



EXCLUSIVE FRI 03 SEP 21

[+] Pandemic Pain Not Enough To Bet Against Melbourne Apartments

Developers have halted apartment projects in Melbourne after a perfect storm of factors prompted investors to turn their backs on the sector. But circumstances may be changing.

The pandemic forced border closures, ending the steady stream of international students and skilled migrants taking up residency in inner city high-rises.

That was followed by the ongoing [cladding crisis](#), a global shortage of [construction materials](#), tightening planning requirements and widespread issues with [building defects](#).

And to top it off, federal and state governments have eased support for the sector at the same time as apartment buildings have been locked down due to localised Covid-19 outbreaks

Now, vacancy rates have more than doubled in parts of the inner city as supply, existing and new, is slowly absorbed amid subdued rental conditions.

But is now the time to bet against the Melbourne apartment market? Opinions differ.



The Urban Developer

Not fit for purpose

While the broader property market has been resilient, apartments haven't been deemed fit for purpose in the current climate, chief executive of First National Real Estate Ray Ellis says.



▲ While houses have experienced huge growth, apartments have not during the pandemic, and no more so than in Melbourne.

“I’d never say that the quarter-acre block or that inner-city investment has disappeared, but we’re all evaluating everything, because right now our homes are our office, our playground, our holiday area, entertainment area ... so the impact of Covid is that it’s made us re-evaluate what we’re looking for in our home,” Ellis says.

“At the moment, there’s a construction quality stigma attached to large-scale apartment projects, and it would take a fairly game developer to push ahead in the current market,” one developer told *The Urban Developer*.

Beyond the challenges of the product design and suitability, is the rising planning risk associated with CBD sites. Recent changes to restrict building heights have also had an impact on developer appetite.

Buyer’s agent Lloyd Edge says developers have stopped buying sites unless they are permit-approved, however, more speculative developers are unwilling to bet against Melbourne’s future.

“Demand will dry up for six months or so. Once vaccine rates are up, people will move back into the city, and rents will rise,” he says.

Melbourne's two-speed market

Melbourne's apartment supply data is showing continued [signs of slowing](#). A number of approved projects are experiencing delays brought on by weakened pre-sale demand, rising land and building costs and stricter funding conditions.



▲ The pipeline of apartment projects in Melbourne has dwindled in the past year.

At the end of the 2020 second quarter, 15,900 apartments were under construction and due to be completed up to 2024, mostly in the city precinct. That is 12.6 per cent less year-on-year to previous years.

JLL reported signs of settlement default starting to appear, with Melbourne beginning to see apartment sales fall last year as the pandemic began.

“A soft pre-sales environment is seeing some projects abandoned or delayed, as developers reassess their feasibility,” the report stated.

But it's worth noting that built apartment development projections are rarely a sign of new stock to market, with many apartment projects never actually making it to market, chief investment officer of real estate debt and investment specialist MaxCap, Bill McWilliams, said.

“Apartment build projections are at a 10-year low compared to where stock has been historically, but the fact is that a percentage of these will never eventuate,” McWilliams says.

However, it's a two-speed market. The slowdown is mostly impacting inner-city, high-density developments, while smaller boutique projects on the city fringes continue, noted a recent report by Charter Keck Cramer.

That's certainly the case for Birkill Developments. Managing director Brett Birkill confirms he is pushing ahead with five separate developments in the sub-\$1-million sector in the eastern and northern suburbs, appealing mostly to first home buyers and downsizers.

Educating consumers

But there are moves to settle public nerves over the future of apartments. The Australian Apartment Advocacy is rolling out an [education kit](#), answering questions for buyers about the asset class.



▲ Consumer confidence in apartments is down after a slew of defects in developments.

A recent poll reveals 33 per cent of apartments have defects, so the issue is trying to convince apartment buyers that the asset class is a good choice, chief executive Samantha Reece says.

The Apartment Living Report surveyed 3600 apartment owners nationally and found that 54 per cent of the more-than-1000 Victorians surveyed are living in apartments with defects.

One example, Reece says, was a Melbourne buyer who paid \$750,000 for an apartment only to discover that when it rains, the water does not drain away, flooding the balcony and then into the apartment.

Once the pandemic retreats, is over and things return to normal, Reece says, demand will exceed supply and apartment prices will rise, despite only 15 per cent of buyers revealing they are comfortable buying off the plan.

“Developers have pivoted away from these developments, which have had good returns historically. There won’t be immediate issues, but there will be a shortage of accommodation in years to come,” she says.

A strong return

Many predict the asset class will return even stronger, with the undersupply issue pushing prices higher for both the purchase and rental markets.

Chief executive of Investorist Jon Ellis believes waning consumer interest will turn before long.

“A lot of these people buying in the outer suburbs don’t actually want to live where they’ve been buying properties. They’ve done this as a financial play, and I think we’re going to find those people wanting to move back to the city.”

Ellis says a quick glance at Google Earth reveals an availability of possible sites ripe for development across Melbourne, many which have already been secured.

The inner-Melbourne area of Fisherman’s Bend, for example, has been a problematic development area, with few successful projects, he says.

But he sees light at the end of the tunnel for the Melbourne apartment sector.

“The sector has copped a bad rap, but it will be short-lived. Once borders open, international professionals and students will want to return to Australia and seek apartment living,” he says.