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House rents set to rise again

With the economy on the mend and the property market back on the boil. Life is about to get harder for Melbourne renters.

Why? Because, as strange as it sounds, the global financial crisis actually tempered some of the worst effects of what had been considered a deepening rental crisis in 2007-08.

Far too few houses and apartments were being built to meet the needs of Melbourne's rapidly swelling population. In turn, strong property price growth and rising interest rates meant a growing number of renters could not afford to become home owners.

The result? Demand for rental housing soared, Melbourne's rental vacancy rate hit rock bottom and, ultimately, rents skyrocketed.

Back then, the market was awash in grim stories of families priced further and further out of the city; of every property, regardless of quality, attracting scores of applications; of inspection lines that ran out the door; and "rental auctions" where would-be tenants competed to pay rents well above market value.

Australian Property Monitors, which is owned by Fairfax, reports that Melbourne's median weekly rent rose in 2007 by a record-setting 15.8 per cent for houses and 16 per cent for units.

In 2008, rising interest rates (with costs passed on to renters by landlords) and pent-up demand pushed rents up a further 9.1 per cent for houses and 10.3 per cent for units.

By comparison, rental growth hadn't topped 3.6 per cent for houses or 4.3 per cent for units from 2005-06, even flattening out and falling during the minor downturn of 2004.

In real money, the 2007-08 growth spurt saw an increase in weekly rents from \$285 to \$360 for houses and \$250 to \$320 for units.

Meanwhile, the metropolitan rental vacancy rate dipped to as low as 0.9 per cent but never rose above 1.6 per cent in any month during that two-year period. The Real Estate Institute of Victoria believes that a vacancy rate of about 3 per cent is "optimal": tight enough to ensure profitability for landlords but flexible and affordable enough to give tenants some choice - a level that hasn't been seen in five years.

No wonder there was so much talk about a rental crisis. Then came the global financial crisis and the spectre of a lengthy economic recession, which caused enough uncertainty to see rents nearly freeze in place and vacancy levels increase, albeit only slightly, following frantic bids to prop up the property market.

APM estimates the median weekly rent for houses held steady at \$360 in 2009. For units, it rose by just \$15 to \$335 per week. "Less people were moving into the rental market. When graduates and school leavers weren't getting jobs, or couldn't count on a steady income, they were more likely to stay (at home) than to move out" APM economist Matthew Bell says.

Others chose to move back home or into shared accommodation. The Reserve Bank's decision to slash the interest rate and the massive subsidies offered to first home buyers by the Rudd Government in late 2008 also played important roles in loosening up the rental market.

"Landlords, whose expenses declined because mortgage rates fell, realised that they'd rather have their property occupied at the same rent rather than vacant if they raised it," says Robert Papaleo, director of research for analyst Charter Keck Cramer.

The low interest rate and first home buyers grant also encouraged many renters to speed up their decision to get on the property ladder, freeing up more rental opportunities.

“The move to (home) ownership has been very strong in Melbourne, so I think that might have relieved a little bit more of the pressure compared to some of the other cities around the country,” Mr Bells says. But this brief respite now looks to be ending.

Many of the same conditions that drove the strong rental growth seen in 2007-08 are set to come back into play now that the threat of an economic downturn is fading. Rents are expected to increase as employment and wage levels improve and landlords seek to cover rising mortgage costs.

While the REIV says the metropolitan vacancy rate rose to 1.6 per cent in December - the highest it has been in three years - Melbourne’s near record population growth and ongoing shortfall in new housing supply are expected to see it tighten once again.

APM is forecasting median rents will rise to \$380 for houses (5.6 per cent) and \$360 (7.5 per cent) for units this year, the strongest growth rate seen apart from 2007-08.

Mr Papaleo agrees. He says [Renters] had a bit of a breather in 2009. I don’t see rents running away to double-digit growth in 2010; it’ll be a much more modest increase.

“But its not as if they have got much of an alternative now. With interest rates going up, the first home buyers grant essentially wound back and property prices at an even higher base than before, all these factors will discourage renters from going into home ownership.”

Hocking Stuart chief executive Nigel O’Neil says rental increases are expected to be about 6 per cent in most areas of the city, rising to as much as 10 per cent in popular suburbs such as South Yarra, Elwood and Richmond.

“There have been up to 120 applications for some rental properties that are well positioned and reasonably priced,” he says.