Urban Development Institute of Australia
NEW SOUTH WALES

Apartment Supply Pipeline Report

"Apartments continue to be the major missing piece for NSW Housing and a reboot of apartment supply is a major key for housing affordability in the years ahead"
– Steve Mann, UDIA NSW CEO

November 2022

Executive Summary

NSW is facing a severe housing shortage and affordability crisis. Historically, two-thirds of the supply of new homes in NSW has been apartments. Therefore, a healthy apartment sector is critical to tackling the housing shortage. Unfortunately, the vital signs for the apartment sector are all flashing red.

Apartment rentals are particularly critical to the well-being of people on low incomes in NSW. However, vacancy rates across the state are below 1% for most of Regional NSW, and at an 11-year low of 1.3% in Greater Sydney. Rental prices are at record highs, with parts of the state experiencing 15% annual growth in median weekly rent, even as house prices drop. None of this is surprising as UDIA estimates that we currently have a backlog of supply for over 48,000 apartments across the state.

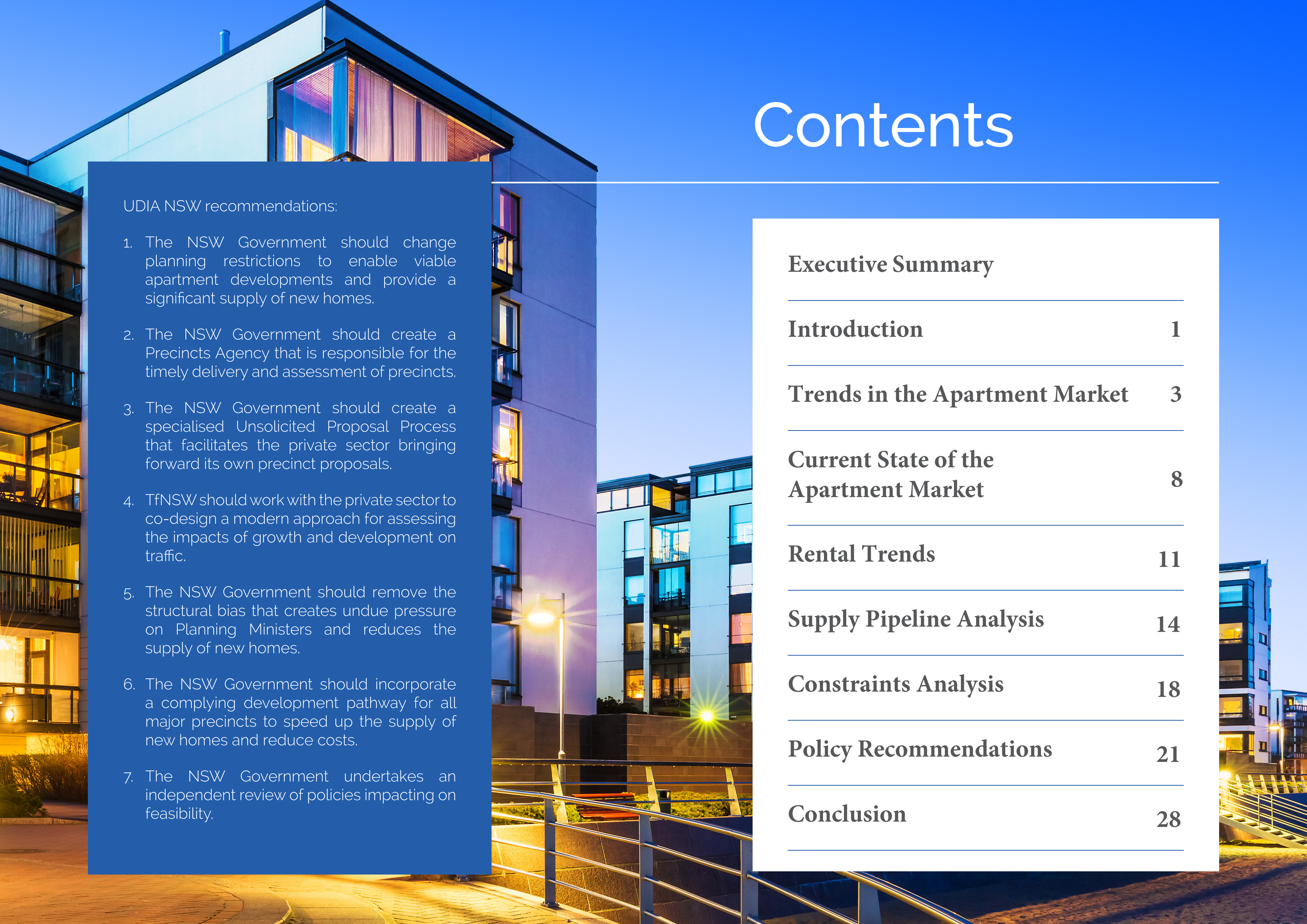
Alas, the outlook for the near future is worse, with NSW facing record lows in large apartment approvals and commencements at a time when we expect the population to begin significantly growing again. UDIA estimates that the apartment backlog will reach close to 60,000 in the next couple of years to place even further pressure on vacancy rates and rents. This is expected to increase prices, and when combined with a reduction in credit availability, make it even harder for first-time buyers to get onto the housing ladder.

This year's Apartment Supply Pipeline Survey of developers reveals that the top issues holding back supply are:

1. Barriers relating to finance including restrictions from the banks, presales and feasibility concerns.
2. The NSW Planning System and VPA negotiations.
3. Engaging with infrastructure providers such as Transport for NSW (TfNSW).

Some people will be tempted to believe that the current lack of apartment supply is an inevitable cause of the downturn in the market, and that increased prices will eventually lead to an increase in supply, meaning there is no need for the NSW Government to do anything. The problem is that UDIA estimates that we will not make any progress in reducing the backlog once the market recovers. This will embed the record high levels of rent permanently into the system, making many people in NSW permanently worse off. The evidence confirms that the lack of supply is not a market failure, but failure of policies restricting development opportunities, the most inefficient planning system in Australia and the highest taxes and charges in Australia (according to NHFIC). These issues combined reduce the feasibility and supply of new apartments, turning developers to other states and hitting NSW's economic growth potential.

NSW can and must do a lot better to tackle the housing shortage and affordability crisis. Minister Stokes' foreword to the Apartment Design Guide states "Apartments provide housing choice for those with a range of incomes and lifestyle preferences. We need more and different types of homes as our State's needs change over time." The recommendations in this paper go a long way towards accommodating these needs by fixing the apartment sector and enabling developers to produce a consistently high level of quality new homes in great places, reducing the backlog and improving affordability.



Contents

UDIA NSW recommendations:

1. The NSW Government should change planning restrictions to enable viable apartment developments and provide a significant supply of new homes.
2. The NSW Government should create a Precincts Agency that is responsible for the timely delivery and assessment of precincts.
3. The NSW Government should create a specialised Unsolicited Proposal Process that facilitates the private sector bringing forward its own precinct proposals.
4. TfNSW should work with the private sector to co-design a modern approach for assessing the impacts of growth and development on traffic.
5. The NSW Government should remove the structural bias that creates undue pressure on Planning Ministers and reduces the supply of new homes.
6. The NSW Government should incorporate a complying development pathway for all major precincts to speed up the supply of new homes and reduce costs.
7. The NSW Government undertakes an independent review of policies impacting on feasibility.

Methodology Notes

UDIA's research of the projected supply pipeline analysis is taken from Cordell Connect's database. Our analysis filtered projects on the database into one of three categories (Under Construction, Approved but not Commenced, and Pre-Approval). For the purposes of this report, an apartment is defined as a 4 or more-storey building with at least 10 units. Our research covers over 130,800 potential units across the Sydney Megaregion from close to 1,200 individual projects.

During October, UDIA went out with a survey of apartment developers to understand the constraints that their current and prospective apartment projects were facing. Our survey results cover 125 projects across the state, and cover over 58,000 potential units in the pipeline (a 32% increase in response rate from 2021).

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Section 1

Introduction

As the affordability crisis and critical housing shortage proliferates, apartments are an increasingly viable living option across a range of demographics. The 2021 Census revealed that 21.7% of people in NSW live in apartments or flats, up from 19.9% in 2016. The preference towards apartment living is reflected in the construction industry, with new apartments consistently making up the greatest proportion of new builds in Greater Sydney, until recently.

Drawing on the 2021 NSW Intergenerational Report, 42,000 new homes are required annually across NSW to achieve 1.7 million new homes by 2061. With the Intergenerational Report also anticipating 90% of population growth to be in the Sydney Megaregion, development of diverse types must match, and must enable locations of high desirability and job opportunity. Aligned with historical trends, we anticipate around 20,500 apartments to be required annually across the Sydney Megaregion, with 14,000 covered by development in greenfield, and the rest with other "missing middle" housing types.

Section 2

Trends in the Apartment Market

New apartment completions in NSW are currently performing well below both the 5-year average (23,200) and 10-year average (18,600), with only 12,600 apartment completions in FY22 (see Figure 1).

Apartment completions hit their peak in 2018-19 (at 31,700) but have fallen since then. As of June 2022, NSW is now at its lowest rolling annual apartment completions since June 2014.

Record high apartment approvals throughout 2016 paved the way for record high apartment completions. However, the downwards trend in apartment approvals that commenced in 2020 has been sustained through to 2022, despite a short recovery in 2021 (see Figure 2).

