

Challenging the Statistical Evidence of a National Housing Shortage

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1 Introduction

A number of organisations have released statistical projections indicating that Australia is in the midst of a housing supply shortage, and/or that this shortage will increase over the coming years. The most comprehensive, publicly available account of these projections is the *2008 State of Supply Report* (referred to as 'the Report' throughout this paper), which was released by the National Housing Supply Council² in March 2009. Other formal proponents of the existence of a housing shortage include BIS Shrapnel and the Housing Industry Association.

The purpose of this paper is to critically assess the methodology used to derive the two key conclusions of the 2008 State of Supply Report.

First, the Report concludes that there is a current (2008) national housing shortage of approximately 85,000 dwellings, based on an estimation on homelessness and private rental market vacancy rates. This paper contends that the evidence presented in the Report does not support this conclusion. Over two thirds of the estimated current housing shortage is attributed to homelessness, however the Report does not acknowledge that homelessness is mainly caused by complex and structural social factors, rather than the quantity of housing supply.

Second, the Report concludes that the current housing shortfall could grow to over 430,000 dwellings by 2028 under medium growth scenarios for supply and underlying demand. The methodology of the Report fails to recognise that market forces will be fundamental to determining future market outcomes. As the projections of an increasing future housing shortage are based on underlying demand, they ignore the influence of price and market forces on effective (real) demand. This is the key deficiency of the Report. The conclusion of the Report also ignores the motivations of market participants (including the desire of nearly all people to seek housing through self interest) in determining market outcomes.

The diversity of the housing market and individual housing outcomes is complex. It is difficult to quantify and draw systemic conclusions through data taken from amidst this complexity, as the Report has attempted. The detachment between the methodology and data sets used in calculating the adequacy of current versus future levels of housing supply is an additional flaw in the Report that is identified in this paper.

Although the purpose of this paper is to challenge the statistical evidence of a national housing shortage presented in the Report, it acknowledges that some circumstantial evidence of housing supply pressure has emerged in recent years. It is necessary for the supply of housing to increase to serve Australia's growing population. Meeting future underlying demand may be achieved through the construction of smaller, lower cost dwellings on smaller lots, and better utilisation of the existing housing stock. Government has an important role in the facilitation of new housing development, including through the provision of efficient planning and approval systems, investment in social housing, skills training and the supervision of mortgage markets.

¹ The views expressed in this paper are entirely the author's, and do not represent those of the Department of Treasury and Finance.

² The National Housing Supply Council was established by the Commonwealth Government in May 2008.

2 Theoretical analysis of the housing market

Before analysing the methodology and conclusions of the Report, it is helpful to set out some of the key characteristics of the housing market that will underlie this analysis.

Central to acquiring a deep understanding of both the Report and the surrounding policy debate is an appreciation of the difference between underlying demand and real demand for housing. Although underlying demand estimates are the foundation of nearly all major statistical assessments of the adequacy of the national housing supply, the concept of underlying demand itself is flexible, and often poorly reconciled with broader economic dynamics. The valid theoretical justification of underlying demand is that the stock of houses must grow in line with a society's population, changes in its living preferences, and to replace demolished homes. However, the law of (real) demand states that the quantity demanded of a good is inversely related to its price. As by far the single most expensive purchase in the lifetime of most people, significant real increases in house prices will have a large negative impact on real demand. Housing is an essential good, yet also an economic one.

A functioning housing market will operate similar to other markets over the long run; to find an approximate balance between levels of supply and demand. This market efficiency is characterised by all people except primary homeless (those sleeping rough) having access to at least basic accommodation. Given that the housing supply gap estimates in the Report extend beyond primary homeless, the term shortage, which implies that demand exceeds supply, is seemingly applied incorrectly. This paper therefore uses the alternative phrase 'housing supply pressure' where appropriate. This term better reflects the likelihood that, apart from the homeless, growth in underlying demand for housing can be met not only through increasing supply, but through better utilisation of the current housing stock, in ways that can not be adequately captured by statistical modelling. Market efficiency does not preclude the ongoing structural occurrence of homelessness, housing stress and other unsatisfactory housing outcomes.

