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Melbourne's High Rise Apartment Boom

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Executive Summary

There has been an unprecedented surge in high-rise apartment completions in Melbourne since the late 2000s – far more than in Sydney, which was once the epicentre of such development. They are located primarily in the inner city, particularly the City of Melbourne (COM) and suburbs on the fringe of the COM.

The apartment surge is just beginning. The inner-city skyline was transformed in the three years 2010-2012 when 22,605 apartments were completed. This transformation will accelerate in the next few years when around 39,000 additional apartments are likely to be completed (Table 2). These are all apartments which have been released for sale (that is, part of developments where off-the-plan marketing has begun) or where construction has commenced.

The apartment boom is driving Melbourne's extraordinary share of Australia's dwelling approvals. In 2012-13 they constituted 24.3 per cent of the Australian total. Yet Melbourne's share of Australia's population in mid-2012 was 18.5 per cent.

Does this mean that households in Melbourne are embracing inner-city apartment living? Our analysis indicates that it does not. Rather, it is an investor rather than an occupier driven boom. Investors are responding to financial incentives, including those deriving from negative gearing.

Apartment residents remain overwhelmingly young singles or couples who are renters. As in the past, they are transients who will move into family-friendly housing when they decide to raise a family. Most of the growth in new households in Melbourne will be looking for such housing (pp. 23-24). There is no large potential source of apartment occupiers (including empty nesters) come near to filling the expansion in the apartment stock expected.

Melbourne is not like Sydney, where restrictions on outer suburban expansion have compelled 11 per cent of households (including some families with children) to occupy apartments (p. 23). In Melbourne, there are huge tracts of outer suburban land zoned for the development. Detached houses can be bought for far less than two bedroom apartments in the inner city. By 2011, only 4 per cent of households in Melbourne lived in apartments of four stories or more.

In the case of the COM, there has been an increase in the number of those who live and work there. Nevertheless, by 2011, they comprised just 27,912 of the 344,790 persons who worked in the COM (Table 7). Overseas students have also been an important source of apartment occupiers. In addition, to our surprise, there has been an increase in the number of those who live in the COM and work outside it. They increased by 5,246 between 2006 and 2011 to 19,108.

There will have to be massive increases in the numbers in each of these categories if they are to approximate the expected surge in apartments on the market.

Local apartment developers, who dominate the inner suburb apartment market are backing off on new proposals. Overseas developers are undeterred. They have the resources to outbid locals for sites in the inner city and are likely to approach 100 per cent of completed apartments in this area by 2016 (Chart 1). They are responsible for the recent surge in proposals for CBD apartment towers.

Melbourne is a more attractive to developers than Sydney because there are more potential sites for high-rise apartment projects which can be developed at prices affordable to most investors (less than \$500,000). These pricing priorities are also responsible for the increasing share of apartment projects comprising tiny apartments (mostly sub 50 square metres in net living area).

Inner Melbourne has also attracted because of its amenities. These have been enhanced by massive State Government and COM investment in infrastructure (including CityLink and Southern Cross Station) public spaces (Federation Square), parks (Birrarung Marr) and laneways.

This investment was intended to enhance Melbourne's prospects of becoming a centre of knowledge-intensive industries by enhancing the city's liveability. It was hoped that this would attract the 'creative class' believed to drive this transformation (pp. 10-11). For its part, the COM has long wanted to transform the CBD and surrounds into an inviting mix for residence, work and entertainment.

This investment has helped in the fashioning of a 'Melbourne Story', which has been particularly attractive to Asian developers and investors.

However the apartment boom is squandering this investment. It is delivering tiny, poor quality apartments that will repel rather than attract the 'creative class'. The COM planners have recently issued a withering critique of the outcome (pp. 29-30). The chief advocate of the COM's original vision, Rob Adams, has declared that the current 'flood' of apartments has gone too far (p. 7).

Despite warnings of an apartment glut the State Government and the COM are pressing on with plans to facilitate further urban renewal. They include Fishermans Bend and the City North and Arden-Macauley precincts of the COM to the north of the CBD. The COM's planning blueprint assumes that the number of dwellings in the COM will increase from 67,533 in 2012 to 110,533 in 2031 (p. 29).

The State Government wants the apartment boom to continue because it is one of the few bright lights of the current Melbourne economy. It can ignore the COM planners' concerns because it holds the planning authority for apartment towers in excess of 25,000 square metres floor space. It is approving almost all proposals put to it.

The outlook is that the investment in the city's amenities will be squandered. The city is heading towards becoming a dormitory rather than a centre for knowledge-intensive industries. The balance between apartments and offices in the CBD is swinging rapidly towards the former with the prospect that apartments will crowd out sites for offices in prime CBD locations.

In the three years 2013 to 2015 there will be three times the amount of floor space completed for apartments in the CBD and Docklands for new office space (p. 29).

The planning elites shaping Melbourne's future are ignoring the disconnection between the investor driven apartment boom and real housing preferences. Their plans for the inner city's expansion and for its economy are based on a property boom that our analysis indicates will implode.

Melbourne's High Rise Apartment Boom

The Issues

Melbourneⁱ is experiencing an extraordinary surge in high-rise apartment construction. It has focussed on inner Melbourne including the Local Government Area (LGA) of the City of Melbourne (COM) and suburbs on the fringe of the COM.ⁱⁱ Over the last few years this spread has widened into more of these suburbs.

However, as is detailed below, the tide is turning back to the COM and particularly the CBD, now that overseas developers have become the dominant source of new high rise apartment proposals. This is why, apart from limits on our research time, we focus on developments in the COM, where the apartment boom appears to conflict State Government and COM aspirations to make the city a globally competitive centre of knowledge-intensive industries.

The apartment boom is driving Melbourne's extraordinary share of Australia's dwelling approvals. In 2012-13 they constituted 24.3 per cent of the Australian total. Yet Melbourne's share of Australia's population in mid-2012 was 18.5 per cent. A central questions is whether this means that households in Melbourne are embracing inner-city apartment living? Alternatively, is it an investor rather than an occupier driven boom?

It is not surprising that the housing construction industry is strong in Melbourne¹, given the city's rapid population growth. Melbourne grew by 650,000 over the decade to mid-2011. It is estimated that a further 79,008 was added over the year to mid-2012. The surprise is that so much of Melbourne's dwelling construction is currently in the form of high-rise apartments.

Melbourne is renowned (for better or worse) for its low-density spread. To counter this, successive Victorian Governments have for years encouraged urban consolidation in the hope of making Melbourne a more compact city. The *Melbourne 2030* planning scheme, legislated in 2002, aspired to locate most of Melbourne's population growth in the form of medium-density development in activity centres located around transport hubs across the city. *Melbourne 2030* also included an Urban Growth Boundary (UGB) which was designed to put a limit on the city's spread.

It has not worked out this way. The activity centre aspiration has failed. Most of the higher-density development is occurring in inner Melbourne in the form of high-rise apartment blocks. Nor has the Victorian government succeeded in curbing the city's spread. Such has been the scale of population growth in Melbourne that, notwithstanding the inner-city flat boom, successive governments have had to massively extend the UGB in order to accommodate those unable to find affordable housing within established suburbia.

