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'Target 80,000': Addressing Challenges and Unlocking Investment to Meet Our Housing Needs and Drive Our Economy

Property Council 2024-25 Victorian Pre-Budget Submission

2023 was an extraordinarily challenging year for the property industry. The economic pressures felt by so many in the community were present throughout our industry, and directly impacted capacity to develop new product across residential and commercial sectors. This can be directly seen in the level of new dwelling approvals throughout 2023, which reduced by more than 11,000 from the year before, and 20,000 from 2021 levels.

2023 was also a foundational year for property policy development nationally and in Victoria. Governments around the country are acting on the housing crisis in a coordinated way not seen before in Australia's modern history.

The Victorian Government's housing statement provided much needed clarity on the government's priorities for growing housing supply in Victoria. The housing statement is a big step forward, but it ultimately only gets us to base camp in the quest for 80,000 homes a year on average over the next decade, and isn't in itself enough to attract the investment we need to meet the scale of the challenge.

The statement's success depends on speedy and effective implementation, and it needs to be accompanied by other positive reforms and initiatives, especially as other states and territories roll out their plans to attract skills and investment.

Property taxation changes have too often been regressive and investment-stultifying. Property owners have started 2024 with significant land tax increases, while those seeking new development opportunities are now forced to factor in the windfall gains tax, which the Property Council already understands is deterring investment and adding to the complexity of transactions.

A different approach is needed on tax to support the government and industry's shared housing aspiration. Given the domestic market relies heavily on foreign capital to support development, taxation policy should support and promote Victoria as a destination for placement of that capital.

Action is also needed to support the capacity of the building and construction workforce to both obtain the skills needed for greater volumes of production, but also to modernising the construction supply chain. We recognise this is not easy and requires a long-term approach, but the Government has the capacity to make targeted investments in this Budget to kick this work off.

The Property Council's 2024-25 pre-budget submission focuses on key policies that both achieve the full potential of the housing statement, while expanding policy reform to other key areas that will drive both housing construction and economic growth in a time of continued budget recovery from the effects of the pandemic. The government's focus in this budget should be on:

1. **Providing a boost to the state's sagging apartment market;**
2. **Making Victoria the most attractive destination possible for investment into new housing;**
3. **Incentivising housing growth in established areas while also ensuring a strong pipeline in growth areas and regions;**
4. **Investing in initiatives to modernise construction; and**
5. **Lessening the burden on commercial and industrial property owners to drive job and economic growth.**

This submission has been developed with the aim of informing government and key stakeholders of the policy changes the Property Council believes could play a significant role in activating latent capacity in the sector. The initiatives outlined herein have the potential to drive the construction of new dwellings and deliver new housing stock to market - thereby alleviating much of the affordability crisis impacting Victorians.

It is essential that any changes to policy must have at the forefront of analysis, alignment with the commercial requirements of the development industry to deliver an appropriate return on investment having regard to the inherent risks of development, the unstable economic environment driving high costs of construction, labour constraints and increasing cost of capital. Without this as the primary focus for policy, development will simply not occur, and we will not meet our supply targets.

This submission also recognises current budget limitations and the reduced capacity for new spending commitments while the government continues a debt recovery strategy. However, there should and must remain scope for well targeted investments required to drive housing growth to be derived from further public service efficiencies across non-frontline services.

Put simply, staying still in the next 12 months means falling way behind the rest.

As we demonstrated in 2023 through our commitment to the new government-industry affordability partnership, our continued focus will be on working constructively with government and stakeholders to support the industry's ability to deliver on this fundamental community need for greater housing supply.

Cath Evans
Executive Director, Victoria
Property Council of Australia

About the Property Council and property industry

The Property Council of Australia is the leading advocate for Australia's property industry.