2.1 Motivations of market participants

Housing and shelter are fundamental human needs. This compels virtually all people to seek at least a basic level of housing through self-interest. Housing is also characterised by a premium component, meaning that as income rises many people will move to higher value dwellings. The combination of being a need and a want increases the diversity and volume of demand for housing. Most people will aspire to the highest quality of housing available, but which is also affordable.

Housing is an important economic industry, with most people accessing housing in a private market (as an owner-occupier, mortgage holder or rental tenant) that is subject to market forces. In this market, builders and investors are motivated by profit to efficiently construct and provide housing to meet demand. Home builders and land developers do not have an incentive to increase the supply of housing and land to significantly above anticipated demand, as this would increase the likelihood of dwellings and lots being unoccupied, undeveloped, remaining unsold or falling in value, and therefore reducing profit.

The importance of housing to society is also reflected in the range of supportive government policies at the national and state level. Such support includes first-home owners grants, reduced stamp duty rates for first home owners, preferential tax treatment for investors, the absence of capital gains tax on primary residence, rental assistance, training support, social housing and homeless shelters.

The combined force of individuals seeking housing through self-interest, along with the profit motive of industry and the influence of government policy, is significant. In a developed nation with high wages and employment, the power of citizens, business and government

acting with complimentary purpose will result in the provision of a roughly adequate supply of housing.

2.2 Market complexity and data limitations

The large and complex nature of the housing market and living arrangements can be difficult to accurately quantify and summarise. It is challenging to reconcile data sets measuring different components of the housing market. This is compounded by the most comprehensive data source measuring housing market outcomes, the Census of Population and Housing, being collected only once every five years. Market conditions can change significantly within the period between census counts.

Housing supply (referred to as *dwellings* throughout the Report and this paper, meaning a physical, formal human shelter) varies from mansions and luxury apartments to suburban homes, townhouses, units, flats, dormitories, granny flats and caravans. Housing demand (referred to as *households* throughout the Report and this paper, referring to a count of separate living arrangements) is increasingly varied. Household composition has grown more diverse over recent decades with the reduced occurrence of the traditional family unit. Households vary from nuclear families and single parent families to shared housing, couples only, single person households and the homeless. Approximately 70% of households are owner-occupiers (either full owners (35%) or mortgage holders (35%)), with approximately 22% in the private rental market, 5% in social housing and the remainder in other tenure types (National Housing Supply Council 2009).

In estimating the adequacy of future housing supply levels, the Report focuses exclusively on underlying housing demand growth. The main sources of underlying demand for housing comes from immigration and young people forming new households. Estimated residential population data is lagged, being released by the Australian Bureau of Statistics approximately six months after the estimated period. Over 2008, net overseas migration constituted 62% (around 253,000 people) of total national population growth, with natural increase (births minus deaths) the remaining 38% (around 153,000 people). Net overseas migration has historically been the more volatile component of population growth (Australian Bureau of Statistics 2009a). The formation of new households by young people is significantly influenced by the price of housing and social trends, such as the young adults remaining longer in, and often returning to, the family home. Over the twenty years to 2006, the portion of young people (aged 20 to 34 years) living with their parents has increased from 19% to 23% (Australian Bureau of Statistics 2009b).

There is significant potential for people to move between different housing outcomes. Although the living arrangements of most people are relatively constant, there is a small, constant level of transition. People will change living arrangements for many reasons, including employment, lifestyle, family, relationships and finance. It is difficult for data collected at a state or national level to track this movement that occurs at an individual household level. It is even more difficult to measure the number of changes in housing outcomes that are due to housing stress, low affordability and low rental availability (the presumed outcomes of increased pressure on housing supply).