The outcome has been an unanticipated surge in inner-city apartments and continued sprawl or perhaps the worst of both worlds. The inner-city surge, which is the focus of this report, is certain to accelerate over the next few years. If you think the inner-city skyline is already cluttered with high rise apartment blocks, you have not, as they say, 'seen anything yet'.

ⁱ Throughout the paper, 'Melbourne' refers to Metropolitan Melbourne as currently defined by the ABS, whereas, COM refers to the municipality, or Local Government Area of Melbourne.

ⁱⁱ The COM LGA includes the CBD, Docklands, Southbank, Carlton, Parkville, North Melbourne, Kensington, Port Melbourne, East Melbourne and South Yarra west.

This study explores two key questions. The first is what is driving the high-rise boom. The second is its social and economic consequences. The first issue explores the role of developers, investors and the ultimate occupiers of apartments in order to understand the boom's impetus. Is it a reflection of the changing demographic make-up of Melbourne's population and of preferences for apartment living, as many commentators argue? Alternatively, is it a product of developer and investor decisions which reflect financial imperatives largely unrelated to the ultimate consumers? Our analysis suggests the latter alternative.

What will be the social and economic consequences of this boom? In one sense it is a success story. From the current Liberal/National Party Government's point of view, the continuing apartment investment boom is one of the few remaining bright lights in Melbourne's economy. The boom has also delivered on the COM and successive State governments' aspirations since the early 1990s to increase the residential presence in inner Melbourne. There has been massive investment in inner-city amenities towards this end.

Successive State governments have contributed to this investment in large part because they believed that this would give Melbourne a competitive edge in generating a more knowledge-intensive economy. The theory was that the 'creative class' needed to drive this outcome would be attracted to live and work in Melbourne.

By 2005, the international architect Jan Gehl pronounced that Melbourne was a success story:

Melbourne in 2005 is a lively, liveable and vibrant city... Important changes have altered the nature of the central city and its daily life from almost exclusively a place of work, to a place of work, recreation and residence in almost equal measure.²

This balance is being lost. Since the time of Gehl's assessment, the apartment building process has gone into overdrive. Voices are now being heard that the boom is degrading the city's liveability. These include Rob Adams, the well-known Director of City Design with the COM, who has been a leading advocate of the COMs transformation. In August 2013, Adams questioned whether Melbourne's 'flood' of apartment development was going too far.³ If Adams is correct, the situation will get much worse as the apartment projects in the pipeline are completed.

How is it that the COM has allowed this outcome? Why is it that the COM has waited until the horse has bolted before raising its voice in protest? The answer lies in the limited powers of the COM and other inner-city municipalities to determine the size and form of the apartment projects proposed within their jurisdiction. For the State government, which dominates these decisions, the priority is to keep the investment boom going.

If the city's liveability is deteriorating, this raises a profound question. At one level the public investment in Melbourne is paying off. It has attracted huge investment in apartment projects, particularly from Asia. But, is this a good outcome from the point of view of Melbourne's long-term economic sustainability?

Since the global financial crisis (GFC), there has been widespread agreement amongst economists that societies which base their economy around residential development and consumption are not sustainable. Instead the advice is that metropolitan centres in developed societies should focus on cultivating internationally-competitive knowledge-intensive industries.

The policy makers in Victoria since the 1990s have endorsed this advice. So far, however, all that has been achieved in inner Melbourne is an apartment investment boom. One of Melbourne’s attractions to foreign developers and investors is the city’s enhanced amenity. In this sense, the public investment in Melbourne’s amenities has been a success. But there are multiple potential downsides which we explore below. These include the prospect that the apartment will crowd out alternative office uses of the available sites as well as diminishing the city’s liveability.

The surge in apartment numbers

Table 1 shows that, since 2008-09, the number of approvals for other dwellings (most of which were for apartments) has doubled while that for houses has declined. By 2011-12, there were more building approvals for other dwellings than there were for houses. Even more arresting, given the strength of fringe housing development during the 2000s, since 2010 housing construction in fringe estates has dropped to a third of the level it reached in 2010.

Year	Houses	Other	Total
2008-09	21,441	10,440	31,881
2009-10	26,080	16,400	42,480
2010-11	24,211	23,924	48,135
2011-12	20,099	19,772	39,871
2012-13	18,210	20,130	38,340

Source: ABS, *Building Approvals, Australia*, July 2013

The recent growth in approvals for other dwellings is consistent with the *Melbourne 2030* planning scheme legislated in 2002. It established development rights in the vicinity of some 120 activity centres across Melbourne. The goal was to locate 255,000 extra households in these activity centres by 2030.⁴ Though no definition of medium-density was given, the accompanying visual representation of what the State Government had in mind was apartment buildings of around five stories.⁵

This is not how it has turned out. The bulk of new apartments approved in recent years have been located in high-rise towers in inner Melbourne. Around 40 per cent of the apartments under construction in Melbourne as of June 2013 were located within the COM. Most of the rest are being built on the fringe of the COM, notably in the suburbs of Abbotsford, Prahran, Richmond and Collingwood.

Melbourne has by-passed the medium-density phase (if there is one) into a high-density pattern. *Melbourne 2030* did aspire to locate another 80,000 households in Designated Centres in inner Melbourne (in the COM, Port Phillip, Stonnington (part) and Yarra). The expectation was that these households would be accommodated in new high-rise developments. As Table 3 below shows for the COM, this has happened. Most of the new dwellings built since 2006 were apartments in buildings of ten stories or more. Henceforth, where the term high rise is used it refers to buildings of this scale.

The results are obvious from the transformation of the inner-city skyline. But, this is just the beginning. The number of apartments under construction is set to accelerate. This is a consequence of the huge increase in the number of off-the-plan sales, particularly in 2010 and to a lesser extent in 2011 and 2012 (see Table 2 below). These sales provide an assured pipeline of commencements and completions into 2013 and 2014. This is because the time between gaining a building approval and the completion of the marketing and construction phase for major projects is normally two to four years.

If the current Liberal/National Victorian State Government has its way, this inner Melbourne apartment boom will continue for years. The Government is overriding objections (where they occur) from the COM and the other local governments for new major apartment projects. In addition, the State Government is pressing ahead with the development of the 240 hectare Fisherman's Bend site adjoining Southbank and the COM is in the process rezoning for urban renewal, the e City North precinct between the CBD and Melbourne University, the E-Gate precinct in North Melbourne and the Arden-Macaulay area adjoining this precinct to the north-west. According to the recent Discussion Paper from the Ministerial Advisory Committee for the Metropolitan Planning Strategy for Melbourne, these precincts could provide for an additional 119,500 residents, almost exclusively in the form of apartments.⁶

The absorption of apartments in the pipeline, let alone the further growth anticipated by the Government, will require a major change in preferences for apartment living on the part of Melbourne households. There are some groups, including international students, who, as we discuss below, do have a high propensity to rent inner-city apartments. But, such is the scale of the projected completion of apartments that a much wider cross section of Melbourne households will need to be attracted. Whether this is likely is a central issue for this inquiry. As we will see, most of the buyers were investors. Their decision to purchase an apartment, or apartments, has reflected the advice they received about the investment outlook (including tax advantages) for apartments at the time they were considering buying. It remains to be seen whether this advice was well informed.