In AEC Group's recently updated analysis for the Property Council completed in October 2023, they found the property industry:

- has the largest economic footprint of any sector of the Victorian economy, directly **contributing $58.1 billion to Gross State Product** (GSP) in 2021-22 (12.1 per cent of the total contribution to GSP by all industries in the state) and is estimated to have contributed a further $83.9 billion to Victoria's GSP through flow-on demand for goods and services.
- **directly employed approximately 393,100 full time equivalent (FTE) employees** in 2021-22 (12.8% of Victoria's total) and supported more than 516,300 FTE jobs through flow-on activity.
- **generates approximately 29.8% of wages and salaries** paid to Victorian workers.
- **contributed approximately $23.6 billion in combined Victorian Government tax revenues and local government rates, fees and charges revenue** in 2021-22, equating to 62.4 per cent of total State taxes and local government rates, fees and charges revenues in 2021-22.

The Property Council is committed to the success of the housing statement and our members are committed to delivering thousands of new homes each year in Victoria. Our ongoing dialogue on housing supply and affordability is aimed to ensure future policy changes are practical for developers, and the wider property industry, so the industry can be fully armed to actively address the shortage of new homes in the market.

Support for homebuyers and the residential industry

Consumer confidence took a significant hit in 2023 as economic pressures bit hard and pressures in the building and construction sector became apparent to a far wider audience through the collapse of home builders like Porter Davis. This has translated directly to lower consumer confidence in home buying in Victoria than in other states and territories.

While supply measures are the right focus of the housing statement, we do believe the continuation of demand stimulus is needed to continue in the short term while confidence recovers.

Current stimulus for the market, such as First Homeowner Grants (FHOGs) and stamp duty relief is targeted, quite rightly towards the affordable end of the market.

Given the government has clearly stated its desire to re-balance growth to established Melbourne and to promote greater density, there is an opportunity to incentivise buyers to inner-urban areas with an extension of incentives that support all parts of the housing market.

Taxation does not feature in the housing statement, but the Property Council's strategic aim is to ensure positive taxation changes that both stimulate overall housing supply and support the government's broader '70/30' housing targets. Without change, the taxation environment is contributing to Victoria becoming an uncompetitive destination for critical new investment.

Reactivating sales with off-the-plan (OTP) concessions should be a key priority for government to support the build-to-sell apartment pipeline. Currently OTP concessions are only available if the buyer is eligible for the Principal Place of Residence (PPR) concession or the First Home Buyer Duty exemption or concession.

Apartment commencements have declined from close to 20,000 a year in 2016-17 to less than 5,000 a year in 2022-23, according to the Charter Keck Cramer's bi-annual apartment market update. This corresponds directly with the tightening of eligibility for this concession, while the PPR and first home buyer thresholds have not been modernised to reflect current market pricing.

A reinstatement of more ambitious off-the-plan duty concessions, with as few restrictions as possible on the investor market, will be key to supporting a lift in commencements.

A potential model

- The current off-the-plan concession should be expanded to be made available for more off-the-plan transactions as well as first homebuyer purchases of completed apartments/townhouses.
- There would be no requirement for it to be the purchaser's primary place of residence or to qualify for First Home Buyer Duty Exemption/Concession, so open to all.
- No stamp duty would be payable on any transaction up to the dutiable value of $1m to reflect the increased costs of development but also to encourage purchasing of two or three-bedroom dwellings, suitable for families.
- A 50 per cent discount would then be available on stamp duty payable up to the dutiable value of $1.5m
- The transaction would need to be the first purchase of the property or nomination, so could be available to both off-the-plan or completed vacant stock, and could not be an established re-sale, ensuring the policy would be specifically prioritising new housing.
- It would be available for both owner occupiers and local investors to alleviate pressure in the rental market.
- The discount should be retrospective to eliminate the risk of buyers cancelling their contracts.

Rightsizer initiatives

A focus on housing supply should not only incorporate the construction of new homes, but the utilisation of existing supply. A barrier to homes becoming available for first home buyers are the lack of incentives for existing homeowners to sell, mainly because of the stamp duty barrier on the next purchase.