3 Weaknesses in the estimation of a current housing shortage

The first key conclusion of the Report is to calculate that there was a housing shortage of approximately 85,000 dwellings in Australia in 2008. This estimation is based upon different categories of homelessness and low private rental vacancy rates. The appropriateness of these measures in forming the basis of the estimated shortage is critically examined below. The crudeness of the estimated current housing shortage figure is even acknowledged in the Report itself.

3.1 Homelessness

Even by its name, homelessness indicates that it should be an important consideration when analysing the adequacy of housing supply. The reasons for homelessness are complex and difficult to address, including mental illness, substance use, fleeing from abuse, financial hardship and even choice.

The best statistical information on national homeless numbers and characteristics is gathered only once every five years through the census. Even this data is subject to significant treatment due to assumed undercounting. Total national homelessness has remained fairly constant from 1996 to 2006, although at an individual level homelessness is typically characterised by regular movement into and out of homelessness, and between different categories.

Total national homelessness was approximately 105,00 people in 2006, representing approximately 74,800 households and equating to a homeless rate of 53 out of 10,000 people. The total number of homeless was approximately 100,000 in 2001 (Chamberlain and MacKenzie 2008) and 105,000 in 1996 (Chamberlain 1999). The stability in the total number of homeless over this period is despite significant increases in real house prices and a fall in the number of social (government provided) housing dwellings. This suggests that homelessness is predominately caused by structural social factors attributable to the individual, rather than society level economic or financial factors.

Homelessness more likely represents an individual's inability to access the private housing market and an insufficient supply of social housing, rather than an inability of the private housing sector (which accounts for around 95% of total supply) to adequately meet demand. Therefore, the validity of using some homeless data in the estimation of a current housing shortage, as done in the Report, is questionable.

The Report estimates the current housing supply shortage attributable to homelessness as equal to the number of specific categories of homeless households as counted in the 2006 census. However, only some categories of homelessness from the census are recognised in the Report as contributing to the current housing shortage, with no justification offered for this apparent subjectivity. Table 1 sets out data for the different categories of homelessness from the 2006 census and which of these categories are included in the Report.

Table 1: Categories of homeless from the 2006 census

<i>Classification of homelessness in 2006 census</i>	<i>Category</i>	<i>2006 census persons / households</i>	<i>Included in estimation of current housing shortage in the Report</i>
Primary	Sleeping rough	16,400 / 9,400	Yes
Secondary	Residing temporarily with friends or relatives	46,900 / 35,300	Yes
Secondary	Supported Accommodation Assistance Program	19,800 / 9,900	No
Tertiary	Residing in boarding houses	21,600 / 20,200	No
Not counted as homeless	Marginal residents of caravan parks	17,500 / 12,400	Yes
<i>Sub total – homeless included in the Report</i>		<i>80,800 / 57,100</i>	
<i>Sub total – homeless not included in the Report</i>		<i>41,400 / 30,100</i>	

Source: Chamberlain & MacKenzie (2008)

Note: There are some minor discrepancies between the data presented in this table and the data presented in the 2008 State of Supply Report, despite all data coming from the same source. This is probably attributable to rounding, multiple classifications, collection difficulties, presumed undercounting and resulting estimation that characterises census homeless data.

3.1.1 Homeless persons – sleeping rough

Primary homelessness is the only category of homelessness where a person does not have access to formal shelter. The responsibility to provide support for people sleeping rough predominately falls to government and the community sector. In recognising the particularly complex needs of primary homeless, the focus of government policy effort has been to provide not only emergency accommodation but support services. Combined with low or no income, this increases the likelihood that many primary homeless are financially unable to access the private housing market. An increase in privately owned dwellings would therefore not lead to a commensurate reduction in the number of homeless.

Primary homelessness is predominately due to structural social factors, rather than due to the inability of the residential construction sector to adequately supply the market. The appropriateness of using the number of people sleeping rough as part of an estimate of a housing shortage is therefore questionable.