The 'Melbourne story' and the apartment boom

What was the 'story' that convinced investors to buy? Why high-rise and not medium-density? Why in Melbourne and not elsewhere in Australia? Given the massive publicity about the implosion of housing prices in the United States, Spain, Ireland and the UK at the time of the global financial crisis, what sustained investors' confidence about the property market here?

Investors were reassured by property experts, including those employed by the big banks, that Australia was different.⁷ For the most part, these experts disagreed with or ignored commentary such as from the *Economist* and by Australian bears, including Professors Keen and Garnaut,⁸ that Australian city dwelling prices were grossly overvalued. Keen and Garnaut argued (separately) that, as in the United States and elsewhere, a bust in the Australian housing market was imminent. They could point to the huge increase in household debt that had stoked Australia's housing price boom during the 2000s. By the mid-2000s, the aggregate debt of Australian households was equivalent to 150 per cent of annual household income (up from around 100 per cent in the year 2000), most of which was attributable to mortgage debt. It was still at the 150 per cent level in 2013.⁹ This is well above the point reached in the U.S. prior to the global financial crisis.¹⁰

As it turned out, the bears were wrong. The escalation of house and apartment prices in Australian metropolises barely slowed in the aftermath of the global financial crisis. There was a brief plateauing of prices in 2008 and 2009 before they took off again in 2010. Furthermore, from the point of view of potential investors, the closer the property was to the centre of the city (in both Melbourne and Sydney), the more rapid the price escalation. It was not until 2011 that there was a slight pull back in prices.

The bankers' confidence that all is well in Australia has been based on the rapid growth in real household income during the 2000s in Australia. Because of this growth, it has been repeatedly stated that Australian households can afford to spend more on mortgage payments and thus take on the greater mortgage debt needed to finance a dwelling.¹¹ In addition, almost all bank and property experts commenting during the 2000s thought that dwelling prices would continue to rise because they anticipated strong population growth (fuelled by immigration) in metropolitan locations. This was expected to intensify competition for housing, especially in areas close to high-amenity locations. In other words, population growth would offer another source of insurance against any downturn.

But, why the sudden new direction for Melbourne's property market towards high-rise apartments? As documented below, this reflects the financial factors shaping developer decisions as to what and where to build. For their part, investors obviously believed that occupier demand for rental apartments would be strong. They could draw on the widely stated assertions of the urban planning fraternity that the loss of amenity in suburbia due to congestion and the ever more distant spread of the suburban frontier would underpin a shift in preference for inner-city living.

The planners have also made much of the impending ageing of Melbourne's population and thus of an assured increase in the number of one or two person empty-nester households. It was often argued that these households would provide a potential market for apartments. Consistent with this perspective, the COM planners state that the trend towards construction of small apartments in the COM, 'is broadly in line with projected housing demand which indicates growth in lone person and couples without dependents households'.¹²

However, probably the most crucial factor in the appeal of high-rise apartments in Melbourne has been their promotion to investors, especially those from Asia, through the propagation of a 'Melbourne story'. As independent property consultant Sam Nathan (from the property advisory firm Charter. Keck Cramer - CKC) argues:

Melbourne's rising prosperity through the 2000s served as a magnet for investment attraction. Stronger than forecast population growth; escalating housing prices; eroding lifestyle affordability; historically tight vacancy rates and associated rental growth; nation-leading international education opportunities and the benefit of a 'user friendly' city layout gave rise to a compelling story for residential investment.¹³

This story has drawn sustenance from the long-standing campaign on the part of Victorian political elites to promote Melbourne as an appealing international destination for mobile business innovation elites and as a knowledge industry centre. Successive Victorian governments have invested heavily in attempting to bring it to fruition. Beginning in the mid-1990s, when Jeff Kennett was premier, then from 1999 when Steve Bracks, followed by John Brumby led Labor Governments,

all have sought to make Melbourne 'the place to be' by promoting glamorous events, like the Grand Prix and exciting places to visit, including the Melbourne Casino. They have also invested massively in the inner city's infrastructure (Southern Cross Station, CityLink, Docklands and Southbank) and civic amenities (Federation Square, Birrarung Marr, Melbourne Park and the MCG).

As Brumby put it in 2005, 'The challenge now is to make Melbourne not just Australia's creative capital, but to establish and brand Melbourne internationally as one of the world's leading creative centres and a magnet city for new ideas and smart people'.¹⁴ This is an idea made popular by U.S academic Richard Florida, whose 2004 book *The Rise of the Creative Class*, argues that the presence of creative people is the key to whether urban areas or regions become leaders in knowledge intensive industries.

Florida was brought to Australia in 2005 to help promote Docklands. He wrote at the time that:

I wouldn't be at all surprised to see Melbourne emerge as one of the defining global creative centres of the 21st century - and that transformation will be made possible in large part by the creative spirit that the Docklands reconstruction both embodies and enables.¹⁵

Though Florida's theories have come under heavy criticism,¹⁶ there is no doubt that the investment influenced by his ideas has enhanced the COM's amenities. The COM has contributed too, through its efforts to make the CBD a more attractive residential location (as by its encouragement of laneway development and civilised drinking locations).

Ostensibly, inner Melbourne is developing in accordance with these expectations. During the intercensal period 2006-2011, 46 per cent, or 58,953 of all the net growth in jobs recorded for Melbourne during these years, occurred within the COM (see Table 7). Most of the employment in question was in the relatively high-paid, professional and financial service industries. By contrast, just 18.5 per cent of the net growth in employment in Melbourne between 2001 and 2006 occurred in the COM. It is widely expected that this pattern will continue. For example, according to the Secretary of the Department of Premier and Cabinet in the Victorian Public Service, Andrew Tongue:

We think over the next 20 years based on the figures in front of us, there could be 200,000 more jobs in and around the CBD.¹⁷

This will be quite an addition since, as of 2011, there were 344,790 jobs located within the COM (see Table 7).

At the same time, the residential population of the COM has greatly increased. According to the latest Australian Bureau of Statistics Estimated Residential Population (ERP) statistics, the COM grew by 20,086 between 2006 and 2011 to reach 100,240 in 2011. Around 3,000 of this growth was in the CBD and 5,000 in Southbank/Docklands. This implies that some of these knowledge professionals (as well as other categories like overseas students to be explored below) are being attracted to live and work in the COM (estimates of their numbers are detailed below – Table 7).

Given this setting, developers have found fertile territory in which to market their apartment product. Melbourne is portrayed in this marketing as a new global city analogous to Manhattan or Toronto. Though verging on the ridiculous at times, as when explicit comparisons are made with Manhattan¹⁸, it seems that this portrayal appeals, especially to Asian investors. Claims about the

city's global status have been enhanced by the city's ranking in the liveability stakes. According to the August 2012 Economist Intelligence Unit's *Global Liveability Report*, Melbourne is the 'most liveable city' in the world.