Apartment approvals for NSW are now officially at record lows. In the year to July 2022, approvals were below 12,000, their lowest in a decade. Despite positive signs in the latter half of 2021, where apartment approvals hit a mini peak of close to 20,000, the decline experienced between 2018 and 2021 has been sustained. **Despite a minor uptick in the most recent August/September figures, apartment approvals are 66% below their 2016 peak.**

Given that high-rise approvals historically take around two years to be realised as supply, these historic lows likely imply a large hole in new apartment supply by around 2025-26.

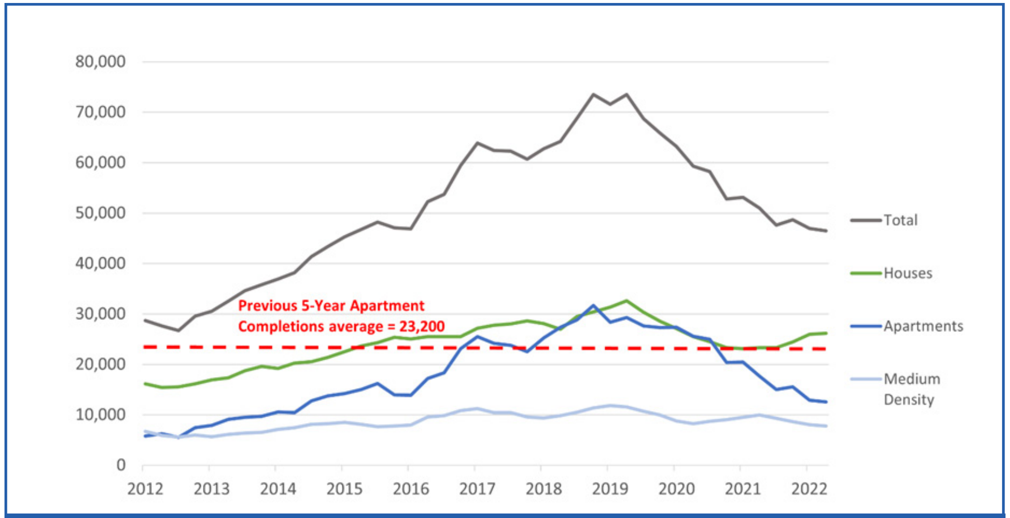


Figure 1: New Dwelling Completions, by Typology, NSW, Rolling Annual to June 2022 *Source: ABS, UDIA NSW*

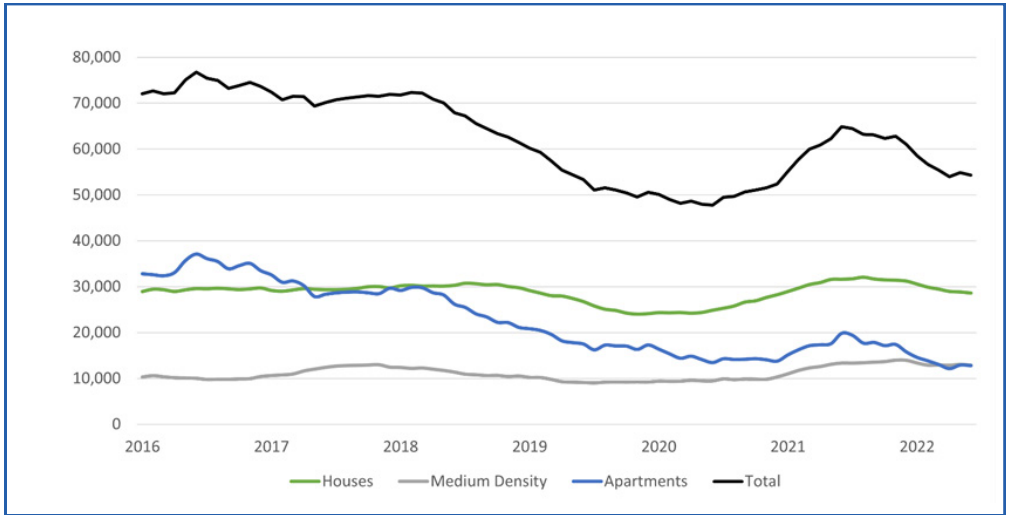


Figure 2: New Dwelling Approvals, by Typology, NSW, Rolling Annual to Sept 2022 *Source: ABS, UDIA NSW*

Low approval levels are contributing to the current decline in commencements (see Figure 3) with rolling annual commencements down by 23% between March and June quarters to 13,700, now sitting 36% below the 5-year average (21,400).

There is a raft of projects also sitting in the 'approved not commenced' category. According to ABS, at the close of the June 2022 quarter, there were over 13,000 residential dwellings that were 'approved not commenced' in NSW. 68% of these (nearly 8,900) are multi-unit dwellings, a 7% increase compared to June 2021. Not only are we seeing a bottleneck in future supply because of low approvals, but a proportion of those that are approved are also struggling to commence development.

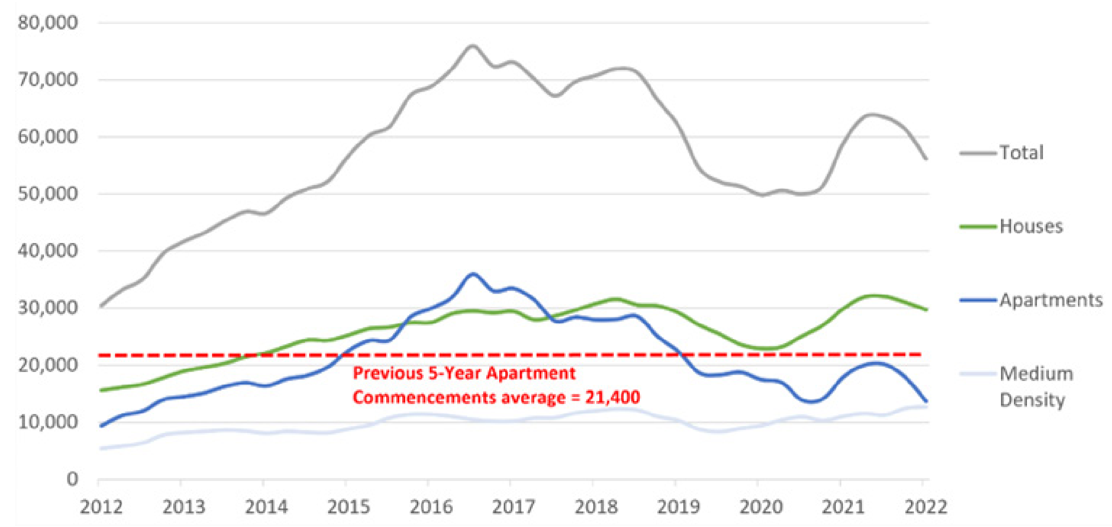


Figure 3: New Dwelling Commencements, by Typology, NSW, Rolling Annual to June 2022 *Source: ABS, UDIA NSW*

> Decade-low approvals will likely imply a large hole in future apartment supply

1.2 | Apartment Demand Factors

Overall Population Growth

Overseas Migration

The 2021 NSW Intergenerational Report expects natural growth in NSW to slow. Migration will increasingly be expected to drive overall growth in the population.

Overseas arrivals to NSW only returned to March 2020 levels in July 2022 (see Figure 4).

Historically, overseas immigration to NSW has been at a greater rate than other states. Pre-COVID trends (between 1991 and 2019) saw 39% of all overseas arrivals to Australia come to NSW.

The recent Jobs and Skills Summit increased the permanent visa cap to 195,000 a year across Australia. A portion of this will include individuals already living in Australia. However, with longer stays of skilled migrants and students expected, demand from overseas migration will increase.

On temporary migration, NSW receives the greatest share of student arrivals in the country, with 37% on average. Over the first 8 months of 2022, NSW received just over 100,000 temporary student visas, compared to the 230,000 arrivals seen in the first 8 months of both 2018 and 2019. The uplift from the Jobs and Skills Summit will more than double expected demand.

Population Trends and Forecasts

An additional 1.5 million people are expected to live across the Sydney Six Cities Megaregion by 2041. By then, these Six Cities are