3.1.2 Homeless persons – temporarily sharing with friends or relatives

Although counted as homeless, this category, by definition, does have access to acceptable shelter. The reasons why these people can not independently access the private housing market or social housing are likely to be largely the same as those sleeping rough. In many circumstances these are likely not be ideal living arrangements, and may often be attributable to the previous incidence of housing stress. However, temporarily residing with friends or relatives provides accommodation with the people most suitable to providing assistance, and may be a gateway to more permanent living arrangements.

3.1.3 Homeless persons – marginal residents of caravan parks

The Report also includes marginal residents of caravan parks³ in its measurement of homeless persons. However, even the Australian Bureau of Statistics census publication from which this data is sourced does not include this category of people as homeless.

“We continue to treat ‘marginal residents of caravan parks’ as outside of the tertiary (homeless) population” (Chamberlain and MacKenzie 2008 p5)

Though often basic, caravans are recognised as an adequate and legitimate form of housing, that are included in the census count of dwellings in the ‘other dwellings’ category. To classify some residents of a recognised form of housing as homeless is contradictory. For many people on lower incomes, caravans appear a valid and appropriately affordable housing option. The inclusion of marginal residents of caravan parks in the estimation of the national housing shortage in the Report, as with the two other categories of homelessness outlined above, is therefore questionable.

3.2 Low rental vacancy rates

The Report notes that 3% is generally acknowledged to be the equilibrium vacancy rate for the private rental market. The Report compared the actual private rental market vacancy rates for the capital cities in the June quarter 2008 to the assumed 3% equilibrium rate. It concluded that all of these rental markets are undersupplied (as actual vacancy rates were below 3%). The Report estimated the housing shortage in these markets as equal to the additional number of vacant dwellings required to increase the actual vacancy rate up to 3%. Although decreasing rental vacancy rates in recent years does suggest increasing pressure on housing supply, the accuracy of the methodology used in the Report is questionable.

The Report concludes that the Sydney and Melbourne markets account for 21,000 of the 26,000 dwellings nationally required to lift private rental vacancy rates to 3% (National Housing Supply Council 2009). However, private rental vacancy rates for Sydney and Melbourne averaged 2.3% and 2.6% respectively for the period from the March quarter 1980 to the December quarter 2008 (Real Estate Institute of Australia, various years). These figures challenge the validity of using the 3% ‘rule-of-thumb’ rate as the basis for precise estimations.

The Report states its methodology measures “the difference between the present rental vacancy rate and that required to ‘clear’ the normal volume of new letting transactions” (National Housing Supply Council 2009 p65). However, the 3% equilibrium rate is not based on long-term historical averages, or on any *formal* measurement of the number of vacant rental dwellings required to facilitate efficient household transition (tenants moving into, out of, and between rental dwellings). Therefore rather than measuring a number of people and households that cannot access dwellings, this estimation in the Report purports that there are not enough spare rental properties. It also ignores the motive of property investors who have a financial incentive to keep their house occupied in order to earn a rate of return.

The accuracy of private rental market vacancy rates is also questionable. The data is produced by the state and territory real estate institutes, and therefore it misses information regarding properties rented informally through the owner. Although the fall in vacancy rates over recent years provides circumstantial evidence of increasing pressure on housing supply, the methodology used by in the Report is questionable. The large increases in real house and land prices over the past decade significantly reduced housing affordability, and probably temporarily priced a number of prospective first home buyers out of home

³ Marginal residents of caravan parks are defined as people renting a caravan as their usual address, with no one in the dwelling having full time work of 35 hours per week or more.

ownership. A number of these people are therefore likely to have remained in the private rental market, contributing to lower rental vacancy rates. This shift demonstrates the ability of market forces to determine housing market outcomes, with the rental market absorbing a shift in demand.

3.3 Social housing

The stock of social housing has declined from the 1996 census to 2008 in absolute and relative terms. There were approximately 400,000 social housing dwellings nationally in 1996, falling to an estimated 390,000 dwellings by 2008 (National Housing Supply Council 2009). The Report calculates that if the 2008 stock of social housing had been maintained at the 1996 share of the total housing stock, there would be an estimated 90,000 additional social dwellings. This amount is approximately equal to the projected national housing shortage. From this it could be inferred that the estimated current housing shortage is predominately attributable to the decreasing share of social housing, rather than an inability of the overall market to meet demand. Given the central role of social housing in providing accommodation for those with special needs and/or low income, there appears to be a correlation between the estimated current shortage and decreasing stock of social housing. However, the Report avoids making this or any other major subjective conclusions based on the data presented.

