

An Insight into Knockdown-rebuild Activity

Introduction:

This ACI Research Snapshot provides a preliminary analysis of Australia's knockdown-rebuild (KDR) market, following our initial research into this segment of new home building early last year.

As previously highlighted, while this will be a growing and increasingly important element of the residential construction sector, there is scarce available data to provide a detailed insight on and understanding of its dynamics.

That is, official sources – building authorities and the Australian Bureau of Statistics (ABS) – do not provide

Background:

Total new home building activity in Australia has a number of components to it, including construction that occurs on greenfield sites as well as construction that occurs on pre-existing or 'second-hand' residential land sites.

Part of this latter type of building activity can be understood as an upgrading in the housing stock, rather than as an augmenting of the overall supply of dwellings to meet demand from population growth. This 'replacement stock' segment of the market – or one-for-one KDR activity – will become increasingly important within Australia's new home building landscape. That is, as the overall stock of housing grows, so too does the need to upgrade this stock into the future. Furthermore, this one-for-one KDR activity will likely be larger in times

The Economic Backdrop:

Australia's gross domestic product (GDP) continued its streak of below-trend growth at the end of 2014/15, growing at just 1.9 per cent that year. In the September 2015 quarter, the pace of annual growth improved albeit remaining below the 3 per cent 'trend' rate, at 2.5 per cent. While this performance does not compare so favourably with longer term trends, it is still reasonable, aided substantially by the strong growth in overall new home building activity.

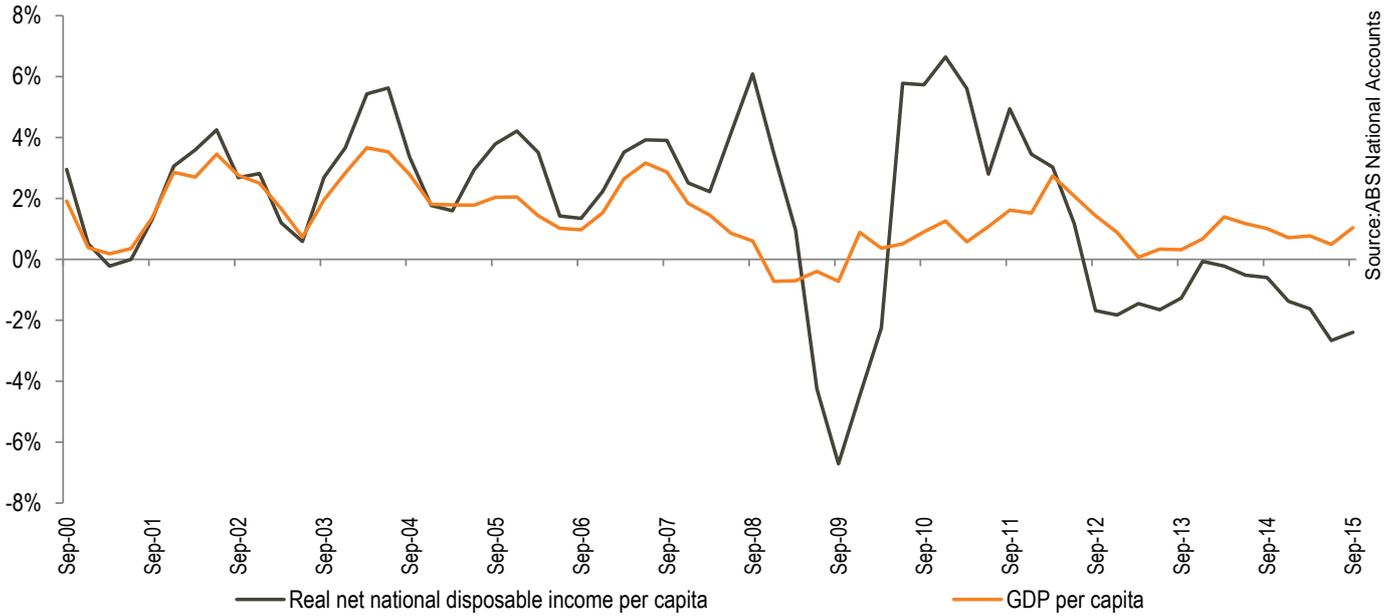
data on this form of activity equivalent to what is available for overall new home building (finance, approvals and commencements data, for example). Results from the HIA-Colorbond steel Housing 100 survey therefore present a useful starting point for understanding this segment of the market, in relation to this kind of work performed by Australia's large volume builders. Moreover, ACI is currently reviewing the scope for more detailed data collection (see further details below).

of stronger increases in real (ie. inflation-adjusted) wealth and incomes and vice versa. In an economic environment where Australian households are experiencing relatively strong growth in real wealth and incomes, they will likely have a higher propensity to upgrade their housing, giving rise to a greater number of households demolishing an existing home and re-building a new home in its place.

