

# Residential Development Market Link Sydney



## Introduction

The residential development property market has been in a period of turmoil since the onset of the Global Financial Crisis (GFC). The GFC saw access to project debt and equity virtually dry up to all but those who had a stellar record. Whilst funding restrictions have eased, banks are undertaking greater scrutiny of new projects. Following from the easing of credit restrictions, demand for development sites improved, with 2010 seeing a significant increase in the number of sites sold. Despite the lessons learnt over the GFC, it still appears that many buyers are not appropriately pricing in the additional risk of non-approved sites, with several sales of non-approved sites recording comparable rates to approved sites.

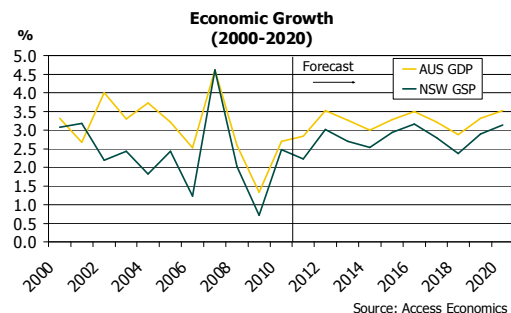
For the purpose of this report, we have reviewed the conditions in the residential development market. To provide the reader with a greater understanding of the current market dynamics, this report focuses on medium density development as opposed to greenfield residential development.

## Economic Conditions

### Economic Growth

The Australian economy grew in the second quarter of 2011, with quarterly economic growth bouncing back after falls in the first quarter of 2011 associated with the impact of the Queensland floods. GDP rose by 1.2% in the second quarter of 2011, after falling by 1.2% in the first three months of 2011.

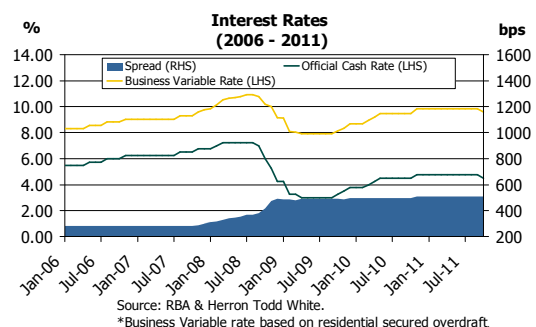
The New South Wales economy has a greater exposure to the finance and professional service sectors, than the mining and resource based states. As a result, economic growth within the NSW economy has under-performed the Australian economy since the onset of the Global Financial Crisis in early 2008.



In the 12 months to June 2010, the NSW economy grew at a rate of 1.71% compared to the Australian economy which grew by 3%, over the same period.

### Interest Rates

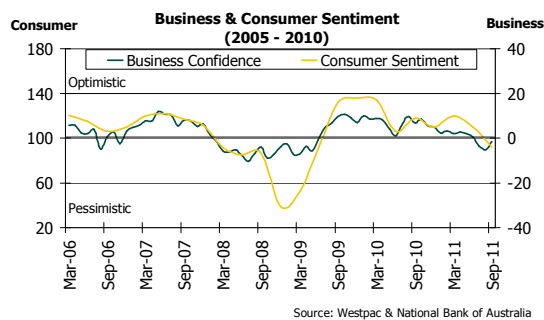
With the global economic outlook now less than certain and domestic demand seemingly reduced, the Reserve Bank of Australia (RBA) cut interest rates by 25 basis points to 4.5% in November.



The RBA noted that Australia's terms of trade have now peaked and are expected to fall in 2012, household spending remains subdued and the high exchange rate is limiting demand. While recent inflation statistics have indicated heightened inflation, the RBA has looked beyond this headline figure, noting that a return to pre-flood production levels is expected to place downward pressure on prices.

### Business and Consumer Sentiment

Business confidence levels are a key lead indicator of future spending and economic growth. After recording a rise in the March quarter, business confidence fell significantly in the ensuing six months. Confidence was impacted in the finance and mining sectors with the high Australian dollar, continued restraint from consumers and concerns about the global outlook continuing to have an impact. The fall in consumer confidence has also had a direct impact on business confidence, with the rumoured scaling back of future employment plans.