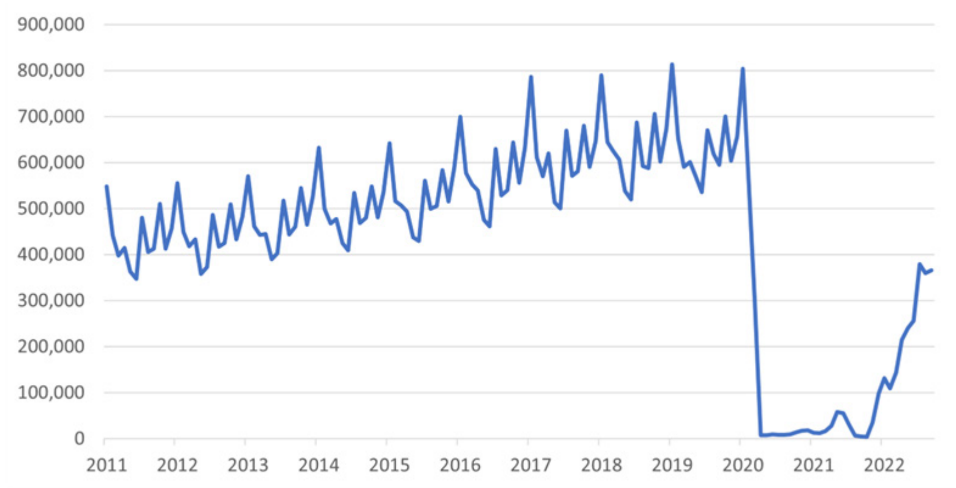


Figure 4: Oversease Arrivals to NSW, to September 2022 *Source: ABS, UDIA NSW*

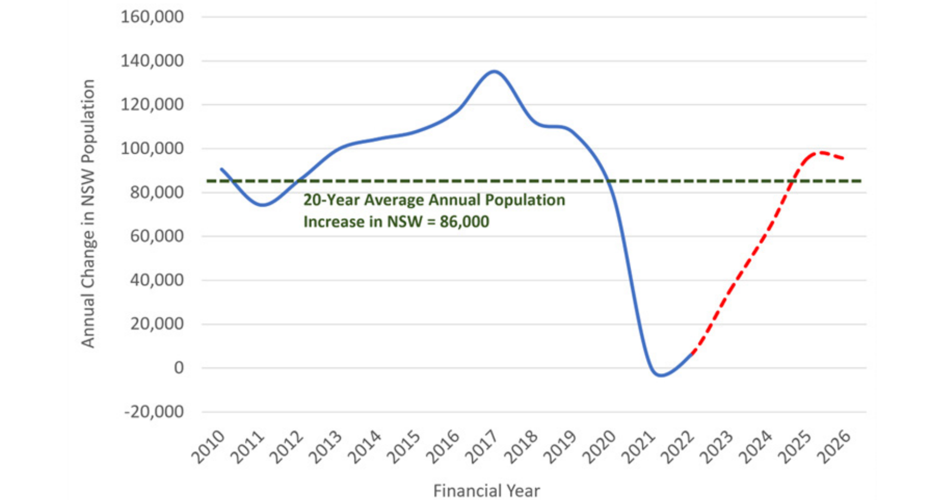


Figure 5: NSW Historical Population Growth and Projections (in Red) *Source: DPE, UDIA NSW*

expected to comprise 80% of the entire NSW population (up slightly from 78% currently).

The Department of Planning and Environment's (DPE) forecast for population growth in NSW expects a return to pre-COVID levels (see Figure 5) around 2024/25. The population is then expected to grow quicker than the previous 20-year average. New apartment commencements are needed now to be ready for this future demand.

Impacts on Affordability

The cost of living in Sydney is now 32% more expensive than Brisbane, where many in NSW are migrating to. In December 2021, NSW saw an all-time low net interstate migration of -14,500. Relative house prices are cited as the main reason for interstate migration across every age group (Australian Centre for Population).

Apartments have become an increasingly attractive living option across a range of generations in NSW. According to Real Estate Australia, the price cap for first home buyers to access the Home Guarantee Scheme of $900,000 currently provides access to just 19% of suburbs for houses, but 52% of suburbs for apartments. Despite this, the value of a new unit in NSW is still 10.9 times greater than the average yearly income (as of May 2022), up from 10.2 just 24 months ago (a 7% increase).

Successive cash rate hikes have exacerbated this shift to the more affordable markets. Home prices have slowed in their growth because of these cash rate hikes (Figure 6). The recent November cash rate hike to 2.85% brings the cash rate to its highest point since April 2013, with the cash rate forecast to increase further.

Apartment prices have been far more moderate when compared to detached houses in NSW. Over the 2021-22 financial year, the median sales price for new detached houses increased 48%, compared to just 7% for new units.

Moody's Investor Services reported in June that the cash rate rising to 2.85% would require residential prices to decline 22% to offset the impact on debt serviceability. With the cash rate now at 2.85%, median house values have dropped just -8%, and median unit values by -4.5%, compared to when the cash rate was last at 0.1%. This is insufficient to alleviate serious affordability pressures state-wide. We expect that these combined factors will push people towards the more affordable apartment living options.

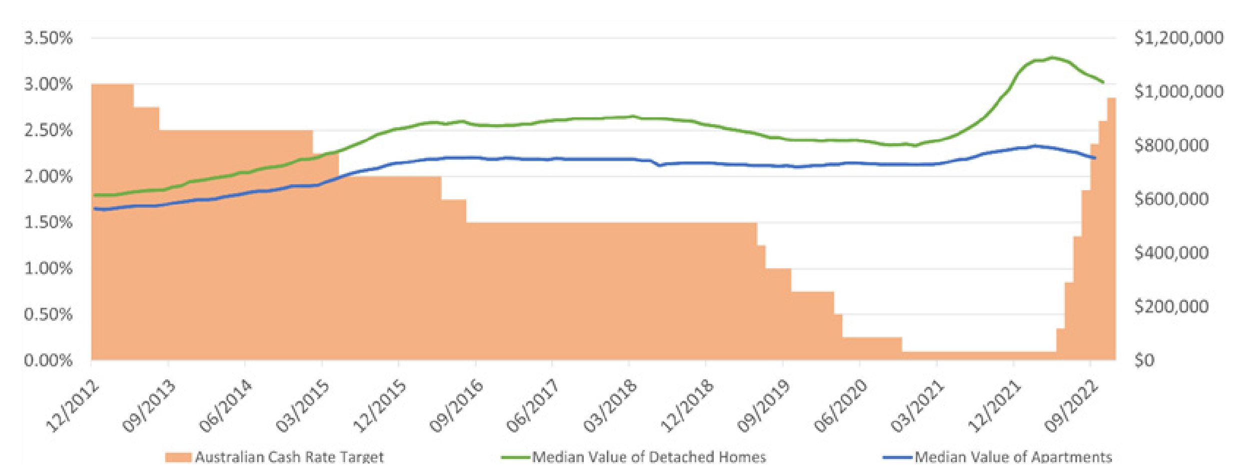


Figure 6: Median Sales Price of Detached Homes and Apartments VS. RBA Cash Rate, Greater Sydney, to September 2022
Source: CoreLogic; RBA; UDIA NSW

Section 3

Current State of the Apartment Market

CoreLogic's Australian Unit Market Update for September revealed that Greater Sydney unit values have fallen -5% in the last year. Comparatively, in Regional NSW where unit values declined -2% over the September quarter, they remain 7% higher on the year.

Despite the decline annually, the value of a new unit in Sydney is still well in excess of any other capital city (Figure 7).

Supply has also not been coming to market at peak rates across the Sydney Megaregion. New unit sales hit their lowest value in the 12 months to July, at less than 7,750, having dropped each month for 12 consecutive months. This reflects a 51% decline annually and is now 76% below the September 2015 peak (Figure 8). More recent CoreLogic data revealed that new unit listings nationally continued falling between August and October.

The RLB Crane Index provides another indicator for apartment construction activity. Sydney has always had the most active cranes in the country, and had a strong recovery in residential crane numbers in the 3rd quarter of 2022. (Figure 9).

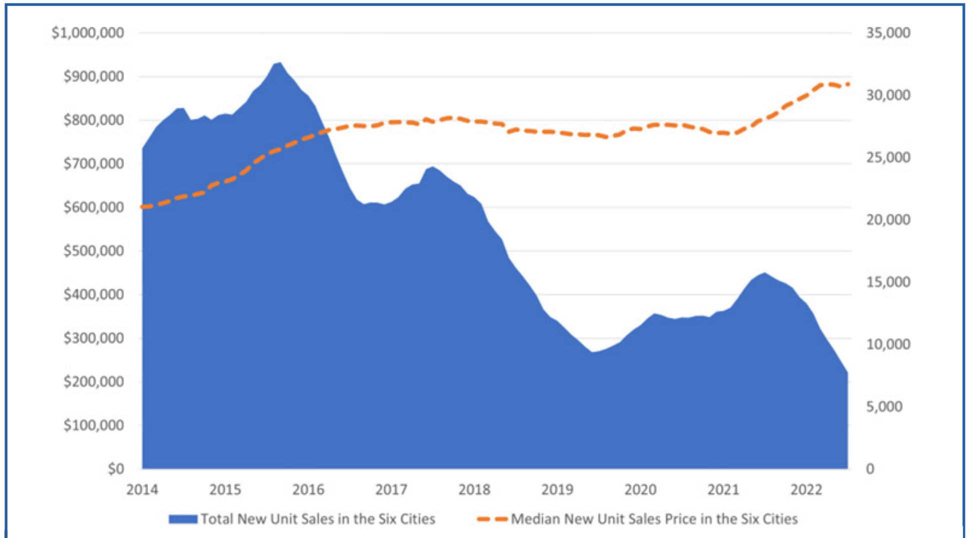


Figure 8: Rolling Annual Number of Sales Price of New Units, Combined Six Cities Megaregion, to July 2022
Source: CoreLogic, UDIA NSW