Another element to construction that occurs on "second-hand" land is activity that does add to the stock of housing by urban densification – the rebuilding of two or more dwellings on a site (or sites) that previously only contained one dwelling, or more loosely, one-for-two-or-more KDR activity.

Of particular concern, however, is the ongoing weakness in real household income growth, which has weighed on consumer confidence, itself remaining fairly anaemic even if just in positive territory. Against this backdrop, household expenditure and business investment have remained at best fairly ordinary, with growth in these elements of GDP remaining below what typified pre-GFC times.

GDP AND NET INCOME GROWTH, PER CAPITA



Following a long stretch of remaining unchanged, the Official Cash Rate (OCR) was reduced to a fresh all-time low of 2.0 per cent in May 2015 and has since remained at this level. While the RBA board is relatively sanguine on the economic outlook, it is also ready to reduce the

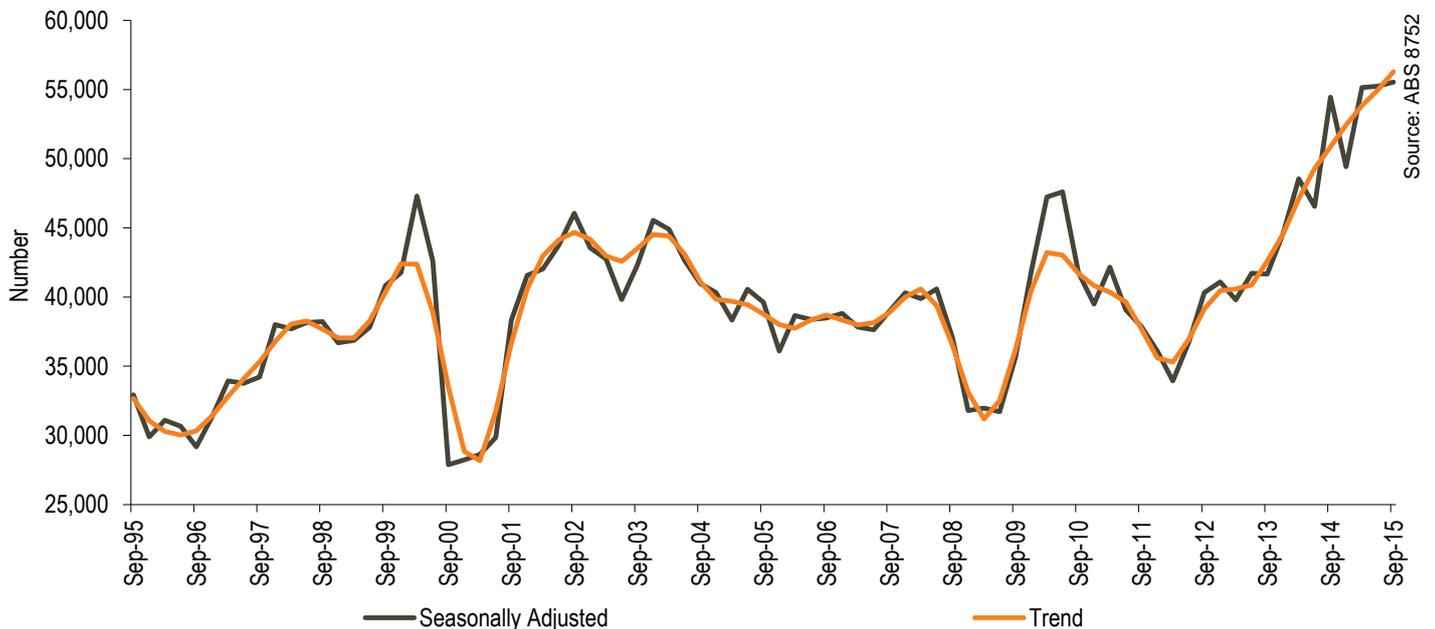
cash rate should any deterioration in global economic and financial conditions derail an improving Australian labour market and dent domestic economic growth prospects.