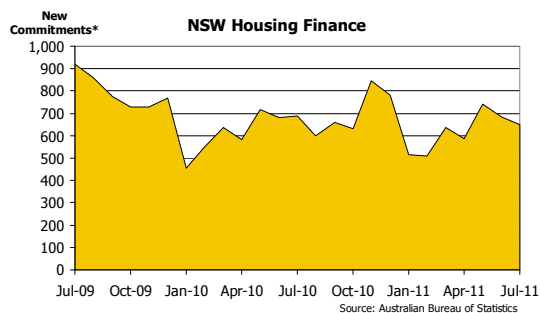
After four consecutive falls in consumer sentiment following the announcement of the carbon tax and the deterioration of the global financial markets, consumer confidence improved in September and October, albeit from a low base. In commenting on the shift in consumer sentiment, Westpac noted that the outlook for reduced interest rates and the movement by the major Australian banks to reduce

their fixed mortgage rates, has helped to boost confidence.

Despite this rise, confidence remains low overall, with consumers remaining concerned about the 12 month economic outlook. Looking forward, the decision to reduce the interest rate by 25 basis points will likely boost confidence. Any boost however, is likely to only serve to wind back the falls recorded in the first half of 2011.

### Housing Finance

After rebounding in 2009 following the doubling of the first home owners grant, Australian finance commitments for new dwellings have been weak, with buyers uncertain about the direction of the Australian economy and the possibility of future interest rate rises.



In NSW, finance commitments for new dwellings improved over the first half of 2011. Commitments for new dwellings however remain low, not yet returning to pre-GFC levels. Despite the low levels of consumer confidence, the NSW property market has largely outperformed the greater Australian market, recording a stronger uptake in new finance commitments from the seasonal low recorded in January.

## Population Growth Outlook

From a residential property development perspective, the demographic outlook for the Sydney metropolitan area remains strong. As Australia's largest city, the region continues to benefit from strong population growth, driven primarily by high levels of net overseas migration.

The continual increase in population and the shifting demographic profile is continuing to drive the demand for dwellings located throughout the Sydney metropolitan area.

### Population Growth

Over the coming five years the population within Sydney is expected to grow by 241,000 people, with the North West and South West sub-regions accounting for much of this growth.

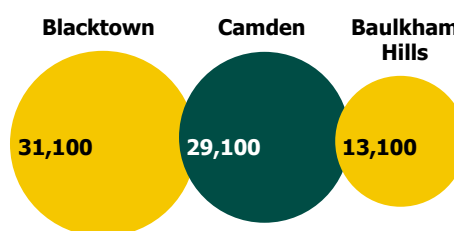
#### Forecast Population Increase

Sub-region	2011-2016	2016-2021
North West	70,400	70,700
South West	61,000	79,200
West Central	42,600	32,000
Inner West	18,051	12,692
South	15,900	11,100
North	11,600	9,500
East	8,900	7,700
Inner North	8,100	7,000
North East	5,200	7,400

Source: NSW Department of Planning

Reflecting these forecasts, population growth within the metropolitan area is expected to be focused on these outer suburban locations. As shown in the chart below, the Blacktown, Camden and Baulkham Hills local government areas are expected to record the greatest increase in population, over the coming five years.

#### Three Fastest Growing LGA's 2011 - 2016

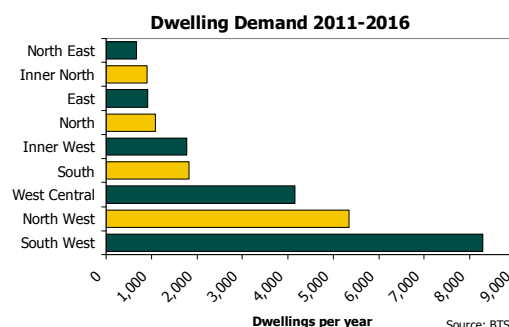


Source: NSW Department of Planning

In the Inner Ring, the local government areas of Randwick, North Sydney and Ashfield are forecast to record the greatest increase in population growth with an additional 5,600, 3,200, and 2,100 additional people respectively.

### Dwelling Demand

Demand for additional dwellings remains high within the Sydney metropolitan area, with over 124,000 dwellings required over the five years to 2016.

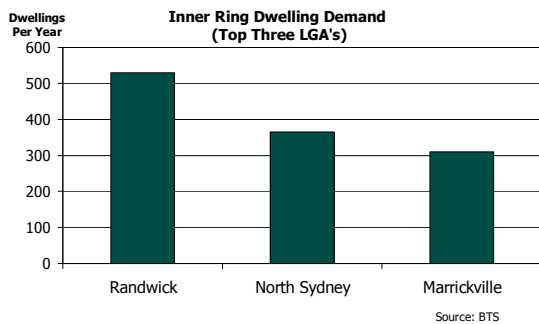


Source: BTS

As shown in the chart above, the demand for dwellings is expected to be highest in the South

West with some 8,285 new dwellings required per year.