Exempting homeowners over 60 years of age from paying stamp duty on their final home purchase would incentivise rightsizing and free up larger family homes, optimising existing housing stock. By encouraging older individuals who own a PPR to transition to more suitable accommodation, this initiative supports their changing needs while addressing housing shortages.

In our proposal, this concession would only be available once and if the buyer re-purchased, they would incur stamp duty on their next transaction. This strategic exemption would not only facilitate smoother transitions for older homeowners but also indirectly contribute to improving housing affordability by making larger homes available for families or individuals requiring more space.

Furthermore, the policy promotes a more efficient housing market by aligning the incentives of older homeowners with the needs of prospective buyers, fostering community integration, and enhancing the availability of appropriately sized residences for different demographics. Its dual focus on aiding older individuals in finding suitable housing and unlocking larger properties for others would foster a more balanced and responsive housing landscape.

Treatment of foreign investment

Foreign investors into the housing market in Victoria have been hit with a range of regressive additional taxes and surcharges over the last decade. In a housing crisis, Victoria needs to be welcoming of foreign investment to develop supply, of which a significant percentage is made available to the local market for purchase or rent.

The Property Council proposes the government temporarily suspend all foreign investor surcharges on property transactions and ownership for two years to support investment into the market. Given the government has made recent steps to expand and increase vacant residential taxes, we believe that measure can work in tandem to ensure foreign investors are attracted to Victoria while penalised for leaving homes empty.

We also recommend specific policy actions that will decrease the tax burden on the critical build-to-rent sector and purpose-built student accommodation sectors.

For build-to-rent, we recommend the government extend its existing foreign purchaser additional duty (FPAD) exemption to the operational phase of build-to-rent projects, to align the exemption with other jurisdictions and support the sector's continued growth in Victoria.

Victoria has 15,000 units in the build-to-rent pipeline, but capacity exists for this to be increased with further positive taxation changes, that are designed to increase capital investment into new and existing assets.

Major international build-to-rent (or multi-family) developers and owners have entered the Melbourne market to provide much-needed rental housing supply, and it's essential that the government continues to work to preserve the advantage it helped to create through its 2020 incentive package.

Like build-to-rent, purpose-built student accommodation (PBSA), which provides a customised and fit-for-purpose accommodation option for domestic and international students studying in Australian cities, benefits from a strong pipeline, with over 26,100 beds for students in Melbourne – the largest PBSA sector in the nation.

Historically, Melbourne has enjoyed a strong supply of PBSA developments due to its strong university sector and attractive investment settings. However, the recent doubling of the Absentee Owner Surcharge (AOS) has had a disproportionate impact on a sector which reduces pressure on the private rental market by providing custom living options for students.

PBSA is an asset type underpinned nearly entirely by foreign capital. This is because of the relatively young age of the sector in Australia (12 years), with local investors and super funds preferring to put their capital in asset classes with long track records, like office and industrial. International investors have much more experience and exposure with PBSA overseas, and thus understand its value proposition.

While this foreign capital is desperately needed to grow the supply of beds in a constrained rental market, it also means they are captured by the AOS. Since the increase, owners of PBSA in Victoria have seen an increase of around 170 per cent in their land tax bills. This equates to an **annual cost per bed** of around $2,500 in land tax alone. In comparison, the cost per bed in NSW and QLD respectively is $915 and $145. We are already aware of developments which have been granted approval, but which have been paused while investors weigh up the viability of continuing with new projects in Melbourne.

We strongly recommend that the Government exempts PBSA developments from the AOS – a levy which was originally intended to free up residential stock is having the opposite effect when applied to PBSA – instead dampening the future supply pipeline and leaving more students searching for homes in the private market.

Expanding the Windfall Gains Tax (WGT) exemptions framework

Since the Windfall Gains Tax's introduction on 1 July 2023, we are hearing clear evidence that the tax is already delaying and, in some cases, preventing transactions that would otherwise lead to the development of housing supply. Explaining the WGT to overseas investors is proving incredibly challenging and a deterrent to investment given no other regime like WGT exists in other states.