The recent public funding commitments to increase social housing supply appears to be in recognition of the declining share of social housing, as well as being an economic stimulus policy measure. However, as pressure on public expenditure increases, and with social housing imposing significant capital and recurrent costs on government, it appears the provision of social housing by government will remain financially constrained. The quickest and most cost-effective way to increase the supply of social (or privately owned) housing would be the concentrated construction of generic, high density and basic quality apartment towers. Previous experience suggests that this solution could lead to a higher concentration of other social problems, and would therefore not be politically or publicly accepted. However if a significantly greater pressure on housing supply was to emerge, the need for such a solution would increase.

3.4 Dwelling size and average occupants

Two long term market trends identified in the Report also challenge the validity of the Report's estimate of a current national housing shortage. From 1976 to 2006, the average number of bedrooms per dwelling has risen from 2.7 to 3.0, while the average number of persons per household has declined from 3.1 to 2.6 over the same period (National Housing Supply Council 2009). This means that the average number of people per bedroom has fallen from 1.15 in 1976 to 0.87 in 2006.

As noted above, a likely response by government and the private market to the emergence of a large housing shortage would be the construction of a larger number of smaller, low cost dwellings. Therefore, the trends towards larger dwellings with fewer occupants discredit the existence of a national housing supply shortage. These trends indicate that the housing market has been driven more by the demand for increasing housing quality, rather than the demand for increasing quantity. It also shows that there is significant capacity in the existing housing stock to absorb more people.

3.5 Indigenous housing outcomes

The comparatively poorer quality of housing outcomes in many remote Indigenous communities has been long identified. Indigenous people accounted for 2.4% of the total

population in the 2006 census, while accounting for 9.1% of total homelessness (Chamberlain and MacKenzie 2008). The difficulty in improving conditions in these communities through new policy and funding initiatives has recently received coverage in the national media. The Report also acknowledges that the quality of data regarding these communities is particularly poor.

Poor housing outcomes in remote Indigenous communities are attributable to a set of partially unique and complex factors, and therefore require unique and multi-faceted solutions. However, these outcomes will push up national averages, possibly contributing to a misdiagnosis of housing supply issues in the major metropolitan areas.

4 Weaknesses in projections of a future housing shortage

The second major conclusion of the Report is to predict the adequacy of housing supply in the future under different scenarios. The key forecast is that the national housing shortage could grow from 85,000 currently to over 430,000 by 2028, under the medium supply and underlying demand growth scenario forecasts. Table 2 summarising the major projections is presented below. Under most combinations of scenarios, the housing shortage is projected to increase over the next 20 years.

Table 2: Summary of National Net Housing Shortage/Surplus Projections

	<i>In 5 years (2008 – 2013)</i>			<i>In 20 years (2008 – 2028)</i>		
	Low supply growth	Medium supply growth	High supply growth	Low supply growth	Medium supply growth	High supply growth
Low demand growth	279,000	130,000	2,000	894,000	270,000	-262,000
Medium demand growth	352,000	203,000	75,000	1,055,000	431,000	-101,000
High demand growth	452,000	303,000	175,000	1,484,000	860,000	328,000

Source: National Housing Supply Council (2009)
 Note: All figures include 85,000 estimated shortage in 2008. Negative figures refer to a surplus.

Instead of attempting to project future levels of homelessness and rental vacancy rates (a challenging proposition), the projections of the future adequacy of housing supply use different data sets. This paper asserts that this data segregation is a flaw in the methodology of the Report.