While demand for new dwellings is highest within the outer western suburbs, a shift in housing preferences has seen the demand for dwellings located in inner suburban locations rise.



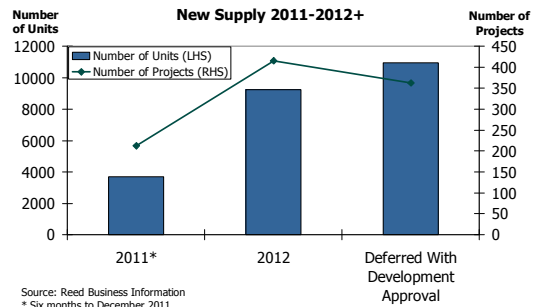
As shown in the chart above, dwelling demand within the inner ring is expected to be strongest in the Randwick LGA, with the location benefiting from its close proximity to the Sydney CBD and nearby beaches.

## Market Conditions

### Dwelling Supply

Over the 18 months to December 2012 it is expected that some 628 projects encompassing approximately 12,941 new apartments or town houses will reach completion. Despite this increase in supply, the greater Sydney market is expected to remain undersupplied, as new construction fails to match the forecasted population increase.

Additionally, there are some 360 projects encompassing over 10,000 units that have development approval, but which have subsequently been deferred due primarily to financing difficulties or poor pre-sales. In addition to these sites, there are an additional 4,800 new units currently awaiting development approval.

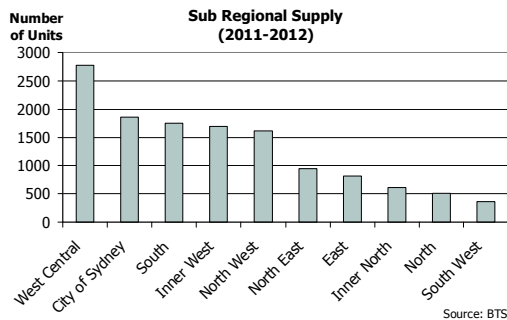


## SUPPLY ANALYSIS

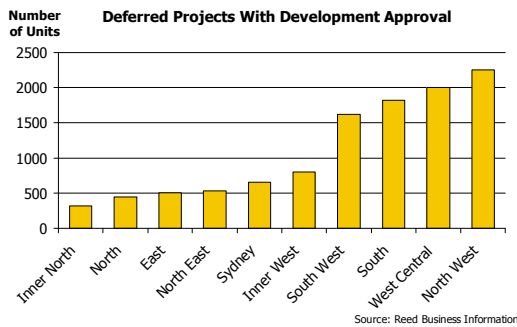


<b>Address:</b>	15-17 Corona Ave Roseville
<b>Developer:</b>	Hyecorp Pty Ltd
<b>Details:</b>	Two residential unit buildings with dual street frontage.
<b>Units:</b>	48
<b>Status:</b>	Approved
<b>GBA:</b>	4,718 sqm
<b>FSR:</b>	1.3:1
<b>Stage:</b>	Construction

The West central sub-region is expected to record the greatest increase in supply over the 18 months to December 2012, with an additional 2,774 apartments expected to reach completion in this time.



As shown above, the western and southern regions account for the greatest number of deferred units, with these regions recording a significant increase in projects prior to the global financial crisis. In the South West, the number of deferred units is four times higher than the number of units due for completion in the 18 months to December 2012.



## Market Demand

Demand for both development sites and new apartments, varies significantly across the Sydney region. Reflecting the heightened demand for new apartments in close proximity to the CBD, demand for development sites is highest in the Inner West and Inner North sub-regions, with these locations recording increased sale activity in the first six months of 2011.

## Market Demand

Sub-region	New Units	Sites
East	Moderate	Low
Inner West	Strong	Strong
Inner North	Strong	Strong
North	Strong	Low
North East	Moderate	Low
North West	Low	Low
South	Strong	Moderate
South West	Low	Low
West Central	Moderate	Low

Source: Herron Todd White

The table above indicates a disparity between the demand for new apartments and the demand for new development sites in the North sub-region. This gap in demand has come as a result of the oversupply of new apartments in the North sub-region over the past five years, subsequently constraining end sales values and increasing selling periods.

While the NSW government has forecast that the North West and South West will be subject to the highest dwelling demand over the next 20 years, it is clear this demand is limited to detached dwellings, with both the demand for new apartments and development sites remaining low. In the South West, discussions with marketing agents reveal that many developers are leasing out units in an attempt to secure a cash flow, awaiting an improvement in market conditions before re-commencing marketing.