An exemptions framework was created that carves out some important rezonings such as rezonings within the growth areas infrastructure contribution areas, as well as other select rezonings. But large volumes of rezonings on vacant land, that would otherwise deliver significant volumes of new homes, will continue to incur the WGT.

We request that rezonings for projects that will produce 50 or more new homes of any type be added to the exemption framework, or that WGT notices issued against the land be expired upon construction of the homes.

Incentivising development and purchasing choices in established areas

Creation of special economic zones

To support the government's ambition of delivering to the 'Plan for Victoria' and 70-30 urban growth aspirations which necessitates greater density, we recommend the creation of 'Special Economic Zones' in underutilised and underdeveloped established urban locations, both in metropolitan Melbourne and regional centres.

Broadly based on the Queensland Priority Development Area regime, the zones should be state-led and offer a wide range of developer and purchaser incentives such as:

- Specialised planning schemes for the built form and process to accelerate approvals;
- Tax exemptions to activate development (payroll tax, land tax, absentee owner surcharges, council rate relief); and
- Stamp duty relief for purchasers.

These zones could be implemented in the government's 10 defined activity centres as well as other strategically important locations with existing infrastructure in place. Enabling geographically defined areas for targeted implementation would facilitate rapid growth and support decentralisation to the regions. Including sunset clauses of 30 years within the enabling legislation would also ensure that the circumstances of these areas could be reassessed, and the policy implementation recalibrated.

Local government housing growth

The Property Council have been long-term supporters of competition policy for generating public and economic benefit. The Federal Government have led this in housing with its creation of New Homes Bonus to reward states and territories for meeting their housing targets.

The Victorian Government has an opportunity to replicate this at a smaller scale for local governments that deliver positive housing outcomes, either through regular approvals or policy initiatives. We recommend the Government set up a Local Housing Growth Fund to make a pool of money available for councils.

In recognition of the current financial challenges, we recommend a small fund be made available in 2024-25 as a goodwill gesture to reward a selection of high-performing councils, with the fund to scale up from 2025-26 onwards.

Ensuring a strong greenfields sector

While the Victorian Government has identified its strong desire to move towards a 70-30 split of housing growth in established areas versus growth areas, a strong greenfields development sector will be critical regardless for delivering on housing targets, especially at a more affordable price point which supports entry into the homebuyer market. Without support for greenfields development, 800,000 new homes in the next 10 years simply won't be achieved.

In last year's Budget, the Victorian Planning Authority's funding envelope was significantly reduced. The VPA is a crucial body for ensuring the timely release and development of greenfields and industrial land, and now has an expanded remit to support the delivery of the 10 new activity centres as announced in the housing statement.

The Government must ensure the VPA's funding in the 2024-25 budget is restored to previous levels to enable them to speed up the delivery of new precinct structure plans (PSPs), especially given the increased complexity in rolling out new and upcoming PSPs.

Two other significant blockages to the delivery of greenfields land must also be prioritised and invested in:

- As named in the housing statement, the performance of Melbourne Water as a development services agency must improve quickly. The defining of prioritised service delivery timeframes must be a focus, as well as funding streams to enable Melbourne Water to deliver its development services. This should include the creation of a framework enabling developers to make upfront investments that bolster Melbourne Water resources in scenarios where they are inadequate.
- The changing and inconsistent experiences with the evaluation of cultural heritage on development sites is also significantly slowing many land development projects. A review of cultural heritage must take place that delivers the changes required that supports appropriate cultural heritage protection outcomes and improves the efficiency of the housing delivery.

Expanding opportunities for affordable housing

The Property Council supports policies that will drive the supply of all housing and agrees that further policy efforts are needed to support the industry's capacity to deliver greater quantities of affordable housing.

