently studying in Australia quoting the Department of Education in 2016<sup>6</sup>.

A recent Government study states that international students were contributing \$19B to the Australian economy in 2014-15. They estimated that \$5.85B was spent in Victoria alone<sup>7</sup>. If we assume that there were 30.8% of the students in Australia studying in Victoria this would equate to 123,596 people seeking accommodation to rent or buy.

Then there were 457 visa holders and other immigrants seeking to meet shortages in labour in Australia. Plus, there are the working holiday tourists and back packers seeking accommodation.

Population growth is changing this city. Its colloquial Australian heart is growing to include a strong international community.

Greater Melbourne residential housing capital growth rates have been amongst the highest in the world according to a recent Frank Knight report<sup>8</sup>. With continued strong drivers for population growth this situation doesn't appear to be changing soon.

<sup>1</sup>[www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/3218.02014-15?OpenDocument](http://www.abs.gov.au/AUSSTATS/abs@.nsf/DetailsPage/3218.02014-15?OpenDocument) Population estimates by LGA

<sup>2</sup>[www.abs.gov.au/AUSSTATS/abs@.nsf/mf/3412.0](http://www.abs.gov.au/AUSSTATS/abs@.nsf/mf/3412.0)

<sup>3</sup>[www.abs.gov.au/AUSSTATS/abs@.nsf/mf/3412.0](http://www.abs.gov.au/AUSSTATS/abs@.nsf/mf/3412.0)

<sup>4</sup>[www.border.gov.au/ReportsandPublications/Documents/statistics/student-temp-grad-programme-report-2015-16.pdf](http://www.border.gov.au/ReportsandPublications/Documents/statistics/student-temp-grad-programme-report-2015-16.pdf)

<sup>5</sup>[www.border.gov.au/ReportsandPublications/Documents/statistics/student-temp-grad-programme-report-2015-16.pdf](http://www.border.gov.au/ReportsandPublications/Documents/statistics/student-temp-grad-programme-report-2015-16.pdf)

<sup>6</sup>[list.juwai.com/news/2016/09/australian-foreign-buyer-taxes-won-t-put-off-chinese-here-s-why?](http://list.juwai.com/news/2016/09/australian-foreign-buyer-taxes-won-t-put-off-chinese-here-s-why?)

<sup>7</sup>[internationaleducation.gov.au/research/research-papers/Documents/ValueInternationalEd.pdf](http://internationaleducation.gov.au/research/research-papers/Documents/ValueInternationalEd.pdf)

<sup>8</sup>[www.dropbox.com/home/Australian%20Market%20and%20Resources/Frank%20Knight?preview=piri\\_100.pdf](http://www.dropbox.com/home/Australian%20Market%20and%20Resources/Frank%20Knight?preview=piri_100.pdf)

**Infrastructure investment** in Melbourne has not kept pace with the increasing population. Roads are clogged causing increasing travel times. This drives appeal for properties closer to the city with access to public transport, that are below the median price of Greater Melbourne.

Houses in the middle to inner rings with good access to employment centres are becoming increasingly expensive. The median price for houses in Greater Melbourne was \$928,000 on 31<sup>st</sup> January 2017<sup>9</sup>. Apartments had a median price of \$541,000 at the same time<sup>10</sup>.

Melbournians favour houses with capital growth rates for all dwellings at 11.82% for the year to 31<sup>st</sup> January 2017. This was divided into 12.86% for houses and 2.77% for units<sup>11</sup>.

Many newer Australian's and first time home buyers are seeking affordability. This is driving uptake of land in peripheral estates; the growth of satellite cities such as Geelong, Ballarat and Bendigo; and affordable infill housing in existing suburbs. Townhouses offer the better opportunity compared to apartments as they are more like houses. At some stage apartment living is expected to become more acceptable, due to price and access to employment, plus cultural and life style amenities.

Many Asian migrants and students are not constrained by Australian real estate prices and form a second tier of demand. They seek quiet, safe and well serviced locations with access to education. Townhouse or apartment living is very acceptable.