We begin the analysis of the apartment industry by first assessing the financial imperatives that drive investment in new apartment projects. We then explore the motives of those purchasing apartments. It turns out that these motives are distant from prospective consumers of the apartment product. This analysis then sets the scene for an exploration of the consumer market. Is it large enough to absorb the flood of apartments that will be completed over the next few years?

The apartment industry

For this inquiry we switch from a focus on building approvals to other measures of the development process. Building approvals data are a poor indicator of the number and timing of apartments being sold off-the-plan, under construction or completed. This is because a building approval does not necessarily signal a building commencement. The purchaser of a potential high-rise apartment site may have in mind enhancing the value of the site for trading purposes. Building on the site may or may not proceed. If it does, it is likely to take several years before the project is completed. There are multiple hurdles for the developer to overcome. They include obtaining financing which, if Australian banks are the source, usually requires the developer to sell 70-80 per cent of the proposed apartments off-the-plan before construction begins.

Table 2 provides a record of actual and forecast completions for apartments throughout Melbourne as of July 2013. It was compiled by the research branch of CKC. It includes all apartments in projects involving more than ten dwellings.

The firm tracks each project from when it gained planning approval to final completion. The sequence starts with planning approval after which the issuance of a building approval is usually a formality. It then proceeds to the release phase, at which time the project is put on to the market normally via opportunities for buyers to purchase off-the-plan. All the apartments tracked in Table 2 have reached the release stage. Commencement usually begins one to three years after release, depending on the scale of the project.

Table 2 provides CKC's estimates of the actual number of releases, commencements and completions to 2012 and forecasts for commencements in Melbourne in the first six months of 2013 and for completions through to 2015. The table documents the magnitude of the surge in apartment completion in recent years (from 3,990 in 2009 to 9,940 in 2012). It also highlights the long gestation of these projects. As noted earlier, 2010 was a truly spectacular year for releases, when projects involving 17,875 apartments were put on to the market. Commencements deriving from these releases lag well behind and by 2012 are still to fully reflect the impact of the surge in 2010.

Calendar Year	Releases (Active + Withdrawn)	Commencements	Completions**
2008	7,030	3,375	4,750
2009	7,970	6,810	3,990
2010	17,875	9,340	5,035
2011	14,510	10,975	7,630
2012	11,810	12,525	9,940
2013f*	7,350*	6,595*	11,345**
2014f	-	-	16,065
2015f	-	-	11,745
* year to end of June for Releases and Commencements			
** full-year forecasts for Completions			

On this estimate, 39,155 apartments will be added to the stock in Melbourne in the three years 2013 to 2015. This is way above the 22,605 completed in the years 2010 to 2012. One indication of the enormous scale of the forecast increase is that, as of 2011, there were only 51,193 occupied apartments in buildings of four stories or more in Melbourne.¹⁹

It is possible that some of the projects recorded as releases may not go ahead. However, according to CKC, only a very small percentage of apartments released since 2008 have been withdrawn. Once a project goes on to the market, it usually eventually goes ahead, even if delays occur.

It is important to note that the completion column does not include all the projects for which recent planning approval has been granted. As our subsequent analysis indicates, the current State Government has been enthusiastically approving new projects. Some of these were released during 2013 and are included in Table 2 in the release column. But, many more are likely to be released to the off-the-plan market over the next year or so. They will add to the completions forecast in Table 2 for 2015 and of course, in subsequent years.

Who is buying apartments?

According to CKC, up to 85-90 per cent of the apartments released in the COM since 2009, have been sold to investors and around 75-80 per cent of releases outside the COM. There has been no lack of investors potentially interested in buying property. As is well known, Australians have a love affair with property investment, partly because of the tax advantages of such investment (notably negative gearing). The Australian tax statistics for 2008-09 indicated that there were 320,625 Victorians with investment properties, almost all of whom reported tax deductible losses on their investment. According to the Household, Income and Labour Dynamics in Australia Survey (HILDA), nearly 20 per cent of individuals in Australia aged 45-64 received income from a rental property.²⁰

This army of investors expect that tax concessions will help finance their losses by way of negative gearing. Recently, this market has been turbocharged by investors adding property to their Self-Managed Superannuation Funds (SMSF). The rules on such investments were changed in 2007 so that people investing in SMSFs can now borrow funds to finance their property investment. In doing so, they can also access the tax advantages gained from investment property for their SMSF, including negative gearing.

But why the surge in investor interest in 2010 and why so pronounced in Melbourne? The answer appears to be that, in the aftermath of the GFC, investor sentiment turned towards residential property as a defensive strategy. Melbourne became a focus because developers could supply apartments in the price range investors were looking for relative to Sydney (more on this below) and because Melbourne had the story (described earlier) which, as Sam Nathan puts it, ‘paved a “golden path” to Melbourne’s door.’²¹

Most of the investors, whether located in Australia or overseas, are buying through financial intermediaries.²² Unlike owner occupiers, who would be strongly motivated to assess their purchase from a future resident’s perspective, these investors are primarily concerned about the financial consequences of their purchase. They want assurances from the financial intermediary that their investment will provide a good financial return. The intermediary (who will be receiving a sizeable commission from the developer) has a strong interest in providing this reassurance.

Investors also want a product they can afford. Most investors prefer to invest in small apartments priced below \$500,000 because of the limited funds they have to invest. This is a major factor in the relative vigour of the apartment market in Melbourne compared with Sydney. There have been far fewer sites in the inner part of Sydney where it is possible to produce apartments within the budget of most investors.

As to what sort of apartments are being built, developers are under pressure to produce small apartments. Particularly in the case of local developers, in order to gain the required bank financing for a high-rise apartment project, the developer must satisfy the bank that the proposal is financially viable. To this end, it is usually necessary for the developer to maximise the yield in apartment sales from the site. This is best achieved by producing small apartments (the smaller the size the more that can be packed into the site, and for reasons noted above, the easier it is to sell the product).

From the developer’s perspective, the ultimate appeal of the apartments they are producing to renters or owner occupiers is a secondary concern. Their profits depend on off-the-plan sales to investors. If there is any subsequent incompatibility between the product and the preferences of renters, it is the investor who will have to bear the risk. The only qualification is that if, at the time of settlement for off-the-plan sales, the investor gets cold feet, the developer may have trouble enforcing the original contract.

The Australian development industry differs in this regard from that in the United States. There, developers often also play a role as subsequent landlords and managers of the projects they construct. They therefore have a more acute interest in ensuring that the product they are selling does meet ultimate user needs.

The outcome, at least for the apartments sold off-the-plan in the late 2000s when Australian developers were the dominant players in the apartment market, was that most of the apartments in question were located in high-rise towers. Almost all of these apartments were small - less than 70 square metres in size, with an increasing share of tiny one bedroom or bed-sitter apartments. Most were located in inner Melbourne, particularly in the COM. There has also been a spread to areas adjoining the COM, but much less so to middle suburban areas like Boroondara (more on this below). It has proved to be difficult to obtain approval for apartment projects in these middle suburbs, relative to inner Melbourne.

Data from the COM for the dwelling stock within its jurisdiction (Table 3) confirms that most of the new dwellings within the COM were part of apartment blocks of five stories or more. The most rapid rate of growth was for apartments in towers of thirty stories or more.