Elsewhere in Sydney, demand for new units remains highly price sensitive, with demand for units priced under \$600,000 far greater than the demand for units priced above this point.

## SALES ANALYSIS

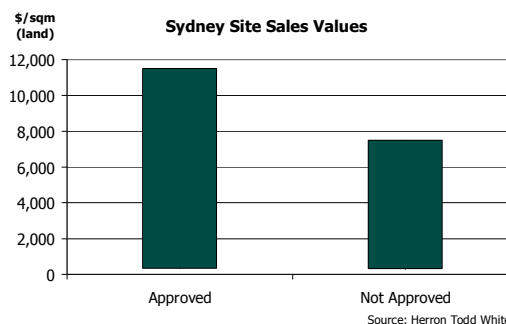


<b>Address:</b>	6 Lillian Road Riverwood
<b>Details:</b>	A three bedroom fibro house in fair condition.
<b>Sale Price:</b>	\$655,000
<b>Sale Date:</b>	12/05/2011
<b>Land Size:</b>	835
<b>Units:</b>	10
<b>Status:</b>	Not approved
<b>GBA:</b>	835 sqm
<b>FSR:</b>	1:1
<b>\$/sqm (land)</b>	784
<b>\$/unit:</b>	65,500
<b>\$/fsr:</b>	784

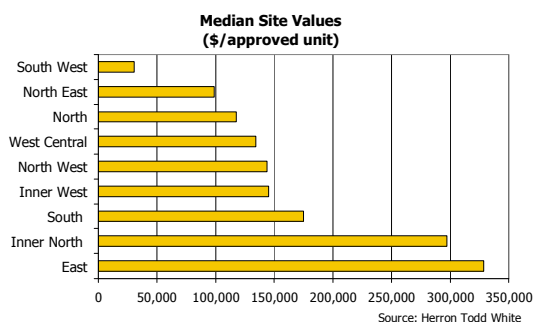
## Site Values

Reflecting the variance in the greater Sydney residential property market, site values vary significantly across Sydney. As shown in the chart below, values for sites featuring development vary

significantly depending on location and size of development



An analysis of development site sales that have occurred over the 18 months to July 2011, reveals that many purchasers are failing to appropriately price in the additional risk associated with a non-approved development site. These sites appear to be trading on comparable rates to sites which have secured development approval.



The variance in site values broadly reflects the conditions in the greater residential market, with those sites located in the eastern and Inner North sub-region attracting the highest values on a dollar per approved unit basis, while sites in the South West record the lowest site values.

## Market Outlook

Looking forward, the Sydney market will continue to record a mismatch between the level of underlying demand and the amount of supply added to the market. Despite the apparent undersupply, increased development costs (noting the recent falls in construction costs), are limiting the affordability of new apartments, and therefore market demand.

Over the coming 12 months, we expect that demand for new units will remain very market specific. In the inner ring suburbs demand will likely remain high, with both investors and owner occupiers seeking out apartments in close proximity to the CBD. In the outer suburbs however, new apartment sales will likely falter as buyers remain on the sideline. While the abolishment of the first home buyer stamp duty exemption for existing properties is intended to boost the demand for new apartments, it is likely that any up-tick in demand will be negligible, with the price of new apartments generally limiting their appeal to first home buyers.

After a period of increased demand during 2010, demand for sites has fallen in 2011. It is likely that demand will remain low in the remainder of 2011 and into 2012 as high lending costs and a cooling residential market limit the profitability of development projects. Site demand will however remain location specific, with sites in the inner ring suburbs being more favoured.

Given the relatively weak demand for development sites, it is unlikely that site values will record any significant growth over the coming 12 months. Values for sites without approval however, may fall as developers reassess the additional risk associated with non-approved sites.

### SALES ANALYSIS



<b>Address:</b>	167-173 Parramatta Road North Strathfield
<b>Details:</b>	Obsolete industrial building.
<b>Sale Price:</b>	\$3,000,000
<b>Sale Date:</b>	6/01/2010
<b>Land Size:</b>	1,545
<b>Units:</b>	30
<b>Status:</b>	Approved
<b>GBA:</b>	3,359 sqm
<b>FSR:</b>	2.2:1
<b>\$/sqm (land)</b>	1,941
<b>\$/unit:</b>	100,000
<b>\$/fsr:</b>	893



## Further Information

For a more in depth understanding of the current conditions within the residential development market and how they relate to your property, or for further information regarding any Herron Todd White service please contact either:

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