

Box C: The Housing Cycle

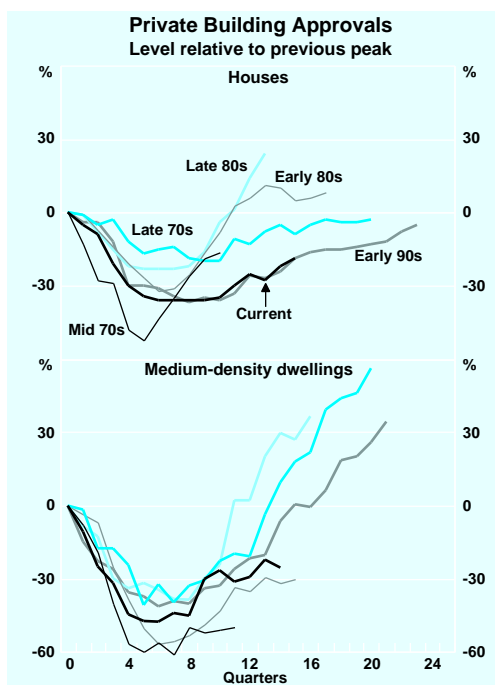
The current housing upswing has, on occasion, been characterised as relatively weak, because the increase in the number of dwellings constructed has been smaller than at a comparable stage of earlier cycles. This characterisation is misleading, however, because the current cycle has witnessed an unusually high level of activity in alterations and additions to existing dwellings and a rising average value of the dwellings being built. As a result, the amount of investment activity in the current cycle, as opposed to the *number* of dwellings being built, has been similar to that in earlier cycles. The current cycle also differs from earlier cycles in the type of dwellings being built and in geographical composition. A higher than usual proportion of medium-density dwellings (as opposed to free-standing houses) has been built and construction activity has been unusually concentrated in New South Wales and Victoria. In part, this geographical concentration of activity reflects shifting patterns of interstate migration.

The strength of dwelling investment relative to previous recoveries

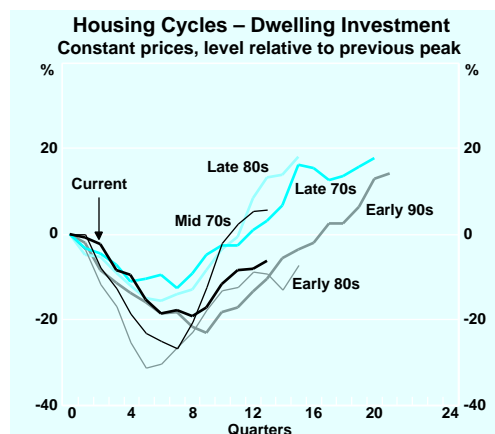
Graph C1 illustrates the current and past recoveries in the number of private building approvals, divided into two components: houses and medium-density dwellings. The relative weakness in the total number of building approvals compared to previous cycles reflects a slower-than-average pick-up in the houses component. By contrast, the number of approvals for medium-density dwellings has been quite similar to earlier cycles.

The smaller total number of building approvals has not translated into weaker dwelling investment (Graph C2). One reason for this is that alterations and additions activity has been relatively robust in the early stages of the cycle. Three years after the latest peak in dwelling activity, investment in the construction of new dwellings was still

Graph C1



Graph C2



7 per cent below its previous peak, while the amount of alterations and additions activity had regained its previous peak. The second reason is that the average value of the dwellings being constructed has risen over the past 4 years by more than 15 per cent

after allowing for changes in the price of building materials, reflecting an increase in the average size and quality of the dwellings being constructed.

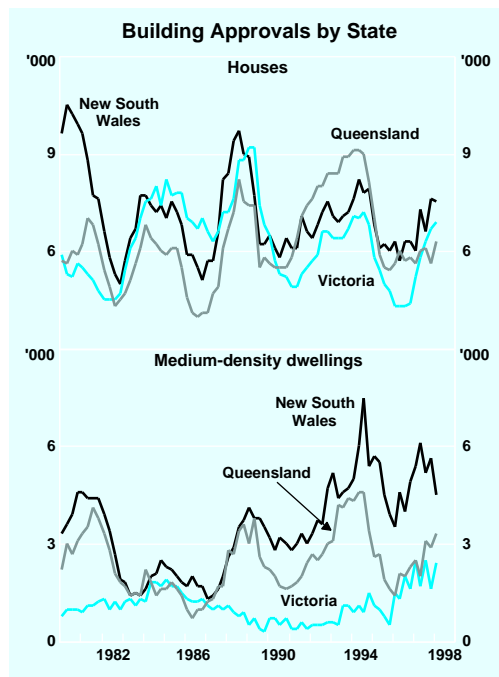
Regional developments

The current pick-up has been heavily concentrated in New South Wales and Victoria. Together, these States have accounted for almost all the growth in the number of dwellings in the current cycle, compared with less than half in the previous cycle. The number of dwellings being built in New South Wales in this cycle has not been unusually large. The cycle in Victoria does stand out, however, particularly for medium-density dwellings, which had been especially weak in the two previous housing upturns (Graph C3).

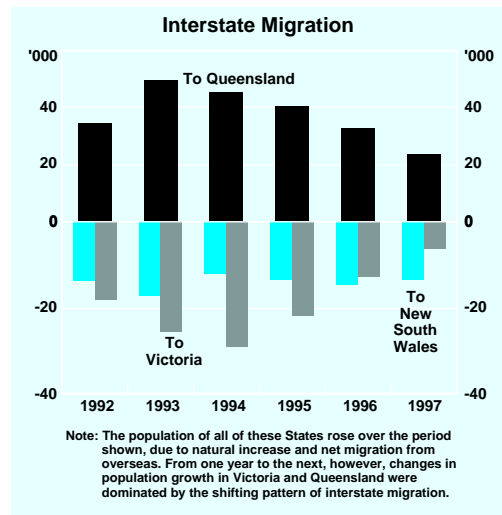
Building approvals in most of the other States have hardly grown at all thus far in the current housing cycle. In Queensland, there has been a modest upturn, but so far it is much weaker than in the early 1990s cycle.

The differing fortunes of Victoria and Queensland seem due in part to shifts in the

Graph C3



Graph C4



pattern of interstate migration. To a large extent, dwelling investment is driven by the rate of population growth, and large flows of migrants into Queensland in 1993 and 1994 resulted in particularly strong housing investment at that time (Graph C4). Since then, migration has fallen markedly, leading to a concomitant fall in demand for housing.

Many of the people who migrated to Queensland came from Victoria, a pattern which is consistent with weak economic activity in Victoria and robust growth in Queensland in the early 1990s. There is some evidence that these people came disproportionately from socio-demographic groups which traditionally favour medium-density dwellings, such as the elderly and less-wealthy households. This pattern of migration flows from Victoria helps to explain the weakness of medium-density activity in Victoria in the previous cycle as well as its more recent strength.

The concentration of activity in New South Wales and Victoria may also help to explain why the average real value of new dwellings has risen in the current housing cycle. Dwellings built in New South Wales and Victoria are more expensive on average than those built in Queensland and the rest of Australia. It is also true, however, that the

average real value of dwellings being built in each state is rising. This development reflects lower nominal interest rates (permitting

households to obtain larger loans) and rising levels of real income and wealth. ✕