**Melbourne's population growth** is continuing to drive demand, and supply is being delivered through record levels of greenfield peripheral housing estates, and through townhouses and apartments. The inner city is currently over supplied with apartments and their demand for tenants is keeping rental returns soft.

Houses, townhouses and apartments that have access to transport, local amenities and education have done well in Sydney. As Melbourne's population approaches Sydney's population this is anticipated to drive more apartment living. There are three groups of tenants to consider: the Asian investment market seeking accommodation for tertiary students or younger children with good primary and secondary schools; locals seeking lifestyle; and new immigrants seeking access and affordability.

<sup>9</sup>[www.corelogic.com.au/research/monthly-indices.html](http://www.corelogic.com.au/research/monthly-indices.html)

<sup>10</sup>[www.corelogic.com.au/research/monthly-indices.html](http://www.corelogic.com.au/research/monthly-indices.html)

<sup>11</sup>[www.corelogic.com.au/research/monthly-indices.html](http://www.corelogic.com.au/research/monthly-indices.html)

**The Forrester Cohen research methodology** seeks to answer the questions many investors ask. “Where should I buy?” “When should I buy?” and “What should I buy?” The following analysis identified the key metrics to be analysed when assessing an area to identify the opportunity for the investor.

## MACROECONOMIC BACKGROUND

**The key macro drivers of capital growth** are population growth, availability of finance, confidence, infrastructure and Government policy. We focus on the current trends for supply and demand and then overlay the information about the capital growth drivers as disrupters of current trends. This helps us to identify and describe the opportunity and its considerations.

## ECONOMIC OVERVIEW

Melbourne’s GDP was \$356B and grew at 2.4%<sup>12</sup> in 2014-15 according to State Government figures<sup>13</sup>. In 2015-2016 SCG Economics and Planning, an independent College of Professionals, estimated its GDP as 28.4% of Australia’s total representing 3.1% growth over the previous 12 months. Financial and Insurance services grew 0.7% and construction grew 0.7% while manufacturing fell with its share of the Melbourne economy at a record low of 6.9%<sup>14</sup>.

CommSec<sup>15</sup> gives us an overview of eight economic indicators quarterly for each state and territory: economic growth; retail spending; equipment investment; unemployment; construction work done; population growth; housing finance and dwelling commencements.

Victoria was solidly in second place to Sydney. Victoria is ranked first in Australia for its population growth and housing finance according to CommSec for January 2017. It is second on construction and dwelling starts. However, its weakness continues to be unemployment. Later in 2017 the Toyota factory will close with the loss of 2,500 direct jobs and many indirect.

To continue to maintain its economic growth and attract people to immigrate or migrate to this city, it needs to create more jobs. The recent announcement of the Melbourne METRO project<sup>16</sup> and the Transurban approach on the Western Distributor<sup>17</sup> are strong projects to link the east and west of the city and drive employment.

## FINANCE AVAILABILITY

This is a measure of the willingness of lending institutions to lend money. Looser policies are largely responsible for our ability to pay more for property and hence create capital growth.

APRA imposed restrictions on lending to investors in May 2015. They required the lending institutions to cap investor-lending growth at 10% of the previous year’s levels, and to hold more capital. In 2015 we saw some sharp changes in lending policies. In 2016 there was a relaxation as bank lending came into line with the APRA requirements.

Sharp rises in investor borrowing at the end of 2016 have driven expected to drive further APRA intervention and some tightening of availability of finance. Banks are also predicted to begin to raise interest rates due to their costs of finance, and the RBA to follow due to economic pressures.

Lending to foreign nationals and non resident Australians has also tightened. This was expected to reduce demand from overseas investors and some developers reported reduced demand. However recent insights show the Chinese have many cash buyers or larger deposits and can manage much lower LVRs.

In 2007 Chinese Government policy restricted the ability of their population to get funds out of China for international property investment. This has seen the Chinese, that need to borrow to buy, preferring long lead time purchases such as apartments, to enable them to get funds together over time.

Availability of finance has historically been a prerequisite for property price growth.

