



# State of the Market

## Residential Apartments

### Metro Sydney

#### H1 2020

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# State of the Market

## Residential Apartments

### Metropolitan Sydney – H1 2020



**The COVID-19 lockdown has stalled the nascent recovery that was beginning to emerge in the Sydney apartment market. The consequential economic and demographic effects are now likely to make the apartment market downturn more protracted.**

The new apartment market was already feeling the effects of a downturn in Off-the-Plan (OTP) purchaser demand. OTP sales peaked in 2016 and slowed through 2017 before declining more sharply from 2018 as investors began to retreat as regulatory pressure resulted in more stringent lending practices and higher interest rates being applied to investor loans.

Foreign investor demand was also curtailed by, among other things, a cap on foreign investment within individual projects and foreign buyer stamp duty surcharges as well as capital controls by the Chinese Government limiting outbound investment. Apartment supply has until now, remained high as projects have worked their way to completion.

#### COVID-19 Impacts

Green shoots in OTP demand began to emerge toward the end of 2019, however the impacts of the COVID-19 lockdown have caused significant ructions in the rental/investor market.

As the economy contracts, the sharp rise in unemployment will constrain the ability of many tenants to pay rent. A moratorium on evictions has thus far prevented a large exodus from rental apartments although landlords will likely face lower rental income as rents are re-negotiated to allow for tenants' revised circumstances.

The closure of international borders has caused a significant reduction in tenant demand as net overseas migration inflows effectively fell to zero. As a result, landlords are adding to the volume of supply by marketing their short stay apartments for long term rental. This will be compounded by the estimated 18,300 apartments forecast for completion in FY2021, above the annual average of the prior decade.

The impacts of COVID-19 saw Sydney's vacancy rate increase from 2.9% in March 2020 to 3.8% in June 2020 while the median unit rent fell by 5% during this time. While lower interest rates may help some landlords adjust, low overall rental yields indicate that many properties are still in a negative cashflow position. Apartment prices are also under pressure with the median unit price falling 1.8% in Q2 2020.

Investors are currently being supported by banks offering mortgage relief, but the number of properties on the market

is likely to increase as this support is withdrawn. Those that are struggling to meet their mortgage obligations are likely to face growing pressure from their financiers to sell, albeit with reluctance given diminishing levels of demand.

Thus far, the owner occupier market is holding up, supported by low interest rates, which have improved affordability for those with jobs. First home-buyer demand is being encouraged by stamp duty concessions. In turn, this is supporting demand for affordable apartments that are suitable for owner occupiers. Both upgraders and downsizers remain active where they are transacting within the same market.

#### Demand and Supply

Key to the outlook for the apartment market will be the level of net overseas migration inflows going forward. After averaging 234,900 per annum in the four years to FY2019, the Federal Government has estimated net inflows to be 154,000 in FY2020, and 31,000 in FY2021.

Based on New South Wales' recent share of the national total, its net inflow of overseas migrants is expected to fall from a peak of 105,500 in FY2017, to approximately 11,000 in FY2021. This translates to a near halving in demand from a peak of 51,000 new dwellings in FY2017, to an estimated 26,000 new dwellings in FY2021.

The combination of high vacancy rates, falls in rents and reductions in apartment prices will continue to weigh on investor sentiment (and to a lesser extent owner occupiers). OTP demand and the supply of new apartment projects is likely to be weak, at least in the short term.

Continuing weakness in OTP demand is expected to mitigate some of the risk associated with the impending potential oversupply in the Sydney apartment market. With only 5,300 apartments launched in new projects in FY2020, completions will decrease sharply from FY2022, helping to keep a lid on vacancy rates.

The decline in completions will however potentially expose the market to a shortfall of apartments in the medium term. The extent of the decline in aggregate supply and long lead time to restart the construction pipeline suggests that the market could quickly move into undersupply once current stock is soaked up. This will place upward pressure on rents, yields and prices, which in turn should kick-start OTP demand.

The timing of apartment absorption and recovery through the next cycle will very much depend on the pace of recovery in net overseas migration and if and when, it returns to pre-COVID levels.