The Government's expanded Development Facilitation Program was an important first step to do this, but early feedback from the industry has been overwhelming that the faster planning timeframes and lack of third-party appeal rights are still not enough to support project feasibility in an incredibly tough economy and pressured construction market.

On top of expedited planning, the Government should be examining additional industry-supported levers to support private sector delivery of affordable housing, including:

- A defined density bonus framework made available for developers with shovel-ready projects containing a percentage of affordable housing, with priority given to existing precincts and activity centres, but access also provided to greenfield and regional developers, and

- A commitment to tax incentives, such as land tax relief to developers upon achievement of construction milestones and/or completion of housing projects with affordable housing components included.

To support further diversity in build-to-rent housing, the Government should also enable flexibility in management that allows build-to-rent operators to become the direct managers of affordable housing product.

Boosting skills and labour

According to figures from Arcadis, the construction workforce has contracted by 11 per cent in Victoria this year while wages have risen by approximately 14 per cent on average. This increase has been even higher in a range of core categories that continue to place financial stress on building and construction companies and put the feasibility of projects in jeopardy.

In February 2023, Urbis released a report on international migration, which revealed insights into the future of Australia's construction industry.

- Construction workers are getting older, with 8-10 per cent currently aged 60 or older. By 2026, if things stay the same, this could rise to 15-18 per cent.
- Construction apprenticeship cancellations have increased due to tightening labour markets and increased wages.
- Over nearly 20 years of migration data to Australia, Construction trades aren't among the top 10 favoured occupations for both permanent and temporary migrants. In the same period, only 1.8 per cent (35,715) of permanent migrants were in construction roles, and it remains unclear whether they chose mining areas or specific types of construction. Of those 35,715, it is assumed at least 25 per cent or 8,900 made their home in Victoria.

To construct 800,000 homes by 2034, with an annual goal of 80,000, Victoria desperately needs construction workers. Achieving this means the construction workforce must expand by 15 per cent, approximately 50,000 jobs. This marks a notable rise compared to the historical growth rate of 3.5 per cent.

To meet the government's housing goal, employment must increase at an average annual rate of 4.2 per cent. This would lead to around 191,000 new jobs by 2034, assuming a consistent rise in dwelling completions, reaching a peak of 103,500 in 2033.

In the Federal Government's recent migration strategy, under the new 'Skills in Demand Visa', which replaces the existing 'Temporary Skill Shortage Visa,' trade workers, machinery operators, drivers and labourers earning $135,000 or above are not eligible to apply.

It is essential that the Victorian Government advocates strongly to the Federal Government to ensure the nation's migration pipeline is bringing in more people with specific building and construction skills to ensure the migration pipeline into Victoria supports industry expansion in the short-term, while skill development and capacity building initiatives support longer term industry sustainability.

Modernising construction: supporting prefabricated building methods

Despite rising interest, only about three per cent of building activity in Australia involves prefabrication (commonly abbreviated to prefab). In countries like Sweden (80 per cent prefab) and Japan (15 per cent prefab) with strong manufacturing, prefab is more significant.

Prefab faces challenges in Australia due to its cost, relying on making building parts in factories instead of on-site. Establishing these factories demands a significant amount of money for both setup (CapEx) and ongoing operations (OpEx). Success in prefab depends on having many ongoing projects to cover initial costs and sustain investment.

Investing in prefab for housing development in Victoria is vital for achieving the goal of building 80,000 homes yearly. Adopting prefab offers several benefits, including:

- Speed of construction: faster timelines due to offsite component manufacturing.
- Cost efficiency: despite setup costs, long-term savings through streamlined processes.
- Consistency and quality control: controlled environments enhance quality, ensuring durable and reliable housing.
- Economic stimulus: supports new industry growth, creating job opportunities.
- Scalability: highly adaptable to meet increasing housing demands.
- Flexibility in design: allows architectural creativity while benefiting from offsite efficiencies.
- Risk mitigation: controlled factory environments help mitigate risks such as on-site weather delays and ensure smoother project execution.
- Meeting housing diversity needs: adaptable to various housing types, including apartments, detached houses, and specialised structures.
- Sustainability: reduces waste generation as materials are measured and used efficiently.
- Innovation and technological advancements: encourages modernisation and innovation.