New home building activity:

New home building activity continues to be the healthiest component of Australia's domestic demand. In the 12 months to September 2015, new dwelling commencements reached a fresh record level of nearly 215,000. The key drivers of the new housing boom include the lagged impact of record population growth, very low borrowing costs, strong dwelling price growth in key markets and record foreign investment in new residential property.

However, many of these factors have since started undergoing changes that will not be as supportive of new home building activity. Namely, population growth has started slowing largely due to reduced inflows of overseas migration; dwelling price growth has since decelerated in key markets; and foreign investors now face higher barriers to entering the domestic housing market.

TOTAL DWELLING STARTS – AUSTRALIA

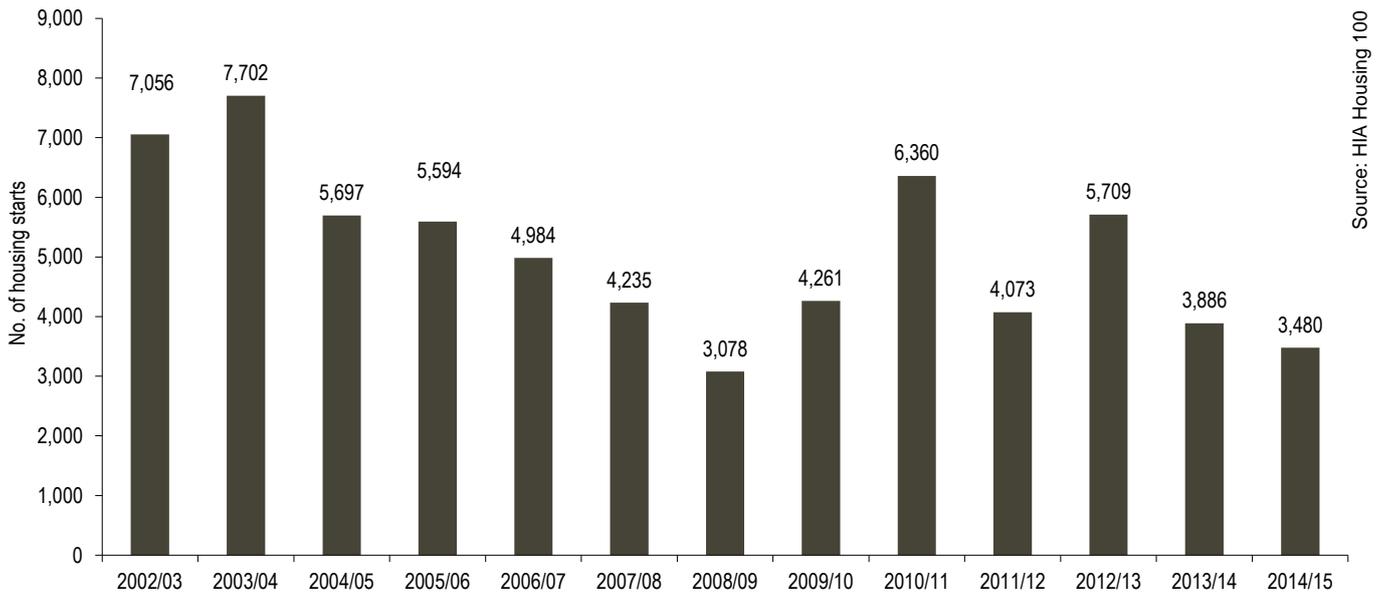


Knockdown-rebuild activity among Australia's largest builders:

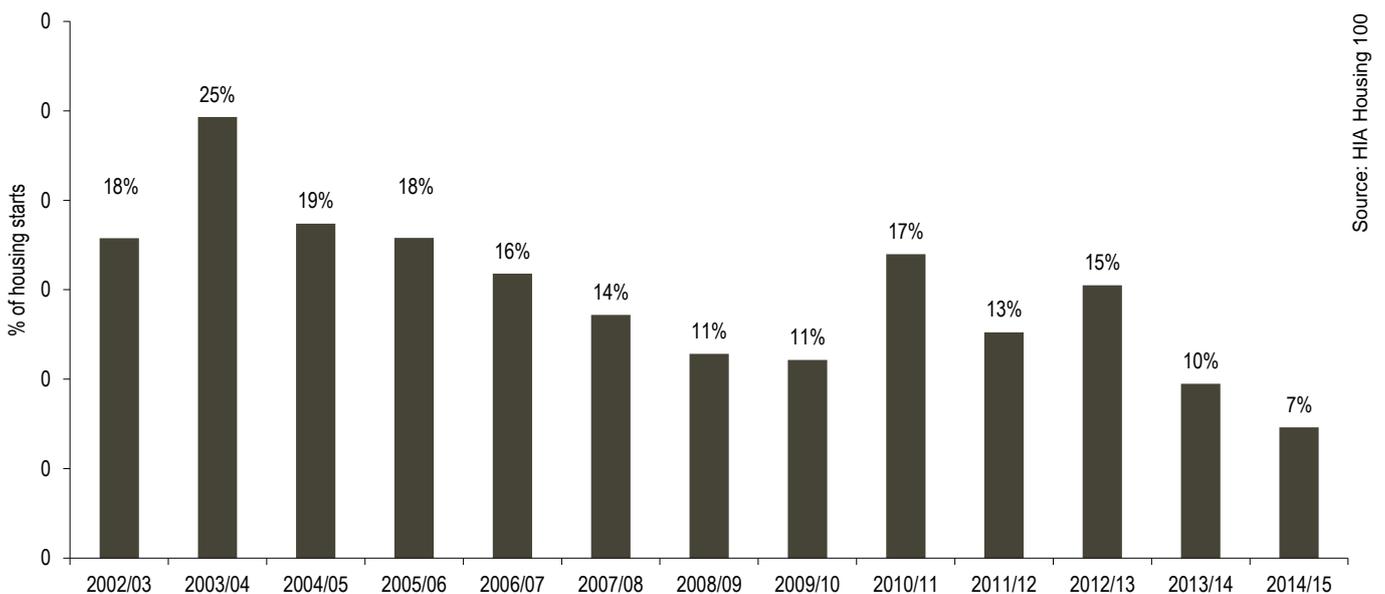
ACI's existing data currently shows the percentage of Australia's largest volume builders' new housing starts that are KDRs. That is, the Housing 100 survey asks participants what percentage of their detached or semi-detached starts were a knockdown-rebuild. Broadly, these survey results show what percentage of these large volume builders' new detached and semi-detached housing starts occurred on 'second-hand', rather than greenfield residential land sites.

The survey results over the past 13 years are summarised in the chart below. Unsurprisingly, amid ongoing weakness in real income growth in 2014/15, the KDR share of total activity fell to a new low of 7 per cent among these larger builders. This latest KDR share compares with previous years where it accounted for at least 10 or more per cent of activity. In 2003/04, KDR accounted for nearly one quarter of detached and semi-detached new home building activity.

KNOCK DOWN REBUILD ACTIVITY - NUMBER OF STOCK



KNOCK DOWN REBUILD ACTIVITY - PERCENTAGE OF STOCK



Scope for further research

As highlighted earlier, KDR activity is composed of one-for-one replacement activity as well as two-or-more-for-one (densification) activity.

A starting point for further to ascertain from those currently surveyed, of their overall KDR activity what represents one-for-one replacement and what provides additional housing stock through densification, or two-or-more-for-one KDR activity.

Moreover, research under consideration is KDR activity undertaken by small and medium-sized builders. These groups of builders are likely to be performing a large share of overall KDR activity.

Nevertheless, KDR activity undertaken by large volume builders is still very significant and provides insight into current conditions within this segment of the new home building market

Further information is available regarding KDR activity undertaken by Australia's large volume builder sector, at a national level and across the five mainland states. Data is also available on the breakdown between single storey and double storey detached house starts. For further details please contact Stuart Hylton-Cummins or Kirsten Lewis at info@aciresearch.com.au

ACI produces a wide suite of publications and research which include the latest industry analysis, forecasts and emerging trends, at a national, state and even regional/local level. For more information on the products and services of Australian Construction Insights (ACI) visit our website aciresearch.com.au



AUSTRALIAN CONSTRUCTION INSIGHTS
Research powered by HIA Economics

CONTRIBUTORS:

Diwa Hopkins Economist

Harley Dale Chief Economist

Disclaimer: This document is produced by ACI based on information available at the time of publishing. All opinions, conclusions or recommendations are reasonably held or made as at the time of its compilation, but no warranty is made as to accuracy, reliability or completeness. Neither HIA nor any of its subsidiaries accept liability to any person for loss or damage arising from the use of this report.