Using the estimated current shortage of 85,000 dwellings as a base, the Report attempts to track the movement in the net housing shortage (or surplus) over time by calculating growth in underlying demand and supply. Underlying demand growth projections are based on population growth forecasts, assumptions about net migration, and an extrapolation of census data on household classification types and transition probabilities. Housing supply growth projections are based on an extrapolation of historical construction levels minus projected demolitions.

The detachment between the varying methods and data used in calculating the adequacy of current versus future levels of housing supply is well illustrated by analysing current supply

and demand data. The Report estimates that there were 8.86 million private dwellings⁴ (supply) in Australia in 2008, with only 8.35 million households (demand) (National Housing Supply Council 2009). In contrast to the Report's estimated current shortage of 85,000 dwellings, a prima facie analysis of these data sets indicates a surplus of around 500,000 dwellings.

This surplus is attributable to holiday and secondary homes, new houses recently completed, houses for sales or between residents, and houses abandoned or awaiting demolition. It is highly unlikely that many homeless people, social housing tenants, those under severe housing stress, or people with other poor housing outcomes would be able to move into this spare housing, as it is privately owned and/or located in different areas.

The simultaneous existence of a structural level of homelessness, and a significant number of surplus dwellings, illustrates that housing is inequitably distributed, similar to the markets for other goods, as well income and other forms of wealth. It also illustrates the limitations of a methodology based on a small number of data sets to make conclusions regarding the total housing market, especially given the complexity of this market stretches from luxurious and secondary homes (wants) to small basic dwellings (needs) and homelessness.

The 2006 census found that approximately 830,000 private dwellings were vacant, representing almost 10% of the total housing stock (National Housing Supply Council 2009). The reasons for the discrepancy between the 500,000 surplus inferred above from the 2008 data and the 830,000 vacant dwellings counted 2006 are unclear. This could relate to the different classification of dwellings, imprecise statistical projections, or illustrate the difficulties involved in the collection of data.

Alternative research shows that official current supply and demand data may be underestimated. An analysis of Australia Post residential postal address data indicates that there are at least 10 million dwellings in Australia, significantly higher than the 8.9 million dwellings estimated in the Report. (Gajewska 2009). The divergence of these numbers shows the difficulties of collecting accurate data on the housing market. It suggests the quality of data regarding demolitions, vacant and abandoned houses is particularly poor.

Significantly, the Report does not conclude that the projected future increase in the housing shortage will lead to a commensurate increase in homelessness. In such an outcome, under the medium growth scenario projected shortage, homelessness by 2028 would likely multiply by many times. This outcome, and therefore the projected overall housing shortage itself, seems highly unlikely, because it disregards the overwhelming need for people to seek shelter, builders and property-owners to achieve returns, government to assist society, and the balancing role of prices on real demand.

The key deficiency in the methodology of the Report is that it ignores the influence of market forces. By focusing on population-based underlying demand rather than price-influenced real (effective) demand, the future projections ignore the role of price in determining market outcomes. The Report itself notes that its long-term estimates of a significantly higher housing shortage are unlikely to be realised, because

"in most conceivable circumstances, a large cumulative gap would cause compensating adjustments in price, and in levels of production and demand that would fully or partially mitigate that deficit." (National Housing Supply Council 2009 p64)

Given the inherent difficulties in any type of long term forecasting, such an acknowledgement severely undermines the utility of the projections. This quote concedes that if pressure on national housing supply significantly increased in the future, it would likely lead to an

⁴ The Australian Bureau of Statistics definition of private dwellings includes privately owned dwellings and government provided social housing.

increase in house prices, an increase in rents and investor activity, a shift in market focus towards the construction of a higher number of smaller, cheaper dwellings, and a decrease in real demand for housing. By failing to recognise that similar market forces have historically worked to bring an approximate equilibrium to supply and demand in the current housing market, the usefulness of the current housing shortage estimate is also brought into further question.

The Report acknowledges the fundamental role of market forces in reducing the likelihood that a significant housing shortage will emerge (in words though not in its methodology and conclusions). However this point has seemingly been overlooked by national media coverage of the Report and similar publications. It is unfortunate that this economic fundamental has been largely ignored by policy debates regarding the supposed worsening national housing shortage.