Table 3 Dwellings by height of building in the City of Melbourne, 2006-2012

Dwellings by floors above ground#	2006	2012	Increase	Share of increase
Less than 5	21,597	24,270	2,673	19.8
5 to 10	5,702	8,566	2,864	21.2
10 to 20	9,373	12,115	2,742	20.3
20 to 30	7,989	9,496	1,507	11.1
30 or more	5,304	9,048	3,744	27.7
Total	49,965	63,495	13,530	100.0

Source: City of Melbourne, *Dwelling Stock and Diversity in the City of Melbourne*, Sept 2012, Figure 4

The source publication does not explain the range overlap.

Table 4 is also derived from the COM dwelling stock data. It covers private dwellings (excluding student, government and serviced apartment projects). The table shows that two bedroom apartments still dominated the dwelling stock in the COM by 2012, but that 39.5 per cent of the increase in the stock of dwellings between 2006 and 2012 was in one bedroom apartments. Table 4 also confirms that very few three bedroom apartments are being added to the stock.

Table 4 Private dwellings by number of bedrooms in the City of Melbourne, 2006 and 2012

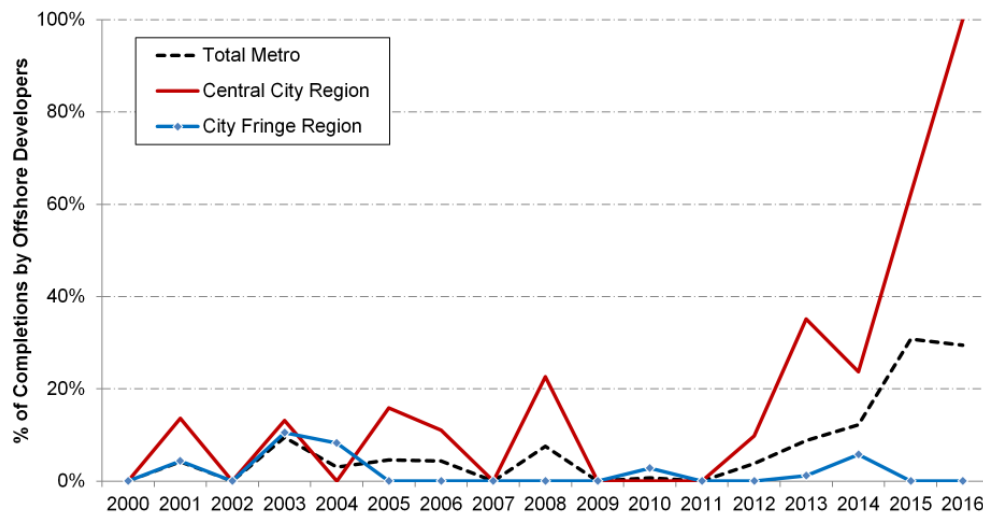
	2006	2012	Increase	Share of increase
One bedroom	9,225	13,307	4,082	39.5
Two bedrooms	20,268	25,145	4,877	47.2
Three or more bedrooms	8,365	9,728	1,363	13.2
Total	37,858	48,180	10,322	100.0

Source: City of Melbourne, *Dwelling Stock and Diversity in the City of Melbourne*, Sept 2012, Figure 4

The new world of Asian property development

The apartment development scene has changed since the late 2000s. Asian developers are now major players in the COM development industry as are Asian investors in the apartments produced. As is shown in Chart 1, CKC estimates that offshore developers the share of apartment completions in the Central City Region (defined by CKC to include the CBD, Docklands, Southbank and St Kilda Road) will approach 100 per cent.

Chart 1 Share of apartment completions in Melbourne by offshore developers, 2000 to 2016



Source: CKC, Melbourne's Residential Apartment Briefing, March 2013, unpublished

By 2015, the recent acceleration in releases from offshore developers in the Central City Region will mean that most newly completed apartments in Melbourne will be located in this region. By this time, CKC expects that the boom in City Fringe apartment completions will have slowed.

The financial setting they operate in is different from that of local developers. Some of those attracted to the CBD market are amongst the biggest property developers in Asia. They have access to offshore funds at much cheaper rates than are available to local developers from Australian banks. Their financial muscle means that they are under less financial constraints than local developers. As a result they are in a better position to compete for inner-city development sites against local developers. They also do not appear to have to pre-sell the majority of the apartments before finance is secured.

They are expanding at the expense of local developers within the inner city. As Melbourne developer Albert Dadon put it recently, Asian developers have an unfair advantage. According to Mr Dadon, offshore funding was not subject to the same checks and balances that Australian banks demanded. 'The process is totally opaque and all happens overseas'.²³

It follows that overseas developers are subject to fewer constraints when it comes to considering the ultimate occupants of the apartments they are building than are local developers. They have a ready market in absentee Asian investors. The latter apparently like inner-city Melbourne because apartments can be built within easy access of all Melbourne's central amenities. The 'Melbourne story' also appeals to both developers and investors. For these developers and investors, their motives for investing in Melbourne may also include a long-term strategy of spreading their investments to diverse and secure locations.

In the case of investors from mainland China, another concern is to place their money in a safe overseas destination. In addition, recent curbs on property speculation in China have forced investors to look internationally for investment opportunities.²⁴

Intimations that the apartment market is in danger of oversupply seems to have had a limited deterrent effect on developers capable of putting together major projects, in part because all rely heavily on selling to Asian investors. A case in point is Platinum, which is to be located at Southbank and will include 435 apartments. This is intended for completion in 2016. The Developer, Salvo Property Group, (in this case, a local developer) claims that it is already half sold after extensive marketing in Asia.²⁵ When asked about headlines suggesting an oversupply of Melbourne apartments, the developer responded that with half the apartments sold 'Why should I feel there is oversupply?' 'I don't see the gloom.' In his opinion, the demand for inner-city apartment living made sense in this day and age.²⁶

Local developers and the spread of high-rise apartment buildings outside the COM

The rise of the Asian developer has prompted the local developers who have been forced out of the inner-city market to move into the suburbs edging inner Melbourne. The apartment boom has attracted both established and new opportunistic local developers. As a consequence of the development rights created by *Melbourne 2030* when it was legislated in 2002, the range of potential sites for medium and high-rise development proliferated. Though, as noted, it has been a battle to win planning approval, many new projects are being located in more financially risky inner and middle-suburban locations. The risk arises where the cost of putting such apartments on the market is likely to be little below that of surrounding detached houses, thus putting a lid on the apartment price point.

According to CKC, the completion of apartments outside the inner city will peak in 2014. These will comprise a greater proportion of medium-density projects than are forecast for completion in the inner city. However, almost all of these apartments will be small (70 square metres or less). It is not possible to put family-friendly apartments (of 90 square metres or more) on to the market in established suburban areas for less than \$700,000.

The high price of these apartments partly reflects site costs (elevated because of the escalation of detached house prices in inner-suburban Melbourne). It also reflects the high construction costs for apartment blocks over three stories in height due to the need for lifts, underground car parks and other construction requirements, and because union labour must be employed on such projects.²⁷ Apartments priced above \$700,000 are well beyond the means of most new home buyers and also outside the price range preferred by most investors.