# State of the Market

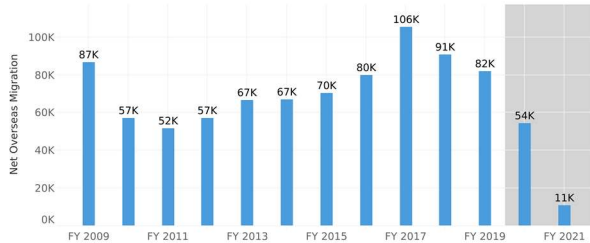
## Residential Apartments

### Metropolitan Sydney – H1 2020



#### POPULATION INDICATORS

##### Net Overseas Migration\*, NSW



##### Annual Population Growth\*, Sydney



\* FY20 & FY21 estimate based on Fed Gov't assumptions for net overseas migration  
Source: Australian Bureau of Statistics, Charter Keck Cramer

#### DEMAND INDICATORS

##### Median Unit Price Q2 20



**\$715,000**

(down -1.8% on Q1 20  
up 2.9% on Q2 19)

Source: PricewaterhouseCoopers

##### Median Rent (Q2 20)

**\$473 p.w.**

(down -5% on Q1 20  
down -6% on Q2 19)

##### Vacancy Rate (Q2 20)

**3.8%**

(up from 2.9% in Q1 20)

Source: SQM Research

#### SUPPLY INDICATORS

##### Apartment Completions



**177,500**

apartments have been completed in Metro Sydney since 2009.

| Project Sizes | Project Sizes |                |
|---------------|---------------|----------------|
|               | Projects      | Apts           |
| 1-50          | 2,189         | 58,000         |
| 51-100        | 683           | 48,400         |
| 101-150       | 199           | 24,300         |
| 151-200       | 96            | 16,500         |
| 201-250       | 58            | 13,000         |
| 251-300       | 20            | 5,600          |
| 300+          | 32            | 11,700         |
| <b>TOTAL</b>  | <b>3,277</b>  | <b>177,500</b> |

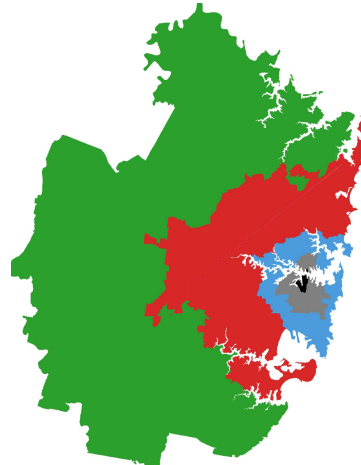
Source: Charter Keck Cramer

#### MARKET UPDATE

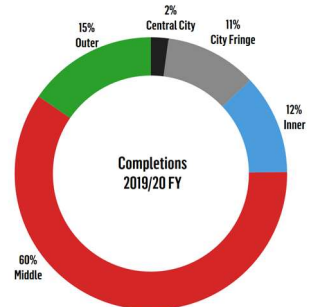
Demand for apartments in Metropolitan Sydney has historically been underpinned by a combination of high house prices and strong population growth driven by high Net Overseas Migration. However, occupier demand is weakening markedly as the international border closure caused by the COVID-19 lockdown causes net overseas migration inflows to collapse.

Supply remains high with 22,500 apartments completed in Metropolitan Sydney in FY2020, the fourth highest on record. Some 60% of completions were located within the *Middle Region*. Although the pipeline of projects under construction suggests that completions in 2020/21 will remain relatively high, supply will fall away quickly with new apartment project launches having declined markedly to only 5,300 apartments in 2019/20.