4.1 Spare bedrooms

If a housing supply shortage was to emerge, excess capacity exists in over three quarters of the current housing stock, in the form of spare bedrooms, that could absorb unmet demand. Spare bedrooms represent significant additional capacity in the national housing stock. The Report estimates that in 2008 there were over 3 million households with one spare bedroom (36% of total occupied households), almost 2.7 million households with two spare bedrooms (32%) and almost a further 900,000 households with three or more spare bedrooms (10%). In contrast, the Report estimates that 1.6 million households had no spare bedrooms (19%), while 200,000 households required one more bedroom (2.3%) and 42,000 households required two or more spare bedrooms (0.5%) (National Housing Supply Council 2009).

As outlined above, a large housing shortage would likely be accompanied by an increase in house prices, which would prompt people without access to accommodation to seek it wherever it available and/or cheaper. The increase in house prices would lead to an increase the market rate for other housing costs, including rents and the rate for property owners billeting individual rooms. The motivation for home owners to rent out a room (and thereby increase the effective supply of housing) would increase with the potential financial return. Such a return would also be more attractive in weaker economic conditions, if the property owner lost their job, or with higher interest rates. This illustrates the significant potential for complex market forces to find an approximate equilibrium between supply and demand.

A survey conducted by real estate agency PRDnationwide found that approximately 20% of respondents would consider renting out a spare room in more difficult economic conditions, 14% of respondents currently had someone renting a room and a further 15% would consider taking in a lodger if they had space (*20pc of property owners would rent out a room* 2009). Although regulatory restrictions on sub-letting in some areas are in place, it is unclear how successfully this is enforced.

4.2 Other statistical shortcomings

There are a number of significant sources of housing market supply and demand that have not been captured in the methodology of the Report. These factors bring further doubt to the accuracy of the projections.

The Report notes that there were over 800,000 temporary residents in Australia at 30 June 2008. This category of people, which mainly consists of international students, tourists and business travellers, are not included in Report's formal methodology. Although individually these residents are temporary, collectively they represent a constant and rising source of demand for housing. It is likely that many of these people reside in private

housing, through many also reside in other accommodation (such as hotels, motels, hostels and lodges). This in turn illustrates that public housing and tourist accommodation are an important additional source of housing supply.

Temporary residents and tourist accommodation can arguably be classified as a separate market, and are therefore not included in the methodology of the Report. However, the ability of people to move between the tourist and permanent housing markets, and inability of data to capture these movements, further illustrates the difficulty of attempting to accurately estimate the adequacy of the current and future national housing stock.

5 Circumstantial evidence of supply pressure and market responses

Although this paper contends that the statistical evidence of a current and future worsening housing shortage is poor, it acknowledges that some circumstantial evidence of increasing pressure on housing supply has emerged in recent years. The key evidence of this has been significant real increases in house and land prices, and falling rental vacancy rates.

With high population growth and strong economic conditions, it is possible that the reduced availability of skilled labour, higher materials costs and constraints on new land release restricted the ability of new housing supply to quickly come onto the market. As most population growth and development has taken place in the major metropolitan areas, this has contributed to increasing land scarcity and prices in those areas. Although the Report notes that there is sufficient land availability to meet growth requirements for at least the next ten years, much of this is likely to be in outer metropolitan areas. Such areas often are characterised by high infrastructure and development costs, higher transport costs, and lower access to major employment centres and cultural amenities.

However these factors are all broad in nature, with interacting dynamics, meaning that they are difficult to include in a methodology approach such as that used in the Report. Housing supply pressures have occurred in parallel to, and resulted in, increases in mortgage lending and real house and land prices. This in turn has led to parallel market-based responses such as falling real demand. Over the short run, high house prices (that may be partially attributable to housing supply pressures) will lead to people seeking cheaper housing outcomes such as staying with parents, living in shared housing or moving to cheaper accommodation. Over the longer run, high house prices and underlying demand growth will lead to the construction of a larger number of smaller, cheaper dwellings on smaller lots, and better utilisation of the existing housing stock.