The result is that the enormous increase in apartments expected to be completed, whether in the Central City Region or City Fringe suburbs, will be predominantly small – suitable only for singles and couples without children. In thinking about the market for these apartments, we begin by exploring the evidence on the characteristics of the recent occupants.

Who is occupying the increased stock of apartments?

We can quickly dispense with the notion that baby boomers are taking up apartment living when they become empty nesters and are beginning to think about retirement. Baby boomers (born 1950 -1965) are the main source of the projected growth in the number of one and two person households in Melbourne.²⁸ However, there is no evidence of any significant downshifting to apartment living on the part of this cohort. Survey after survey shows that most baby boomers

prefer to 'age in place'. It is most unlikely that persons facing their retirement years would want to give up the relative peace of a house and garden setting for a high-rise location. This is confirmed by the data in Table 5. They show the type of housing occupied by persons aged 55 to 74 in Melbourne in 2006 and 2011. Around 80 per cent live in detached houses. There has been no decline in this share between 2006 and 2011. The proportion living in flats of four stories or more was tiny in 2006 and remained so in 2011. (The Census data does not provide any data on apartments by number of stories within the four plus category).

Table 5 Baby-boomers by housing preference, Melbourne, 2006 and 2011

Age	Separate detached dwelling		Semi-detached dwelling		Flat 2-3 storeys		Flat 4 plus storeys	
	2006	2011	2006	2011	2006	2011	2006	2011
55-59	80.9	80.9	8.4	8.6	6.4	6.0	1.7	1.9
60-64	80.5	80.0	8.5	9.1	6.7	6.4	1.7	1.9
65-74	78.2	78.5	9.2	9.4	7.9	7.1	1.6	1.8

Sources: ABS, 2006 and 2011 Census data

Young people dominate the ranks of those living in apartments, particularly those who reside in the COM. This is shown in Table 6. Most are also renters. Data drawn from the 2011 census (not shown in the tables) indicate that 68 per cent of the households occupying apartments in blocks of four stories or more in the CBD were renters, as were 61 per cent of those living in such apartments in Southbank and Docklands, and 64 per cent of those living in apartments elsewhere in the COM.

Table 6 Age distribution by head of household living in 4-storey and above apartments, 2011

Area	15-34	35-44	45-54	55 plus	Total (N)
Melbourne - (CBD)	71.4	12.3	7.7	8.6	6,507
Melbourne- Southbank, Docklands	56.1	16.4	11.9	15.4	7,136
Melbourne - COM -remainder	63.6	11.6	7.8	16.9	10,060
Port Phillip - West	37.5	20.4	14.2	27.8	6,050
Stonnington - Prahran	44.5	13.7	8.4	13.4	3,745
Yarra - North	38.4	23.1	14.8	23.5	2,133
Moonee Valley - Essendon	40.0	17.6	14.0	28.3	1,575
Boroondara - Hawthorn	69.5	13.1	7.1	10.2	1,211
Others					12,778
Total	52.4	15.7	10.5	21.2	51,195

Source: ABS, 2011 Census, Tablebuilder data sets

Who are these young renters? The statistics available only allow a broad brush answer. We focus on the COM in order to simplify the calculations. As noted, the population of the COM grew by 20,086 between 2006 and 2011 (to reach 100,240). According to the census counts, the number of occupied dwellings increased by 10,410 over this period. Some 6,701 of this increase in occupied dwellings comprised apartments of 4 stories or more.

The task is to identify the characteristics of the extra 20,086 residents, most of whom, it has been established, were living in apartments.

Given the rapid growth in employment in the COM of 58,953 between 2006 and 2011, it was expected that many of the new COM residents would be drawn from the ranks of this increased stock of workers. The data provided in Table 7 enables an assessment of this issue. It is drawn from journey-to-work data from the 2006 and 2011 Censuses. It shows the number of persons working in the COM by where they lived in 2006 and 2011.

The first point to note is that only a minority of the 344,790 persons employed in the COM by 2011, lived in the COM. Their number was 27,912, or just eight per cent. Likewise, only 7,787 of the 58,953

growth in the number of persons who worked in the COM between 2006 and 2011 lived in the COM in 2011. However, given that some of these 7,787 workers would have been accompanied by partners and dependents who were not employed as of 2011, it is likely that this group added around 10,000, or half of the growth in the COM residential population of 20,086 between 2006 and 2011. Table 7 also shows that the majority of this 7,787 group were employed as professionals or managers. This finding is consistent with the 'Melbourne story'. The COM is home to many firms with a high propensity to take on knowledge workers. Some of these workers both work and live in the COM.

One additional source of residential growth in the COM that surprised us was those who live in the COM but work outside it. Their numbers are shown in Table 8. They increased by 5,246 over the years 2006 and 2011 – not much short of the extra numbers living and working in the COM.

This finding indicates that the COM is serving as a dormitory suburb for an increasing number of persons who work outside the COM. The main work destination of these COM residents was the adjoining LGA of Yarra.

Perhaps part of the attraction of living in the COM is the opportunity to rent an apartment rather than to gain easier access to a job located within the COM. This is a speculative hypothesis since there is no easy way of testing it. Nevertheless, it is plausible. This is because of the high price of detached houses, townhouses and units in inner suburbia. The price of this housing, as noted earlier, exploded during the 2000s. Young knowledge workers employed in inner suburban locations may have had to look to the cheaper apartment living provided in the COM. They may continue to do so as the stock of apartments in the COM expands.

Table 7 Place of usual residence of employed persons who work in the City of Melbourne (COM), by occupation, 2006 and 2011

Place of residence	Managers	Professionals	Technicians and Trades	Community & Personal service	Clerical and Administrative	Sales	Machinery Operators and drivers	Labourers	Inad. Descr./Not stated	Total
2006										
COM	2,940	8,653	1,020	1,793	3,097	1,567	142	640	273	20,125
Elsewhere in Melbourne	38,604	93,212	17,830	16,637	64,972	15,785	4,876	10,429	3,367	265,712
Total Melbourne	41,544	101,865	18,850	18,430	68,069	17,352	5,018	11,069	3,640	285,837
2,011										
COM	4,021	12,555	1,427	2,548	4,085	1,852	129	763	532	27,912
Elsewhere in Melbourne	49,015	120,434	19,665	18,834	70,709	16,921	4,702	10,240	6,358	316,878
Total Melbourne	53,036	132,989	21,092	21,382	74,794	18,773	4,831	11,003	6,890	344,790
Change 2006-2011										
COM	1,081	3,902	407	755	988	285	-13	123	259	7,787
Elsewhere in Melbourne	10,411	27,222	1,835	2,197	5,737	1,136	-174	-189	2,991	51,166
Total Melbourne	11,492	31,124	2,242	2,952	6,725	1,421	-187	-66	3,250	58,953

Source: ABS, TableBuilder 2011 and 2006

Location	2006	2011	Increase 2006-2011
Yarra	2,053	2,911	858
Port Phillip	2,463	2,717	254
Stonnington	979	1,242	263
Other outside COM	8,367	12,238	3,871
Total	13,862	19,108	5,246

Source: ABS TableBuilder, 2006 and 2011

The student market

Another important source of demand for accommodation in the COM's growing apartment stock has been overseas students. According to industry sources, they have been the main occupants of the cheaper small apartment stock within the COM. It is difficult to obtain accurate figures on this issue because census data probably undercount the number of overseas students.²⁹ The COM estimates that there were nearly 18,000 overseas students in the higher-education sector alone who were living in the COM by 2010.³⁰ Some of these would have been living in the substantial stock of dwellings assigned for students within the COM.³¹ Nevertheless, given that in 2010 the COM population was 97,623, the scale of the student presence at the time will be evident.