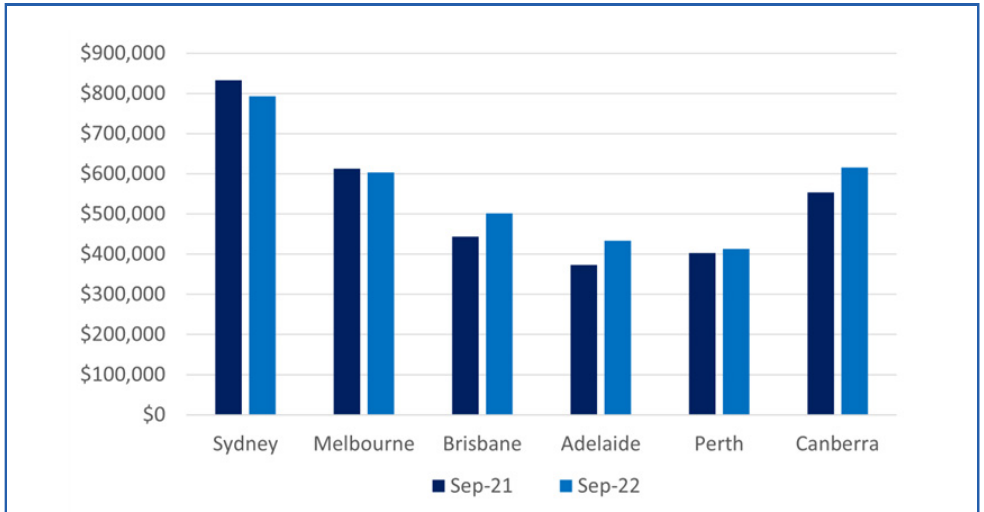


Figure 7: Medium Value of Units, Select Australian Capital Cities *Source: CoreLogic, UDIA NSW*

Figure 9: Number of Active Residential Cranes, Sydney and Melbourne *Source: RLB, UDIA NSW*

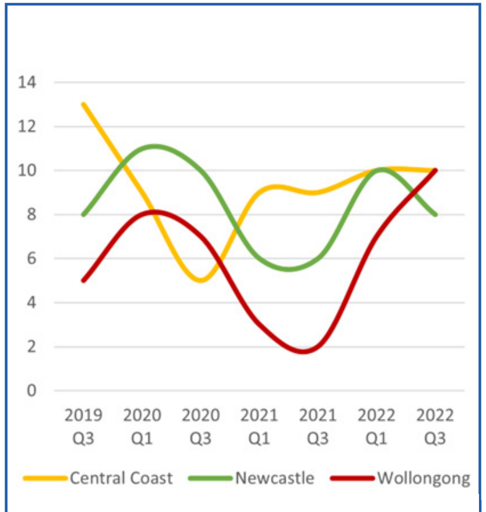


Figure 10: Number of Active Residential Cranes, Regional Cities in NSW *Source: RLB, UDIA NSW*

However, this was not matched by the churn rate, i.e., the proportion of cranes finishing their work over the quarter. The 'churn rate' was lower in Sydney than for every other capital city, at 24%. The protracted period for apartment project completions is unsurprising, given that 2022 produced a record-breaking run of inclement weather events, and labour and material constraints continue to slow down progress. However, Canberra, despite also seeing a 14% increase in rain days compared to its average, had an impressively high churn rate, at 70%.

The churn rates in Newcastle (25%), Central Coast (20%), and Wollongong (20%) are equally poor. Although comprising smaller real numbers than Sydney (see Figure 10), these low proportion of cranes completing their work is indicative of constraints being felt state-wide.

In the 12 months to September, Sydney's CPI rose 7%, the largest annual increase in 32 years (see Figure 11). This has been reflected in the construction industry. CoreLogic has found that, over the September quarter, construction costs rose 4%, the largest quarterly increase in NSW of the 21st century. Annually, costs have risen by over 10%, with only Victoria recording a larger increase. This unprecedented challenge is impinging on the ability for recently approved projects to reach completion, having a sizeable impact on project feasibility.

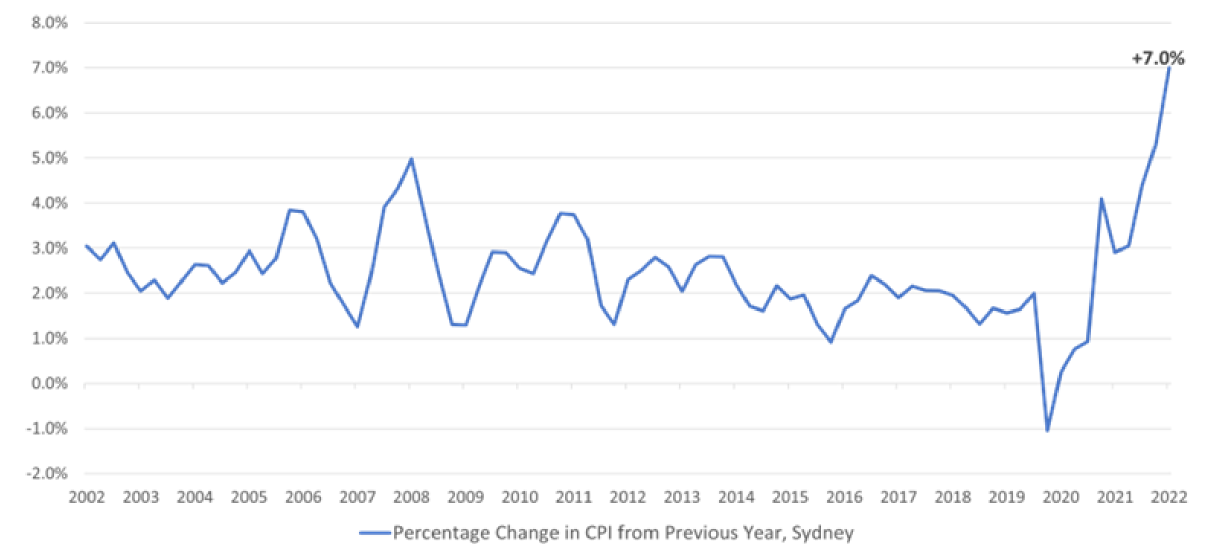


Figure 11: Annual Change in CPI, Sydney, to September 2022 *Source: ABS, UDIA NSW*

> Over the September quarter, construction costs rose 4%, the largest quarterly increase in NSW of the 21st century

Section 4

Rental Trends

The rental market provides important insights into the apartment market. According to the 2021 Census, renting is now the most popular tenure type in NSW.

Low rental availabilities and high rents are a leading indicator on rates of homelessness, as low-income earners and those on societies' fringes are more likely to be renters.

Weekly Rent

Census data revealed that 35.5% of renters in NSW are paying more than 30% of their household income towards their weekly rent, which is over 3 percentage points higher than the national proportion.

Despite house prices easing, there is no alleviation in the rental market especially with the return of overseas migration. As of October 2022, every City of the Sydney Megaregion is currently experiencing record high median weekly rents (Figure 12). September was a month which saw the fourth consecutive cash rate rise and saw Sydney dwelling prices drop 5.9% in just a month. Yet weekly rents continued to rise and hit these new peaks.

Vacancy Rates

The resilience of rental prices is mostly explained by the severe shortage in available rental stock.

	Eastern Harbour City	Central River City	Western Parkland City	Central Coast City	Lower Hunter & Greater Newcastle City	Illawarra-Shoalhaven City
Weekly Rent at Oct '22	$750	$518	$417	$506	$509	$520
Annual	↑ 15.2%	↑ 15.1%	↑ 9.6%	↑ 7.5%	↑ 8.5%	↑ 10.2%

Figure 12: Median Weekly Unit Rents Across the Six Cities, October 2022. *Source: CoreLogic; UDIA NSW*

The number of vacancies in Sydney, as of October 2022, are at their lowest since March 2016. This is not only because demand for rental properties remains high across the megaregion, but because incumbent renters are less able to purchase and free up rental accommodation.

Each region is reporting vacancy rates well below their long-run average. Figure 13 outlines the megaregion-wide inability to achieve anywhere near the healthy vacancy rate of 3% (according to REIA).

In Sydney, the current vacancy rate of 1.3% is the lowest since March 2011. In the regions, not one has seen the vacancy rate at 3% since 2014. However, with increased migration to the regions, these record lows will become more damaging to the economic growth and prosperity of regional communities, as key workers will be unable to find somewhere to live close to where they work.

Importantly, these record lows are being experienced before immigration to NSW returns in full.

UDIA conducted a comparison between Sydney and Melbourne's rental markets, looking at the relationship between weekly rents and vacancy rates. In theory, when weekly rents are high and increasing, we would expect the vacancy rate to go up, as less people can afford to rent. For example, as of October 2022, Melbourne's median weekly unit rents are at $475, and have increased 13% annually. As a result, they also have a tight rental market at 1.5%, their lowest in four and a half years. However, Sydney, which is currently at a decade-low vacancy rate almost identical to Melbourne's (1.3%) and has also seen weekly rents rise 14% over the last year, experiences rental prices that are **27% higher than Melbourne's**. There is a clear attraction to Sydney that has led people to continue renting despite an extremely unaffordable market. This desirability has not, and will not, wane, which shows that people have become willing to accept rental price growth, on top of already high rents, to live in this famous global city.