<sup>12</sup>[www.invest.vic.gov.au/resources/statistics/economic-indicators](http://www.invest.vic.gov.au/resources/statistics/economic-indicators)

<sup>13</sup>[www.invest.vic.gov.au/resources/statistics/economic-indicators](http://www.invest.vic.gov.au/resources/statistics/economic-indicators)

<sup>14</sup>[www.sgsep.com.au/publications/gdp-major-capital-city-2015-2016](http://www.sgsep.com.au/publications/gdp-major-capital-city-2015-2016)

<sup>15</sup>[www.commsec.com.au/content/dam/EN/StateoftheStates/VIC\\_State\\_of\\_the\\_States\\_January2017.pdf](http://www.commsec.com.au/content/dam/EN/StateoftheStates/VIC_State_of_the_States_January2017.pdf)

<sup>16</sup>[metrotunnel.vic.gov.au/](http://metrotunnel.vic.gov.au/)

<sup>17</sup>[www.transurban.com/our-operations/our-projects/western-distributor](http://www.transurban.com/our-operations/our-projects/western-distributor)

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## POPULATION GROWTH

**Population growth** is the headline for Melbourne. Its rate of growth exceeds most western nations and many developing nations. This consistent driver of demand has steadily changed the face of this city. The statistics for these changes are in the introduction of this report.

Add to this that Melbourne is the most searched Australian city on Juwai.com for Chinese students and investors looking to invest in Australian property. Their appetite for property has not been diminished by the recent increase in stamp duties and land taxes in Victoria.

Fresh drivers for population growth are the changes to the visa system by the Federal Government. In July 2016 a new student and guardian visa was introduced to support children as young as primary school studying in Australia. In September 2016 Juwai.com announced that searches for Australian property increased by 20% at that time. This was on a base of 35% of all searches for Australia<sup>18</sup>.

Secondly the Government has announced a new ten year visa open to all Chinese citizens that gives them repeated entry to Australia and a stay of up to 3 months on each occasion. The first visas of this style were written in late 2016<sup>19</sup>. This is being heralded as making it easier to visit Australia for tourism, business and to support children in their education.

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## GOVERNMENT POLICY

**Infrastructure Victoria**, the Statutory Authority formed in October 2015, has been tasked to undertake the huge process of consultation to deliver a framework of infrastructure priorities to the Parliament. The infrastructure investment plan is to cover the next 30 years. It was delivered in Dec 2016. This gives an indication of their priorities.

1. Increasing densities in established areas and around employment centres to make better use of existing infrastructure.
2. Introducing a comprehensive and fair transport network pricing regime to manage demands on the network
3. Investing in social housing and other forms of affordable housing for vulnerable Victorians to significantly increase supply<sup>20</sup>.

The Government continues to expand the footprint of Melbourne through the release of greenfield land. There is currently a 12 -18 month wait for land to register and settle in many estates. They have also changed local planning laws to increase density. Fisherman's Bend, the car manufacturing suburb, is planned to be redeveloped as a greener residential neighbourhood.

The Victorian Government recently announced increased stamp duty and land taxes for foreign investors. According to Juwai.com and numerous property developers it has not dampened demand for Australian property.

<sup>18</sup>[list.juwai.com/news/2016/04/juwai-reveals-top-10-chinese-buyer-picks-for-q4-2015](http://list.juwai.com/news/2016/04/juwai-reveals-top-10-chinese-buyer-picks-for-q4-2015)

<sup>19</sup>[list.juwai.com/news/2016/04/juwai-reveals-top-10-chinese-buyer-picks-for-q4-2015](http://list.juwai.com/news/2016/04/juwai-reveals-top-10-chinese-buyer-picks-for-q4-2015)

<sup>20</sup>[www.infrastructurevictoria.com.au/sites/default/files/images/IV%2030%20Year%20Strategy%20WEB%20V2.PDF](http://www.infrastructurevictoria.com.au/sites/default/files/images/IV%2030%20Year%20Strategy%20WEB%20V2.PDF)

## Western Distributor<sup>21</sup>

The \$5.5 billion Western Distributor Project will provide an alternative river crossing to the West Gate Bridge and direct access to the Port. The Victorian Government is progressing the project planning milestones through exclusive negotiations with Transurban as part of Stage 4 of the State's Market-led Proposals Guideline.