These signs have recently emerged, as the market responds to the increase in real house and land prices. There has been a recent shift towards smaller 'cottage' lots and smaller dwelling sizes in outer metropolitan land estates popular with first home buyers, which aids affordability. The increase in land prices associated with the direct cost transference of infrastructure provision in new residential land development has likely hastened the push towards smaller lot sizes. There has also been a focus on increasing diversity and innovation in new dwelling design, materials and construction methods.

It is only the recent improvement in affordability through lower interest rates, moderating prices and temporarily increased government incentives that has prompted a rebound in the number of first home buyers entering home ownership. This illustrates that strong underlying demand from first home buyers for affordable housing exists, though the time of entry into the market by this segment is significantly influenced by affordability.

Recent comments by Reserve Bank Governor Glenn Stevens illustrate the interaction between bank lending, housing supply and house prices.

“A very real challenge in the near term is the following: how to ensure that the ready availability and low cost of housing finance is translated into more dwellings, not just higher prices” (Stevens 2009 p7).

This analysis suggests that the Reserve Bank sees both increased bank lending and housing supply pressures as distinct, significant factors contributing towards recent house price increases.

5.1 Private room rental market

A recent article regarding the Melbourne private room rental market is probably indicative of the often poor housing outcomes occurring at the lower end of the market. A private group of businessmen control a stock of over 220 lower end suburban homes, which it rents to tenants on an individual room basis only (Reilly 2009). Given that tenants cannot access the private rental market (as they can not afford a bond, do not have referees or are unemployed) and the long waiting list for social housing, tenants are forced to pay a relatively high price for basic accommodation, which could often be dirty, overcrowded and/or in a state of disrepair.

The interpretation of an economic rationalist would be that this demonstrates the efficiency of the housing market clearing to equilibrium. These outcomes have become more likely given the focus on building larger homes rather a higher number of smaller homes. Private room rental assists poorer people to access housing. By definition, a person renting a private room has access to housing, and therefore this does not represent a shortage, even though they may be in housing stress. An alternative perspective would be that this represents the human face of the housing shortage, with the immoral exploitation of lower income earners by ‘slum’ landlords due to the falling stock of social housing.

6 Conclusion

The 2008 State of Supply Report, released by the National Housing Supply Council in March 2009, contains two key conclusions. First, that there is a current (2008) national housing shortage of 85,000 dwellings. Second, that this shortage is likely to grow significantly over the next 20 years in most scenarios. This paper contends that the statistical evidence and methodology used to make these conclusions is highly contestable.

The use of homelessness data and low rental vacancy rates to estimate a current housing shortage is questionable, as an increase in new private housing supply would not lead to a commensurate decrease in the estimated shortage. By focusing estimates of the future adequacy of housing supply exclusively on underlying demand rather than real demand, the Report has ignored the fundamental role of price and market forces in bringing an approximate equilibrium to the market. By failing to recognise that similar market forces have historically worked to bring an approximate equilibrium to supply and demand in the current housing market, the usefulness of the current housing shortage estimate is brought into further question. Linking the estimated current housing supply shortage to future projections that are based on different data sets is a further flaw in the Report’s methodology.

It is unclear the extent to which the methodology of other significant proponents of an increasing national housing shortage would withstand similar critical scrutiny, as these are also all seemingly based on underlying demand. There is significant opportunity for further academic research on this topic. Better information on the complex range of housing outcomes would be difficult to obtain, but would be of great value to policy makers, the construction, land development and real estate industries, and consumers.

Although the statistical evidence of a national housing shortage is contestable, this paper acknowledges that some strong circumstantial evidence of increasing pressure on housing supply has emerged in recent years. This is largely attributable to strong population growth, buoyant economic conditions and the lags associated with new housing supply responding demand spikes.

7 References

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