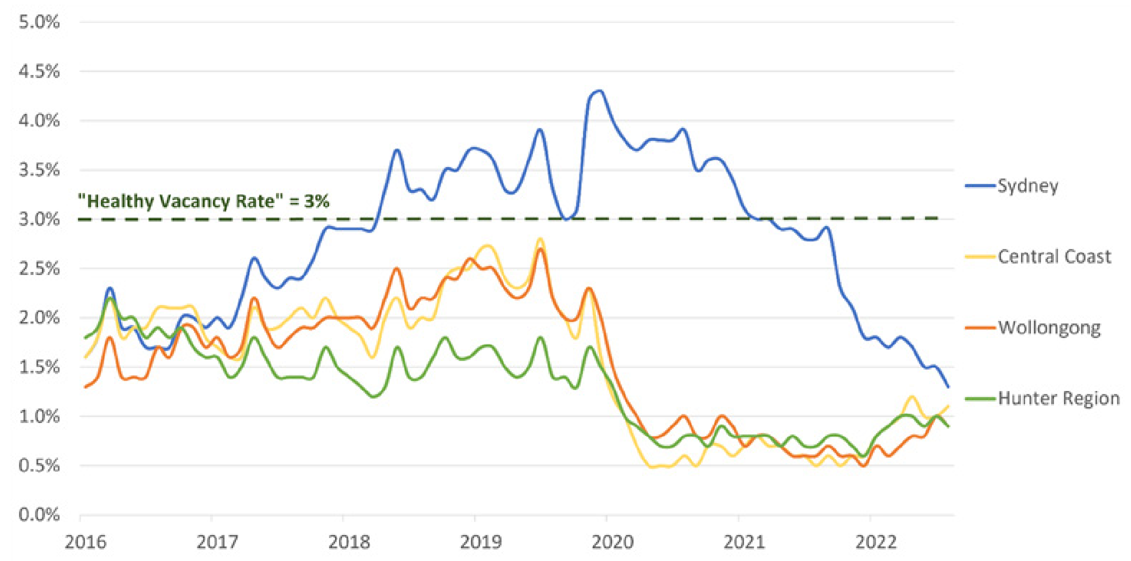


Figure 13: Vacancy Rates Across the Sydney Megaregion, to October 2022 *Source: SQM Research, UDIA NSW*

> Record low vacancies and record high rents are being experienced before immigration returns in full

Section 5

Supply Pipeline Analysis

UDIA's forecasts for future apartment supply in the Sydney Six Cities Megaregion are placed against estimated annual demand of 20,500 units (Figure 14). This is derived from the NSW Intergenerational Report, applying the historical average of 67% of total completions to multi-unit dwellings. We expect 20,500 of these to be high-rise apartments, and another 6,000 to be attached row houses and terraces.

Improving on our last report, the pipeline is expected to hit its 20,500 target in each financial year from FY25, but that is only if approved projects reach commencement and if pre-approved projects achieve their approvals. However, this has come at the expense of current development.

Figure 15 compares last year's pipeline forecast to this year's. **Here, it becomes clear that the apartment pipeline is being 'pushed out.' For example, over the next two financial years, our forecast expects there to be a 24% reduction in units compared to last year's forecast,** while

in the two years following that, there is a 31% increase in units expected for delivery. The uncertainty that's plaguing development in the current market is evident.

Figure 16 presents another way to compare our projections to our last report. Over the next 5 years there has been a 43% increase in the number of units in the pre-approval stage of the pipeline. There are now almost as many apartments in the pre-approval stage as there are under construction. There is also a considerable build-up in apartment approvals that are struggling to commence development.

Apartment projects usually take around 2 years following their approval to get to completion. Only a minimal number of high-rise projects end up discontinued or significantly delayed (around 3% historically). However, our survey of apartment developers revealed that 60% of large apartment projects that reported not receiving development approval have been in that stage for in excess of a year. Therefore, with these increasing financial constraints, a heightened proportion of the 25,000 units in the pre-approval stage may be at genuine risk of deferral or abandonment.

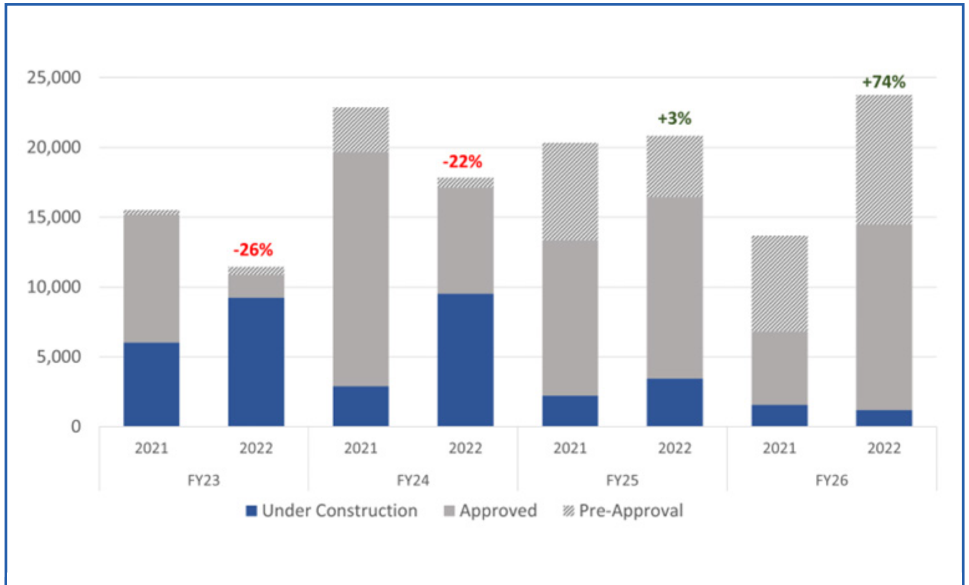


Figure 15: Comparison of Forecasted Apartment Supply in UDIA's 2021 Report and 2022 Report
Source: CoreLogic; UDIA NSW

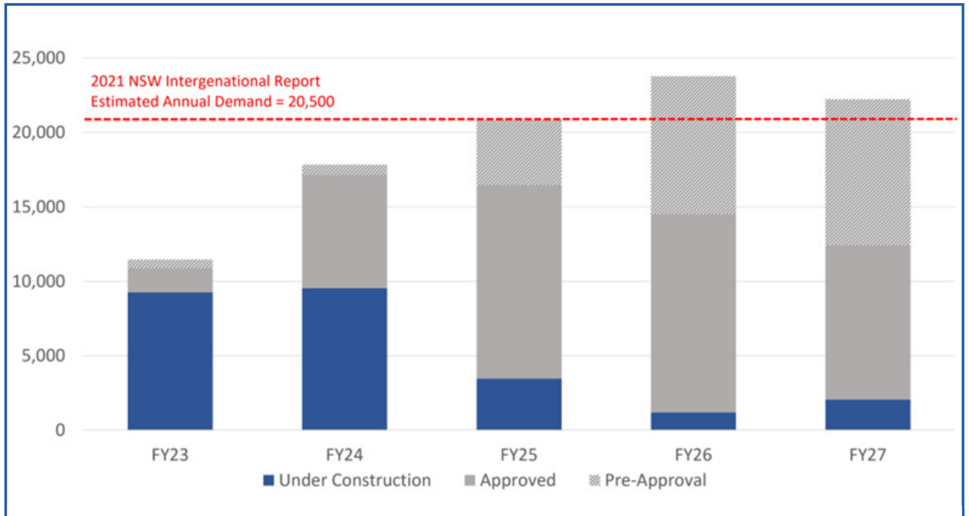


Figure 14: Forecasted Apartment Completions in the Greater Sydney Megaregion, by Project Stage
Source: CoreLogic; NSW Intergenerational Report 2021; UDIA NSW

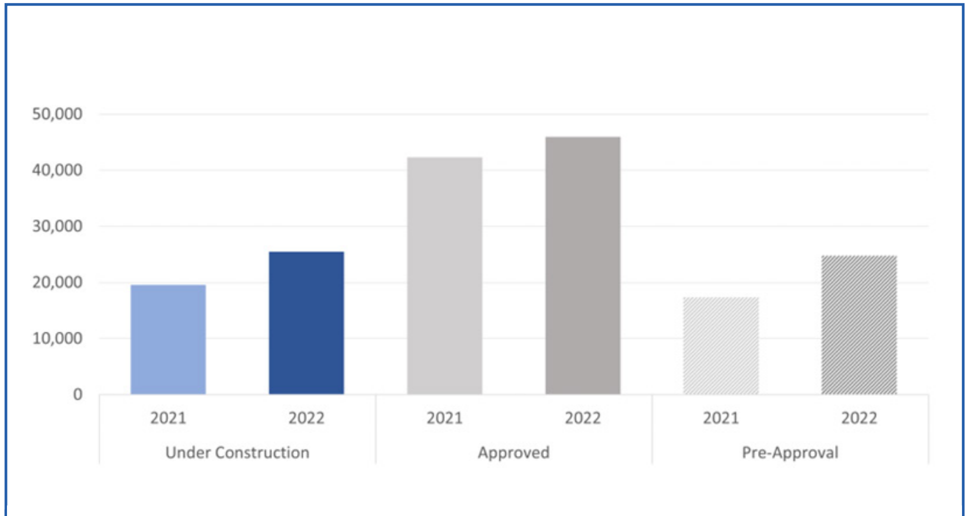


Figure 16: Total Number of Units Forecasted in the Next Five Years by Progress Stage
Source: CoreLogic; UDIA NSW

Unmet demand backlog

In our previous Report, we used the NSW Productivity Commission White Paper 2021 to identify that there was already a backlog of 40,000 apartments across NSW in 2021. Applying the estimated annual demand of 20,500 from the Intergenerational Report to official data on apartment completions in NSW for FY22, we have found an additional shortfall of 8,000 units. We now determine cumulative unmet demand in apartments to have extended to 48,000 heading into the 2022/23 financial year in NSW. The pipeline for FY23 is currently expected to set the State back even further.