#### METROPOLITAN SYDNEY APARTMENT REGIONS



Source: Charter Keck Cramer



#### METROPOLITAN SYDNEY APARTMENT SUPPLY SNAPSHOT – FY2020

**22,500**

Apts. Completed  
2019/20 FY

**9,100**

Apts. Commenced Construction  
2019/20 FY

**5,300**

Apts. Launched  
2019/20 FY

**4,400**

Apts. Approved  
2019/20 FY

Source: Charter Keck Cramer

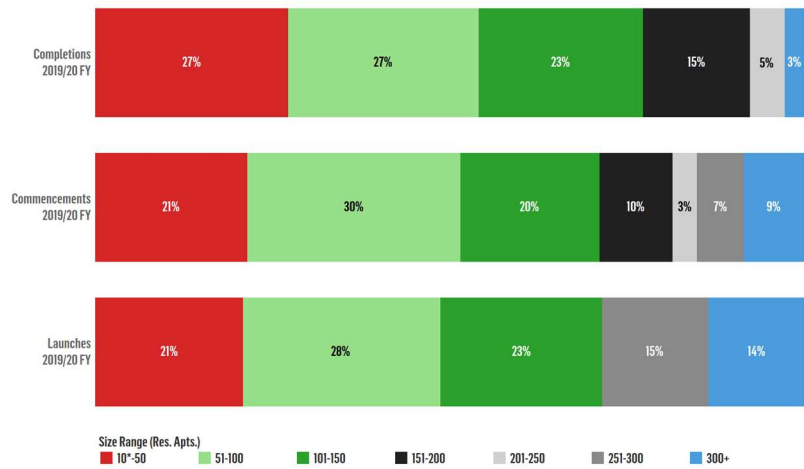
## COMPOSITION OF SUPPLY

**Project launches in FY2020 show a greater proportion of apartments in larger projects.** Notably, projects of 250+ apartments accounted for only 8% of completions in FY2020, 16% of apartments commenced, and a significant 29% of apartments that have launched.

The proportion of apartments in buildings of 300+ apartments has increased from 3% of completions to 14% of total apartments launched in FY2020.

This is in part due to the significant reduction in total projects being launched and larger projects making up a greater share.

## COMPOSITION OF SUPPLY – FY2020



Source: Charter Keck Cramer

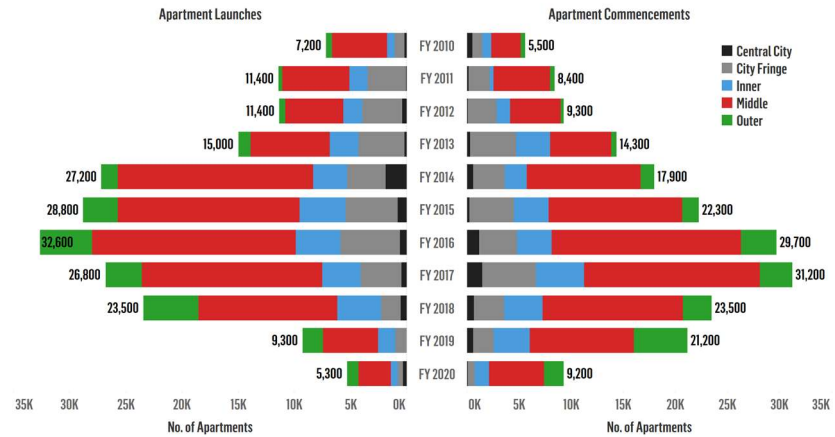
## APARTMENT COMMENCEMENTS

**In FY2020, construction commenced on 9,200 apartments.** This is a 57% decrease from the 21,200 commencements recorded in FY2019 and is the lowest number of commencements since FY2011.

## APARTMENT RELEASES

**In FY2020, there were a total of 5,300 apartments in projects that commenced marketing ('launched').** This represents a dramatic fall from the 23,500 apartments launched in FY2018. Since the peak in FY2016, the volume of apartments launched in new releases has fallen by 84%.

## LAUNCHES AND COMMENCEMENTS OVER TIME



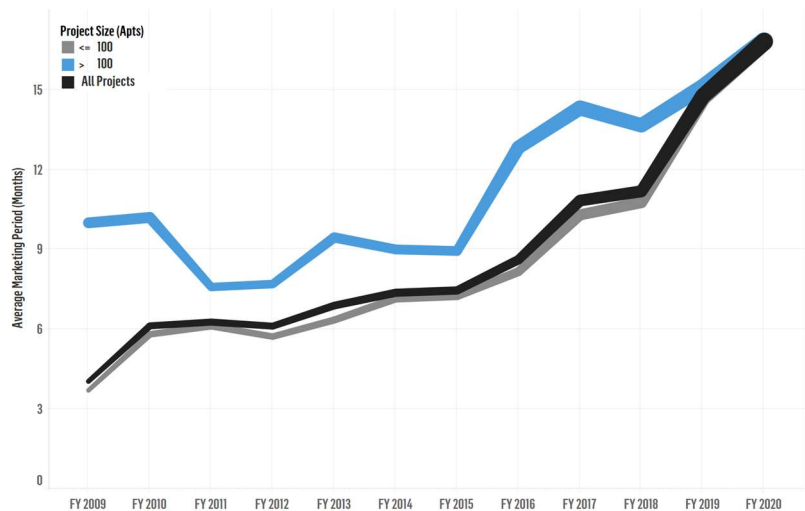
Source: Charter Keck Cramer

## APARTMENT PIPELINE

**The time required to deliver new apartment projects has pushed out since OTP sales rates began slowing in 2016, with projects taking longer to proceed to construction commencement.** Over 2011 to 2016, there was an average eight month lag from project launch to commencement, taking a little longer in larger (100+ apartments) projects