## Monash Freeway Upgrade

The Monash Freeway Upgrade will improve safety and reliability along the 44 kilometres between Chadstone and Pakenham, extending what is already Australia's longest stretch of managed motorway. This is part of the Western Distributor project.

## The CityLink Tulla<sup>22</sup>

The CityLink Tulla Widening project involves adding new lanes and other measures to improve traffic flow across 24 kilometres of freeway between the CityLink tunnels and Melbourne Airport. The project is jointly funded by the federal government, the Victorian state government and Transurban (CityLink's operator) and is forecast to be completed in 2018.

Regional Rail Link<sup>23</sup> project delivered June 2015. New dedicated rail line for country trains from Ballarat, Bendigo and one line from Geelong with dedicated Southern Cross platforms. Increased reliability for travel without congestion of suburban services.

Ballarat rail to be duplicated to Melton \$518M, improved platforms and more car parking at stations. Announced April 2016.

Melbourne Metro Tunnel to link west and eastern services is in planning and procurement stages with construction forecast to start in 2018 and delivery in 2026. The overall project is at EIS stage. New stations will be at Arden, Parkville, CBD North, CBD South and Domain. An expansion of the suburb of Arden is planned with an additional 15,000 residents<sup>24</sup>. This will provide huge changes in accessibility for inner city residents.

The Victorian Government allocated \$2.4 billion in its 2015-16 budget to remove at least 20 level crossings by 2018. These selected sites form the basis of a long-term strategic plan being developed to remove all 50 level crossings by 2022.

**Melbourne Airport** will invest \$10B over 20 years to expand its services<sup>25</sup>.

These projects have included:

- A major upgrade of the access roads for passengers into and out of the precinct completed in 2015
- T4 Upgrade completed 2015
- Increased business lounges and passenger services completed early 2015
- Southern apron expansion completed late 2015.
- Increased taxiway, 45,000sqm delivered early 2016
- TNT warehouse at 45,000sqm due for completion late in 2016
- Toll IPEC warehouse at 71,000sqm due for completion in late 2016
- Quest Melbourne Airport has just opened.
- Planning for a third runway is underway.
- Car park lights being converted to LEDs

**Melbourne Port** has just sold for \$9.7B, resulting in Government revenue of \$11B, to a consortium of Future Fund, Australia's QIC, Global Infrastructure Partners (GIP) and Canadian pension group OMERS<sup>26</sup>.

<sup>21</sup>[economicdevelopment.vic.gov.au/transport/major-projects/western-distributor](http://economicdevelopment.vic.gov.au/transport/major-projects/western-distributor)

<sup>22</sup>[citylinktullawidening.vic.gov.au/about](http://citylinktullawidening.vic.gov.au/about)

<sup>23</sup>[www.heraldsun.com.au/news/victoria/regional-rail-link-makes-trains-to-melbourne-cbd-faster-from-country-than-from-suburbs/news-story/2ffa8b677cb60d69d3e98f02c10a7105](http://www.heraldsun.com.au/news/victoria/regional-rail-link-makes-trains-to-melbourne-cbd-faster-from-country-than-from-suburbs/news-story/2ffa8b677cb60d69d3e98f02c10a7105)

<sup>24</sup>[www.abc.net.au/news/2016-09-01/plans-for-new-suburb-in-melbourne's-inner-north-unveiled/7804530](http://www.abc.net.au/news/2016-09-01/plans-for-new-suburb-in-melbourne's-inner-north-unveiled/7804530)

<sup>25</sup>[melbourneairport.com.au/about-melbourne-airport/current-projects/overview.html](http://melbourneairport.com.au/about-melbourne-airport/current-projects/overview.html)

<sup>26</sup>[www.afr.com/business/transport/shipping/port-of-melbourne-reaps-97-billion-for-victoria-20160919-grj9l6](http://www.afr.com/business/transport/shipping/port-of-melbourne-reaps-97-billion-for-victoria-20160919-grj9l6)

Employment is a key driver of homeowner confidence. It underlies the ability and willingness to pay more for property. The capital growth of property in Melbourne has given home owners and investors increased confidence about the amount of their wealth which is reflected in the increased retail spending figures.