At the current rate, undersupply could be around 59,700 by FY25. The years after that may see only a slight improvement. Even if NSW achieved apartment completions that replicated the record 5-year average of 25,000 in successive financial years, it would need to produce this every year for the next 13 years for the backlog of unmet demand to be cancelled out.

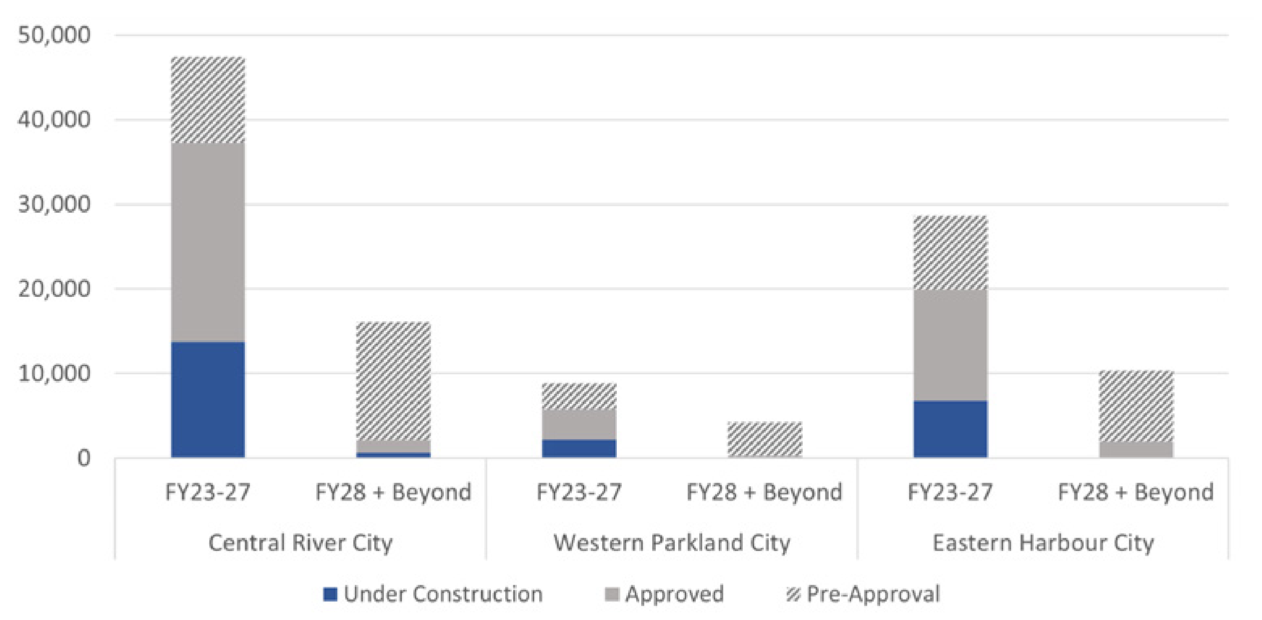


Figure 17: Projected Apartment Pipeline for Cities in the Greater Sydney Metropolitan
Source: CoreLogic; UDIA NSW

Regional Pipeline Analysis

The story of apartment supply can also be considered across regional lines. Apartment development continues to be concentrated in the Greater Sydney metropolitan region, particularly in the dense Central Sydney where nearly 51% of all projects in the pipeline are expected to occur (see Figure 17). The Parramatta LGA alone will produce 14% of all apartments projected in the Megaregion by 2030.

Compared to our 2021 report, there is a **67% increase in apartments in the pre-approval stage across Greater Sydney, but only a 30% increase in apartments under construction.**

The state of the apartment pipeline weakens as we move West. For projected apartment completions, the 3 largest LGAs of the Western Parkland City (Liverpool, Penrith, and Campbelltown), are forecast to produce less than 10,000 units combined by the end of the decade. The lack of diverse high-density opportunities will increase pressures on affordability, especially with the economic potential surrounding the new airport and creation of the 'Third City.'

Figure 18 shows the projected apartment supply pipeline across the regions (Central Coast, Lower Hunter and Greater Newcastle, and Illawarra-Shoalhaven).

Compared to last report, there is a 171% increase in apartments in the pre-approval stage throughout the regions, a 50% increase in apartments that are under construction, and a 36% increase in apartments that are approved, but not commenced.

There is an increase in apartment supply across every region compared to last year. However, the majority of this has come in the form of apartments approved not commenced. For example, in the Illawarra, 1 in every 3 lots in the pipeline are at the pre-approval stage and are not expected to be completed before FY28.

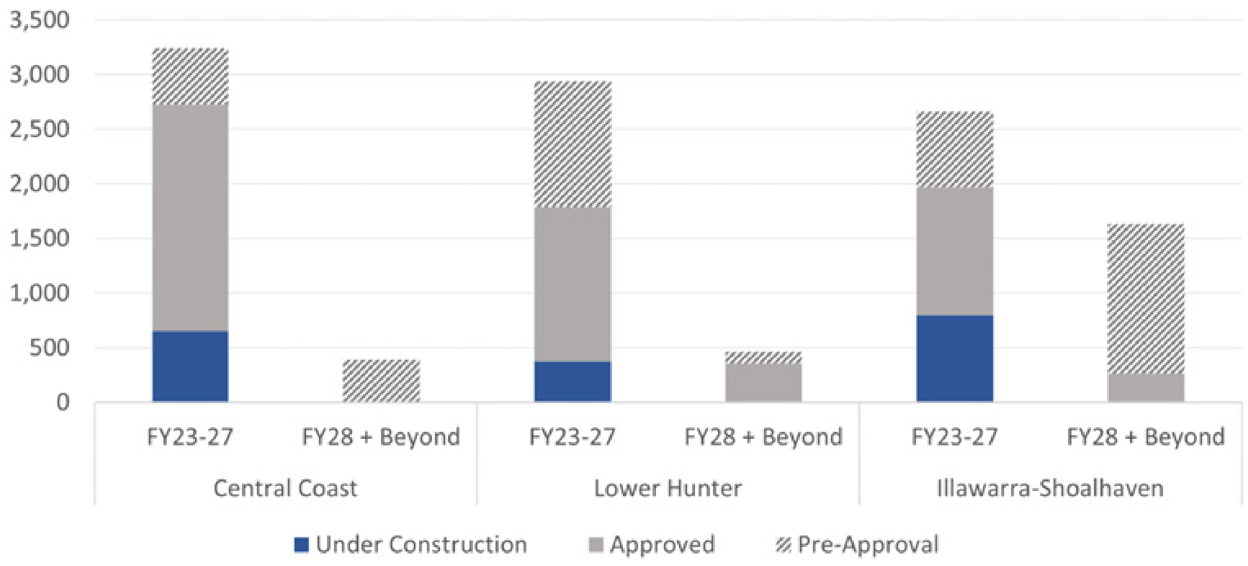


Figure 18: Projected Apartment Pipeline for Cities in the Regions *Source: CoreLogic; UDIA NSW*

Section 6

Constraints Analysis

UDIA surveyed apartment developers in October 2022 to quantify the constraints they are facing.

These can be consolidated into three main issues:

1. Land constraints
2. An inexorably bureaucratic NSW Planning System.
3. Feasibility and financing constraints.

Close to 92% of all units in the survey are facing at least one constraint impacting its development. Our survey covers 58,100 units in the upcoming pipeline.

Large Projects

According to the UDIA developers survey, 88% of units in the pipeline of large projects are currently facing constraints impacting their potential for delivery, an increase from 72% last year. The top 4 constraints remained the same, the need for more presales, delays from VPA negotiations, the prohibitive planning system, and development finance (Figure 19).

Other than presales, all constraints that were captured last year have reported a greater proportion of units constraining them in 2022. Most notably, there was a 127% increase in units reporting roads and transport as a constraint. Significant increases were also seen in obtaining development finance (32% increase), and our new metric for capturing feasibility concerns drew over half of responses reporting it as a genuine concern. **34% of large projects considered development finance, presales, and feasibility to ALL be constraints on development.**