Slowing sales volumes and more onerous requirements to secure finance have extended the period between launch and construction start, which blew out to an average 18 months for apartment projects commenced in FY2020. Notably, the time taken to commence construction in projects of 100+ apartments has stabilised since 2017.

## AVERAGE PERIOD FROM LAUNCH TO CONSTRUCTION COMMENCEMENT



Source: Charter Keck Cramer



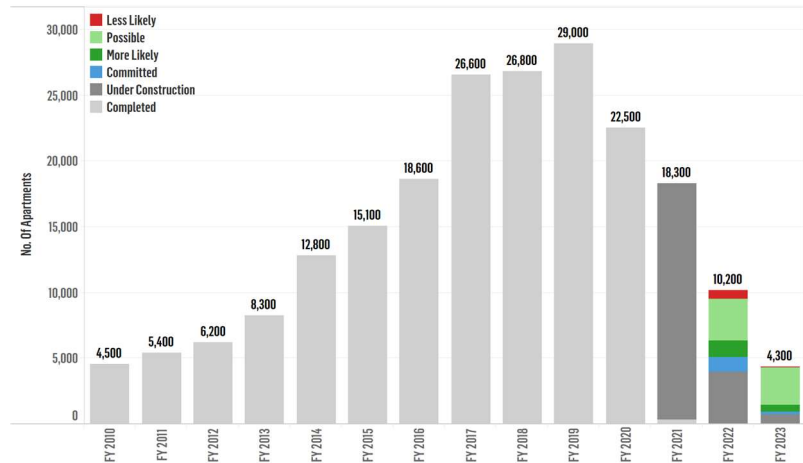
## APARTMENT COMPLETIONS

**In FY2020, 22,500 apartments were completed in Metropolitan Sydney.** This represents a 22% decrease from the record 29,000 apartments completed in FY2019.

Apartment completions across Metropolitan Sydney were at their lowest level since 18,600 completions were recorded in FY2016.

Apartment completions across Metropolitan Sydney are on track to fall to 18,300 completions in FY2021. Although completion dates may be delayed as construction is slowed due to COVID restrictions. The pipeline is nevertheless diminishing quickly with completion levels to fall dramatically from FY2022.

## COMPLETIONS OVER TIME



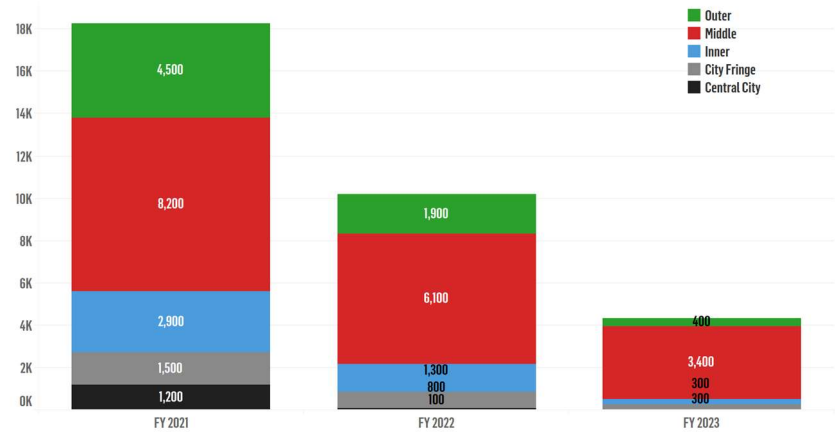
Source: Charter Keck Cramer

## FUTURE COMPLETIONS BY REGION

**Over FY2021 there are projected to be 18,300 apartment completions in metropolitan Sydney.** Supply will be concentrated in the *Middle Region*, which will account for 45% of the total, followed by the *Outer Region* (25% of the total). Only 7% of total completions will occur in the *Central City Region*.