CommSec reports on the results compared to decade averages. A growing and expanding economy is demonstrated by its level above these averages.

- VIC's economic growth is currently at about 22.3% above decade averages<sup>27</sup>.
- Retail spending is also up at 13.3%<sup>28</sup>.
- Population growth is strong at 2.07%<sup>29</sup>.

## CAPITAL GROWTH

Dwelling prices in Greater Melbourne have risen in value by 11.82% for the year to January 2017<sup>30</sup>. Within these figures units in Greater Melbourne have risen 2.77%, and houses 12.86%<sup>31</sup>. Above average capital growth opportunity correlates with the relationship of the property to median price and the accessibility to employment areas.

## VACANCY RATES

Vacancy rates at 3% are widely held to favour the investor. Vacancy rates in Greater Melbourne for all dwellings were 2.5% in December 2016<sup>33</sup>. They usually rise from August to December and then drop back in January to trend flat for the balance of the year. Since 2012 this plateau from January to August has also been trending down.

## DAYS ON THE MARKET (DOM)

DOM for Greater Melbourne have trended slowly up from May to August 2016 from 66 to 72<sup>32</sup>. When DOM is trending up it indicates demand is slowing. However, a concurrent rise in median price indicates supply not meeting demand.

## GROSS RENTAL RETURNS

Gross rental returns for Greater Melbourne are reported at 3.2% for houses and 4.1% for units<sup>34</sup>. This makes units easier to leverage and hold with rental income.

<sup>27</sup>[www.commsec.com.au/content/dam/EN/ResearchNews/CommSec\\_State\\_of\\_the\\_States\\_January2017.pdf](http://www.commsec.com.au/content/dam/EN/ResearchNews/CommSec_State_of_the_States_January2017.pdf)

<sup>28</sup>[www.commsec.com.au/content/dam/EN/ResearchNews/CommSec\\_State\\_of\\_the\\_States\\_January2017.pdf](http://www.commsec.com.au/content/dam/EN/ResearchNews/CommSec_State_of_the_States_January2017.pdf)

<sup>29</sup>[www.commsec.com.au/content/dam/EN/ResearchNews/CommSec\\_State\\_of\\_the\\_States\\_January2017.pdf](http://www.commsec.com.au/content/dam/EN/ResearchNews/CommSec_State_of_the_States_January2017.pdf)

<sup>30</sup>[www.corelogic.com.au/research/monthly-indices.html](http://www.corelogic.com.au/research/monthly-indices.html)

<sup>31</sup>[www.corelogic.com.au/news/corelogic-june-quarter-regional-report-released](http://www.corelogic.com.au/news/corelogic-june-quarter-regional-report-released)

<sup>32</sup>[www.homepriceguide.com.au](http://www.homepriceguide.com.au) 1st August 2016

<sup>33</sup>SQM Research, vacancy rates.

<sup>34</sup>[www.sqmresearch.com.au/property-rental-yield.php?region=vic%3A%3AMelbourne&type=c&t=1](http://www.sqmresearch.com.au/property-rental-yield.php?region=vic%3A%3AMelbourne&type=c&t=1)

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## SUMMARY

Melbourne has had unprecedented population growth that is driving capital growth strongly in areas with good access to transport, employment and valued educational centres. Capital growth is driven by increased demand. Gentrification areas offer above average opportunity as increased demand brings increased life style amenities, willingness to pay more for rent or purchase; and prices in surrounding suburbs increase.

Melbourne inner city is currently over supplied with apartments. Bank lending policy should indicate the risk profile they associate with this through postcode based LVR policies.

With continued population growth fuelling demand for housing we can expect to see continued capital growth, especially in locations with good access to employment centres such as the CBD.



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