The period 2004 to 2010 represented the peak years of the overseas student industry. This outcome reflected the ease of gaining a permanent-resident skilled visa after completion of an Australian university or Technical and Further Education (TAFE) trade qualification at the time. Changes to the migration rules since 2010 have largely removed this link for TAFE graduates and attenuated it for university graduates. As a result, the annual number of student visas issued overseas in 2011-12 by comparison with 2008-09 fell by 77 per cent for TAFE students and by nearly 40 per cent for higher education students. The stock of those in Australia on a student visa was just on 300,000 in December 2010. It has since fallen to 242,210 in December 2012.³² The student market will remain significant, if at a lower level than the peak years 2004 to 2010. One factor likely to contribute to its maintenance is that, beginning in 2013, those finishing any university course (though not a TAFE course) will be permitted to stay on in Australia and to work without restriction for at least two years.

Transients and future apartment demand

The three groups discussed (those who live and work in the COM, those who live in the COM and work outside it and overseas students) appear to constitute the bulk of those attracted to occupying apartments – at least in the COM – between 2006 and 2011. They are predominantly renters and young. Most are transients. This is obvious in the case of overseas students. In the case of residents living and working in the COM, and living in the COM but working outside it, if past behaviour is a guide almost all will move to more family-friendly accommodation when they partner and enter the family building phase of their lives. The result is a high turnover rate for those occupying apartments. One consequence is that just 30 per cent of the COM's population in 2011 lived in the COM in 2006. This compares with 80 per cent of the state-wide figure for people who lived in the same LGA in 2011 as they did in 2006.³³

This analysis implies that the main driver likely to produce an increase in the number of COM residents is further growth in the number of those working in the COM or the adjoining inner city

locations. They will be replacing an earlier cohort of transients for whom apartment living no longer suits their needs. It follows that there will have to be a continued strong increase in the number of jobs available in the COM and adjacent suburbs if the stock of transients is to increase.

Whether the COM will continue to experience the boom conditions of the 2000s is questionable. We explore this issue later in the context of the COM's recently published studies of the city's economic future.

Whatever the economic prospects of the COM there remain two other key arguments that advocates for medium and high density living believe will influence preferences for apartments. These are that this market will be sustained by changes in preferences for apartment living and by continued growth in population.

Could preferences change?

It is often asserted that inner-city living has increased in appeal as the city spreads ever further outward and new settlers allegedly face long work commutes and poor services. Urbis, the Melbourne-based planning firm, exemplifies this opinion. In reference to the downturn in housing starts in fringe areas since 2010, Urbis says that the increase in the cost of petrol 'has suddenly led to concerns about car expenses and public transport usage surged in response, reducing the appeal of the suburbs served mainly by auto transport'. These stresses, so Urbis claims, are 'combining with more positive attitudes towards the greater affordability of higher density living, and the amenity benefits of inner urban life'.³⁴

Luci Ellis of the Reserve Bank puts a variant of this argument. She notes that Australian metropolises are notable for a much higher share of low-density housing than is the case for most other major cities in developed countries. In this context, she argues that with continued strong population growth in Australian metropolises, the 'price of our low-density life has become unaffordable for some'.³⁵ This is surely correct for housing in established suburbia because of the increasing competition for such housing and the consequent rise in prices noted above. Ellis goes on to conclude that, as a result, 'the mix of residential construction will be tilted more towards medium-density and high-density dwellings than in past decades'. She regards the recent sharp rise in the share of dwelling approvals for apartments in four storey plus buildings³⁶ as evidence for this argument.

There are two fundamental reasons for doubting this thesis. The first is that there is a more convincing alternative reason for the recent downturn in housing starts on the fringe than a change in attitudes to fringe living. This is the state of the economy.

Economic downturn and the fall in

fringe housing sales

The escalation of house prices in established suburbia has meant that for most new home buyers the only affordable family-friendly option has been new estates on the fringe. This point is documented in the Victorian Government's Discussion Paper on Melbourne's planning options. It notes that the only housing now affordable for families with children with an annual household income below \$90,000 is located in suburbs on the periphery of Melbourne.³⁷

Since fringe housing remains less expensive than established detached housing and population growth in Melbourne is being sustained at record high levels, one might expect a continued strong demand for new house and land packages. Yet, as noted earlier, this has not been the case. The number of housing lots sold in fringe estates has shrunk to a third the level of 2010. As detailed elsewhere, this decline is not due to an inability on the part of developers to supply new blocks of land.³⁸ The stock of unsold blocks by the end of 2012 was several times higher than it was in 2010. Moreover, the recent drop in demand has also occurred in the face of some discounting of block prices and a fall in interest rates.

As noted, one explanation is that outer suburbia is losing its attraction, perhaps because of the remoteness of frontier estates from employment opportunities and backlogs in community services. The remoteness issue is sometimes exaggerated because most of those purchasing new houses on the fringe do not work in the inner city. They work in the middle suburbs. They have had to trade off this commute and the backlogs in service provision against the benefit of the lower costs of buying a detached, family-friendly house on the fringe. This situation is unlikely to change in the near term because most new households will struggle to afford detached housing in established suburbia.

The decline in sales of new house and land packages since 2010 is more plausibly linked to the change in the employment market in Melbourne. Those looking for employment face a job market in which the number of vacancies is declining sharply. The *Australian Government's Vacancy Report* for job vacancies listed on the internet indicates that they fell by 22.7 per cent for Melbourne in the year to March 2013. No data is provided by occupation for Melbourne, but for Victoria as a whole, there was a 20.1 per cent decline in vacancies for professionals over the year to March 2013. The worst affected occupations were technicians and trades workers where the vacancy index fell by 30.4 per cent in the year to March 2013.³⁹

According to the ABS estimates, since the August quarter of 2011, employment in Melbourne has stabilised (after huge growth in the preceding years).⁴⁰ This slowdown has occurred at a time of rapid growth in the labour force (partly driven by migration). This is a worrying time for those looking for work or holding jobs vulnerable to the downturn (including construction workers).

Though fringe housing is cheaper than that in established areas, new home owners still face a minimum price for a 20 square house (around 186 square metres) on a small 450 square meter block of \$400,000. Most would need to obtain a mortgage of at least \$300,000. Many first home buyers were prepared to risk such a debt during the boom years of the 2000s. At this time, the job outlook was strong and there was an expectation that house prices would move ever upwards.

This is no longer the case. As a result, it is not surprising that many households are not prepared to take on such debt. The households who move to fringe suburbia are predominantly drawn from the ranks of blue and lower white collar households. This section of the workforce has been the most severely impacted by the recent weakening of the employment market.