The number of completions in FY2022 and FY2023 are expected to decrease significantly across all regions. Apartment completions across these years will continue to be located mainly within the *Middle Region*. The *Outer Region* is expected to experience the biggest decrease in share on FY2021 volumes.

## FUTURE COMPLETIONS – REGIONS OF METROPOLITAN SYDNEY



Source: Charter Keck Cramer

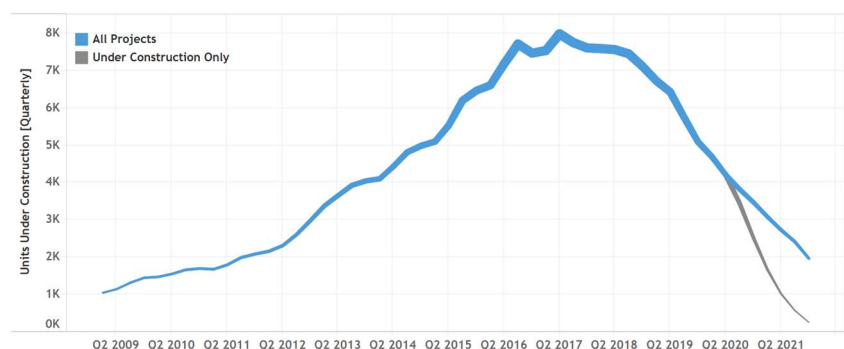
## CONSTRUCTION INDEX

**Residential construction activity in Sydney peaked at the equivalent of around 8,000 apartments per quarter in Q2 2017 but is now continuing the long period of decline.** This reflects the fall in sales and new projects being launched after the 2015 peak.

Assuming all currently marketed projects proceed, residential construction activity in Sydney will steadily fall to the equivalent of around 2,000 apartments per quarter by the end of 2021.

Notwithstanding the launch of any new projects, construction levels are likely to fall below this level beyond 2022.

## RESIDENTIAL CONSTRUCTION ACTIVITY INDEX



Source: Charter Keck Cramer

The Residential Construction Activity Index is an indication of the construction work done per quarter, represented as the number of apartments to more accurately reflect the flow of construction activity and related employment/economic activity across higher density residential related real estate.

Detailed and comprehensive data forms the basis to a reliable understanding of the residential market. Charter Keck Cramer's Research & Strategy group maintains a proprietary national apartment supply database across Australia's major capital cities and selected regions that has been continuously updated since the early 2000s.

The database comprises:

- Tracking of over 5,500 currently live apartment projects and over 24,000 complete apartment projects
- Tracking of associated residential apartment uses, including student accommodation, serviced apartments and retirement apartments, and
- Expansion of the database in recent years to include major townhouse developments.

Charter Keck Cramer's proprietary national database is an invaluable tool for stakeholders in the residential development industry, with major benefits including:

- Simple and Clear outputs
- Buildings and Multi-Stage Projects
- Indicators of Actual & Real Activity
- Reliable & Dynamic Forecasts
- Spatially Referenced
- Optimised for Complex Analytics

Key metrics monitored within the national apartment database are as follows:

| Item                        | Comment  |
|-----------------------------|--|
| Geographic Coverage         | All capital cities (full metro: Sydney, Melb and Bris + Core regions: Perth, Adelaide, Canb) |
| <b>Data Coverage</b>        |  |
| Location / address          | Street number, Street Name, Suburb, LGA, Region, City  |
| Building scale              | Number of apartments & Number of levels;   |
| Development Status          | Completed (2017, 2018), Under Construction, Marketed, Approved & Application                 |
| Project Delivery Team       | Developer and Builder entities   |
| Forecast Completion         | Recently Completed, Under Construction and Marketed projects (to nearest quarter)            |
| Milestone dates             | Acquisition, Planning, Marketing, Construction, Completion (to nearest quarter)              |
| <b>Outputs</b>              | Spreadsheet (.xls or .csv file format) + Basic standard charts & tables (suburb)             |
| <b>Frequency of updates</b> | Monthly (with quarterly audits)  |

For more information about Charter Keck Cramer's proprietary apartment database and how it can help you, contact:



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Sources: Charter Keck Cramer, Australian Bureau of Statistics, SQM Research, Domain.com.au, New South Wales Planning Department

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