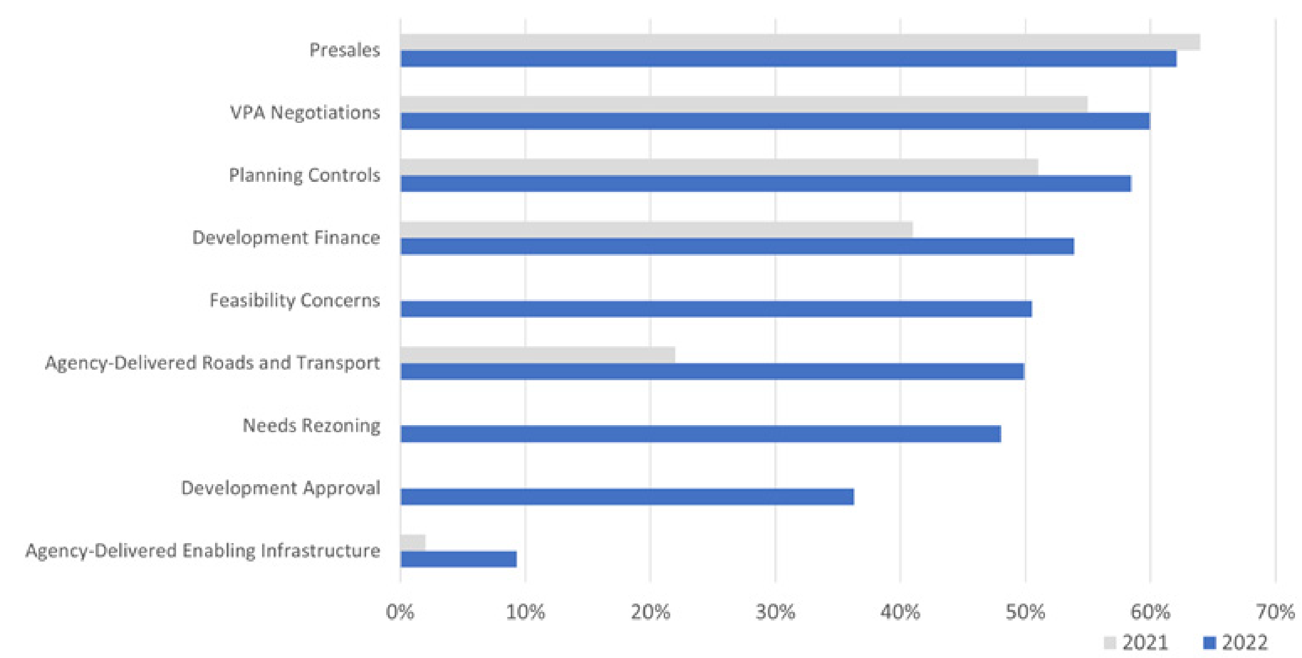


Figure 19: Proportion of Units Impacted by Constraints, Large Projects (>300 Units) *Source: UDIA NSW*

Small Projects

17% of units captured in our survey were part of small apartment projects (expecting to deliver less than 300 units). Figure 20 outlines the top constraints faced by these small projects.

While development finance remained the largest constraint on smaller projects, the rate has more than doubled compared to last year as banks have restricted lending and become less confident in developer's ability to deliver the required margins.

Also unique to smaller projects are the shortages in materials and labour, with the former getting worse over the last 12 months. One fifth of small projects are also awaiting enabling infrastructure (water, sewer, power or transport infrastructure), a five-fold increase from 2021.

With 74% of the pipeline expecting to be delivered by FY27 not commenced construction, and more than 92% of projects reporting at least one constraint on project delivery, completions could be even lower than our projections imply.

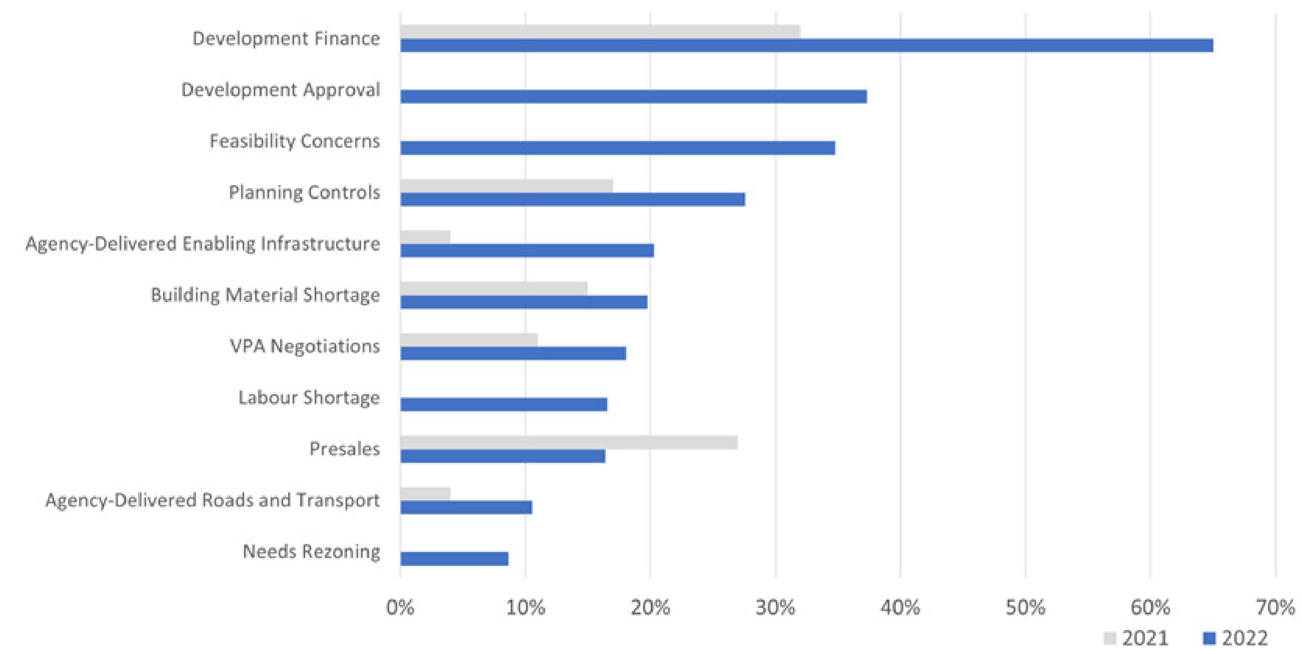
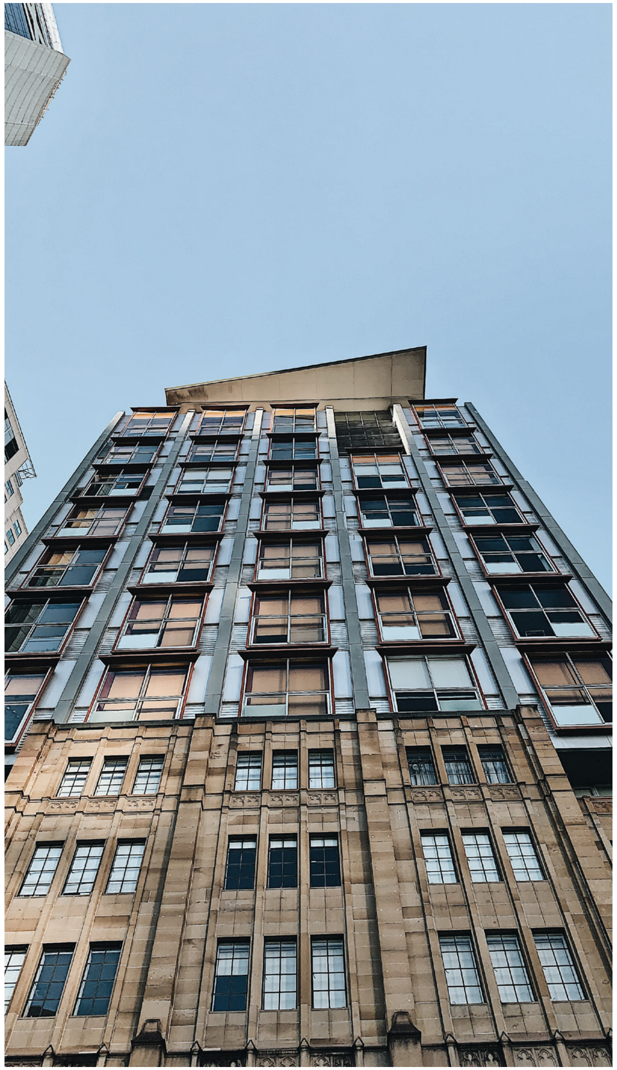


Figure 20: Proportion of Units Impacted by Constraints, Small Projects (<300 Units) *Source: UDIA NSW*

Section 7

Policy Recommendations



As the data section of this report clearly shows, NSW has a significant backlog of apartment demand and a shortage in the supply pipeline that will increase the backlog in the next couple of years. This is likely to lead to further increases in rents above the current record highs as the record-low vacancy rates continue.

After FY24, with a fair wind and a strong policy focus on approvals for feasible projects in the next 6 to 12 months, the supply of apartments has the chance to match the demand, resulting from the migration-led increase to the population. However, even if this was achieved, we do not expect to see enough supply to make a significant dent in the backlog or bring rents back down to historical averages, let alone bring them down to averages in other states. Without action, we will continue to see many less well-off people in NSW struggle to pay their rent, tipping them into poverty and in some cases homelessness. To moderate rental growth, we need to increase supply year in, and year out above what we have historically been delivering. To achieve this uplift in supply, we need to fill the apartment pipeline.

The supply of apartments can be thought of as a pipeline with three phases: Land, Planning and Finance.

At the beginning of the process, there is a need to find appropriate sites for development. This will either be on sites that have been rezoned or sites that a developer expects/hopes to be rezoned. Several indicators suggest that the availability of sites is a significant problem. In Sydney, land costs around $1500 per square metre. By comparison the next highest state or territory is the ACT at well under $1000 per square metre. A second indicator is that major developers are pulling out of buying land for apartments in NSW. At the UDIA NSW State Conference in October 2022, Harry Triguboff AO, Managing Director of Meriton, said that he is no longer buying land in Sydney for his apartments because it does not make sense commercially.

This indicates a problem with the supply of sites for development. For a sprawling low-density city like Sydney with a major shortage of homes, this is unnecessary and approval pathways must be resolved if we are to avoid further escalation of the housing supply and affordability crisis. Fortunately, amongst those interested in shaping our cities for the future, there is a widespread consensus about where we should be putting new apartments – near new and existing transport hubs, especially train stations.

Recommendation 1

The NSW Government should change planning restrictions to enable viable apartment developments and provide a significant supply of new homes.

The second phase of the pipeline is planning.