We encourage the Victorian Government to explore investment they can make in the 2024-25 Budget to support a domestic prefab supply chain, given the capital expenditure that will be required, and undertake direct engagement with large-scale residential developers to determine the precise nature of how investment can be deployed. We recommend the establishment of a joint industry and government working group to examine these issues and how to incentivise the domestic market to participate.

Priorities for commercial property owners

Commercial and industrial property owners across different asset classes have not escaped the tough economic conditions. Office asset owners and investors are dealing with a highly bifurcated market, with the Melbourne CBD vacancy rate for B grade buildings now beyond 20 per cent. Given more than 60 per cent of commercial offices in the CBD were built before 1990, we expect this trend will only deepen over time.

Industrial property demand has been incredibly strong over the last few years, with demand only slightly softening from record low vacancy rates in the second half of 2023. E-commerce, data centres and an increase in domestic manufacturing is expected to keep demand strong, but a combination of escalating construction costs, scarce land supply and a higher tax base but will put cost pressures on owners – and therefore on tenants and customers.

For many larger commercial property owners with a mix of investors from on and offshore, they're now dealing with not only the COVID debt levy on their landholdings, but the doubling of the absentee owner surcharge to 4 per cent which began on 1 January 2024.

In an increasingly competitive environment, Victoria needs to do more to attract investment into commercial property, which underpins so many jobs and industries. A couple of important steps for the Government to take in this Budget are to:

- Provide exemptions or discounts from the absentee owner surcharge for commercial property owners which can demonstrate a history and commitment to creating and supporting local jobs, either through their organisation or their tenancies.
- Revisit the narrow Victorian stamp duty wholesale unit trust regime, which has a minimum land holdings requirement, and is only available where certain limited categories of investors hold at least 70% of the units in the trust and not typically available to foreign investors.
- Finalise a strategy through the 'Plan for Victoria' development process for ensuring a boost to short and long-term industrial land supply in Victoria.

Seizing the Geelong opportunity

The key success of Victoria's growth trajectory has been the rapid rise of Geelong into a true 'second city' for Victoria.

Our Geelong Committee is working collaboratively with stakeholders and allies in the region to support more ambitious development outcomes that will cater for central city population growth where so much more is possible, as Newcastle and Wollongong demonstrate in NSW.

The Central Geelong Framework Plan released in early 2023 provides clarity on strategic direction, but the Government can do more to accelerate investment in central Geelong and seize the current opportunity by:

- Creating a specific Geelong development concierge service, a standalone department between council and ministerial level to assess applications of scale with a focus on creating new housing supply and mixed-use developments in central Geelong.
- Prioritising the Central Geelong Framework Plan action of the preparation of a Geelong Station precinct master plan that supports an appropriate mix of commercial and residential development.

Scaling up our energy transition plans for buildings

The Property Council's *Every Building Counts* policy platform was updated in 2023, providing governments across all tiers with a series of recommendations to drive the transition of the built environment to meet our state and national net zero targets.

In many areas, the Victorian Government is to be commended for its leadership across many areas of energy policy, and we anticipate further developments in the ongoing Gas Substitution Roadmap in 2024 but we believe there is scope to prioritise some key actions so far missing or limited to date, such as:

- Delivering the state's first building retrofits strategy, focusing on older commercial properties, which incorporates financial and planning incentives for building upgrades.
- As part of wider planning reform, affirm a series of incentives such as density bonuses for new medium-rise residential projects or height bonuses for new commercial projects that go beyond current energy and sustainability benchmarks.
- Implement a long-term taxation incentive program for high performing buildings, focusing on land tax.
- Working with local government, finalising a suite of available incentives for potential adaptive reuse projects.