UDIA's Urban Renewal and Precinct Delivery policy paper from July indicated that inner city precincts, like Camellia, Cherrybrook Station and Rhodes, have spent on average 5.3 years since their announcement as strategic precincts, without rezoning. There are multiple problems with the NSW rezoning and precinct creation process that are essential for a healthy pipeline of apartments:

1. The process is slow sometimes taking over a decade to get to a workable plan, creating significant uncertainty and significant holding costs leading to reduced investment.
2. Rezonings often fail to successfully integrate land use with community or transport infrastructure creating poor outcomes.
3. Outdated methods for transport modelling dramatically restrict development, damaging feasibility.
4. Failing to consider commercial realities. The NSW Planning system is very good at creating utopian plans that are undeliverable for the private sector.
5. The amount of rezonings is bottlenecked by the resources available in the NSW Government.
6. The micromanagement of precincts leads to unnecessary costs and delays.
7. Political interference undermines precincts.

UDIA has worked hard to try and get significant improvements made to the rezoning and precinct process. Unfortunately, this has currently led to only minor improvements at best. Feedback from our members is that there is a significant cultural barrier to improving the process. This is not just affecting private sector developers but is also a major headache for the different parts of the NSW Government that are tasked with creating precincts including DPE, LAHC, TAHE and Landcom.

Given the lack of progress in process improvements, UDIA believes that more radical surgery is required. We believe that there is a strong case for the creation of a new Precincts Agency that develops a rezoning and precinct process, co-designed with the private sector. In addition, to centralise capabilities and focus the agency on the effective delivery of precincts, it should incorporate at least some of the government agencies that are tasked with delivering development. This would be a significant step forward, speeding up the process, improving quality and creating an agency that inherently understands the commercial realities of development and the costs of delayed decision-making.

A streamlined process that assesses precincts by objectives rather than micromanagement will dramatically reduce the resources required for each precinct, allowing more precincts to be created with the same resources and significantly boosting supply.

Recommendation 2

The NSW Government should create a Precincts Agency that is responsible for the timely delivery and assessment of precincts.

Although the recommendations above would go a long way to fixing the problems with government-led precinct planning, given the scale of the challenge to create development opportunities to tackle the housing shortage, UDIA believes that the NSW Government needs to go further by allowing the private sector to carry some of the burdens of planning precincts around transport hubs. To facilitate this, we believe a specially tailored Unsolicited Proposal process should be created that enables the private sector to bring forward precinct masterplans that can be assessed by the new Precinct Agency, and if approved, developed by the private sector. The Government would need to develop a clear set of guidelines on where this could be applied to ensure industry confidence in the process.

Recommendation 3

The NSW Government should create a specialised Unsolicited Proposal Process that facilitates the private sector bringing forward its own precinct proposals.

A key consideration for the supply of new apartments is the density that can be achieved. Unfortunately, there are two significant factors that hinder appropriate levels of density. Firstly, the current transport modelling guidance is widely recognised to be out of date and overly conservative, a problem validated by our survey feedback, where 43% of all apartment projects reported delays with agency-delivered transport. This results in overestimates for car journeys, resulting in lower densities to avoid a theoretical problem with congestion. UDIA is pleased to see that TfNSW has agreed to review the Guide to Traffic Generating Development, which will be the first update in two decades. However, we do not yet have confidence that the approach will deliver the optimum solutions for integrating transport and land use. Much of the time taken by TfNSW is focused on protecting the road network and therefore planning to accommodate growth is limited.

We would prefer to see a co-designed solution that considers the context of individual developments, including the nature of the people in the precinct, the community infrastructure that can be accessed via active transport, and integrating approaches that reduce travel demand such as providing local car share schemes.

Recommendation 4

TfNSW should work with the private sector to co-design a modern approach for assessing the impacts of growth and development on traffic.

The second constraint on density in a precinct is often largely driven by political considerations rather than good planning outcomes. Most major developments encounter significant local opposition. This creates political pressure for the local MP. If the local MP is from the governing party, they will talk to the Planning Minister about reducing the size of the development to placate the opposition. Regardless of who the Planning Minister is, this creates a dynamic that will see the development's density significantly reduced to avoid upsetting a colleague. This is a structural problem and needs a structural solution. A way needs to be found to prevent a Planning Minister from being put in this difficult position. UDIA believes that for major precincts, the densities should be agreed upon upfront by NSW Cabinet and, critically, only amended by Cabinet. This will mean that local members need to get Cabinet to change a decision rather than individual planning ministers, setting a higher bar to reducing densities.

Recommendation 5

The NSW Government should remove the structural bias that creates undue pressure on Planning Ministers and reduces the supply of new homes.

A huge amount of time, effort and resources go into strategic planning for precincts. The resultant masterplans and rezonings come on the back of extensive consultation with stakeholders to understand their aspirations and prepare plans which seek to deliver the greatest possible place outcomes for all. While the success of the current process is debatable, the outcome is meant to be a built and natural environment that is consistent with the finalised strategic plans. And yet the delivery of outcomes aligned with these strategic plans is hamstrung by a convoluted planning process with excessive amounts of time and resources required to have development assessed and approved to deliver outcomes that have already been agreed to.

The environmental impacts of development have been considered through the strategic planning process and should not be re-prosecuted at the development assessment stage. Likewise, the community and stakeholders have had the opportunity to input in the strategic plans and are now fully aware of what development will occur. Provided development is consistent with the strategic plan and established development standards and controls it should be able to be approved quickly and proceed to be built. This should include a complying development pathway where development standards and controls are prepared for the precinct alongside the strategic plan. To ensure this does not further delay the strategic plans being finalised, the complying development plans should be streamlined to only include essential development standards and controls. Overly restrictive complying development controls have the perverse impact of forcing development into a lengthy approval pathway or delivering poor cookie-cutter outcomes.

Enabling development to proceed when it is consistent with strategic plans reinforces the value of strategic planning in NSW which has in the past been called into question. It also enables precincts to be realised in a timely and efficient manner and not be circumvented through a slow and inefficient assessment process.

Recommendation 6

TfNSW should work with the private sector to co-design a modern approach for assessing the impacts of growth and development on traffic.

The final phase of the apartment pipeline is financing.

Like many investments, the financing of apartment development is based on risks and returns. For apartments, financing occurs after planning approval has been granted and an agreed level of pre-sales has been achieved. Historically, most of this funding has come from the banks. As can be seen in our survey data, both pre-sales and financing are major issues for the supply of apartments.

For the banks (or other financiers) to provide development finance, they consider the risks to the development that the loan is not repaid and the level of interest they will charge to get an adequate return. Similarly, a developer will consider the costs of financing in deciding whether to proceed with development and its impact on the hurdle rate (the minimum rate of return on a project to make it worthwhile).

Unfortunately, the current environment is not conducive to financing. Rising interest rates and falling home values have significantly reduced the risk appetite of banks.

Given the scale of the apartment shortage we are facing, we cannot afford to have years where supply is dramatically constrained. We need to have policies that enable new homes to be delivered to meet demand levels consistently.

Contrary to some claims, developers do not deliberately constrain supply when the market is falling. Instead, it is the feasibility of a project that drops below the hurdle rate. Therefore, to keep up the supply of new homes even when the market goes through a downswing, the NSW Government needs policies that significantly increase feasibility and get over the hurdle rates and risk appetite of the banks.

Alas, current NSW Government policies do not appropriately integrate the feasibility of development, inherently assuming rising apartment prices will make feasibility stack up. The problem with this approach is that when the market turns as it has now, feasibility drops, increasing the bank's exposure, and reducing lending and the supply of new apartments.

Key NSW Government policies affecting apartment feasibility include:

- The levels of taxes and charges (including foreign investor taxes) imposed on development and the restrictions placed on housing diversity such as Build to Rent (according to NHFIC, NSW has the highest median charges in Australia).
- Holding costs due to the time it takes to get development approved (NSW has the slowest planning system in Australia).
- The uncertainty created by the NSW Planning System generates a risk premium.
- Restrictions on density (see above).

The continuing accumulation of policies that damage feasibility is unsurprising given the lack of financial and commercial expertise in development within the government. To improve policy making moving forward, this needs to be corrected. The lack of commercial expertise means that most of the NSW Government is inadequately placed to develop appropriate policies for improving feasibility. Instead, a review of policies impacting feasibility should be led by an independent review.

The NSW Government undertakes an independent review of policies impacting on feasibility..

Unfortunately, the current problems with feasibility could get worse if emerging government policies are not properly thought through in areas such as environmental standards and the need for social and affordable housing. UDIA is also currently working on policies that will enable the industry to efficiently reach Net Zero and deliver significant volumes of social and affordable housing without negatively impacting feasibility and the supply of new homes.

Conclusion

The current outlook for the NSW apartment market is not a healthy one, with the supply pipeline dwindling and constraints dominating the decision for projects to commence. Without policies to turn this around quickly, rents are expected to continue to reach record highs and supply will be inadequate to address the demand backlog.

None of this will be fixed if we simply wait for the economy to turn around. With current policy settings, we will simply never build enough apartments in the right places to improve affordability in NSW.

The NSW Government needs to make policy changes in three areas:

1. Increase the number of feasible opportunities for apartment development.

2. Improve the planning system, especially in the way that precincts are developed.

3. Remove the policies that are crippling development feasibility and don't impose new ones.

With policy changes recommended by UDIA in these areas, we can tackle the apartment shortage and the broader housing affordability crisis that we face in NSW.