If this interpretation of the fringe downturn is correct, it cannot be taken as an indication of any decline in the attachment to detached housing. For those who think continued rapid population growth in Melbourne will force households to choose apartment living, the existence of ample opportunities for detached housing on the fringe should constitute a warning. Melbourne is not like Sydney. Detached suburban housing is still an option for new households in Melbourne.

The contrast with Sydney is instructive. For the past decade or so, restrictions on the release of suburban land in Sydney have meant that the number of blocks produced during the 2000s was half the level of that in Melbourne. As a result, few blocks have been available for less than \$200,000. The median lot price sold in the March quarter of 2013 in Sydney was \$275,000 compared with \$199,000 in Melbourne.⁴¹ The lack of affordable house and land packages in Sydney is the main reason why a much higher proportion of Sydney households live in units and apartments than in Melbourne. In 2011, apartments of four stories or more comprised 11 per cent of the occupied dwellings in Sydney, compared with four per cent in Melbourne. It also explains why four per cent of couples with children in Sydney live in apartments compared with one per cent in Melbourne.

What are new households looking for?

There is no doubt that many new dwellings will be needed in Melbourne over the next decade. As we have just seen, however, there is no automatic connection between population growth and dwelling demand. As is evident from the experience in Sydney, the high cost of housing and lack of availability of affordable detached housing appears to have led to a slow-down in household formation, one manifestation of which appears to be that the average household size in Sydney by 2011 was larger than in Melbourne.⁴² Nevertheless, population growth is a key driver of the housing market. In order to estimate its impact, one has to examine how this growth manifests in household formation and, in particular, the characteristics of new households. They are the key drivers because, by definition, each new household must occupy a dwelling.

The household formation projections summarised below assume that Melbourne's population will grow by around 550,000 over the decade 2011-21. This number includes a continued strong net in migration gain, mainly from overseas. This is less than the 672,000 figure projected over the same period in the Victorian Government's *Victoria in Future* projections. The difference mainly reflects our lower overseas migration assumptions. They are based on the expectation that job creation in Victoria will slow, thus diminishing the attraction of Melbourne to migrants. The expected slowdown in the numbers of overseas-born persons locating in Melbourne has not (yet) occurred, in part because the Australian Labor Government has maintained record high permanent and temporary migration intakes despite the softening of the Australian labour market.

As a consequence, the projections probably understate the current rate of household formation. There may be more households forming, but the characteristics of the households being formed will be much the same as we have projected. This is because most new migrant households are in the 25-34 age group.

Table 9 summarises the results of these household projections. There will be 266,492 more households in Melbourne by 2021 than in 2011. This implies the need for a net addition of 26,649 dwellings a year over the decade. The calculations assume that household formation rates (the rate at which residents belong to households by type of household by age) will remain the same as in 2011.

Table 9: Estimation of the contribution of household formation and dissolution on the number of households, by age group, Melbourne, 2011 to 2021

	15-24	25-34	35-44	45-54	55-64	65-74	75-84	85 plus	Total
Net change from household formation/dissolution	69,954	242,111	77,578	15,379	-10,633	-10,848	-21,239	-95,811	266,492

Net gain in households 15-54 = 405,022

Net loss in households 55 plus = 138,531

Source: Bob Birrell, et al., *The End of Affordable Housing in Melbourne*, CPUR, 2012, p. 82

The projection indicates that most of the growth in new households resulting from the formation and dissolution of households will be amongst those aged 25-34. As Table 9 shows, there will be a net addition of 242,111 new households in the 25-34 age group between 2011 and 2021. These are new households which did not exist in 2011 and thus will need accommodation in existing or new dwellings. In addition, there will be some 69,954 additional households aged 15-24 and another 77,578 aged 35-44.

Where are these new households going to find accommodation? In a population with a relatively even age distribution, most of this accommodation would come from the dissolution of older households and the vacating of their dwellings. However, the number of households dissolving (as by death or movement into care) is far lower than the number of younger new households. According to the projections in Table 9, only 138,531 households will dissolve over the decade to 2021 in the 55+ age category. However, there will be 405,022 new households aged 15-54 formed by 2021.

In Melbourne, as elsewhere in Australia, the number of baby-boomer households entering the retirement ages of 65-74 will increase sharply over the decade to 2021. But, few of these households will dissolve, and few will be looking for accommodation. This is because they already own a detached house and because, as argued above, few of the baby boomers will be interested in downshifting.

The result is that, if these younger households are to be accommodated, it will have to be via new construction rather than from vacancies caused by households dissolving or downshifting.

Most of the new younger households will want detached housing. It is true that only about half of the 25-34 year old households likely to be formed between 2011 and 2021 will be couples with children by 2021. Apartment or unit living may be acceptable in the initial years of their relationship. However, by far the majority of these households will be raising a family when aged 35-44. If past preferences prevail, they will seek to occupy detached housing and will do so before they begin raising a family. According to the 2011 census, 88 per cent of all couples with children living in Melbourne were occupying detached housing.

Given the current cost of housing, most of the new younger households projected will not be able to afford detached housing in established suburbia, particularly in the inner suburbs. This will mean continued interest in relatively cheap fringe housing. For those who do not want to move to the fringe, the likely preferred option will be a semi-detached townhouse or unit located in the lower priced middle and outer suburbs. This is because it is only in these suburbs that town houses or units will be available for less than \$400,000. There are some households who intend to raise a family who have a strong preference for inner-city living. If they cannot afford a unit or townhouse, they may

have to accept apartment living. If so, it will probably be located in the inner suburbs rather than in the COM, which is distinctly non child-friendly.

Ignoring the warnings

We have arrived at a crucial juncture. If our analysis is correct there is likely to be a glut of high-rise apartments within a few years. This is no secret. According to Robert Mellor, Managing Director of forecaster BIS Shrapnel, the number of apartments being approved in Melbourne is unsustainable, with a bubble looming.⁴³ Warnings signs abound that the market for apartments is already weakening. Among the indicators, when off-the-plan purchasers now seek a bank loan to settle their purchase, they are finding that the banks are valuing their property at below the original purchase price. The financial intermediaries who place apartments with investors are also demanding a greater selling fee (presumably reflecting purchaser caution). Rental levels for COM apartments are also softening. This is well-known, as headlines in the financial press, like 'High rise glut hits returns'⁴⁴ attest.

Yet, developers are pressing ahead with new apartment projects, especially in the Central City Region. The building approval data for the COM is startling in this context. In the June Quarter of 2012, there was a record number of building approvals for the COM of 3,420. As noted earlier, some of these are now showing up as releases, with 2,900 apartments put on to the market in the first half of 2013.

Nor is there any sign that the State and municipal authorities are rethinking their plans. The COM is currently forecasting that the stock of dwellings within its jurisdiction will increase by 64 per cent, from 67,533 dwellings in 2012 to 110,533 in 2031.⁴⁵ Residents are being told that the City is preparing carefully for this outcome. The COM planning officials have prepared a *Future Living Discussion Paper* (released on 13 May 2013), which sets out the standards that should guide the massive redevelopment expected. It has also initiated planning amendments which will facilitate the urban renewal required in the City North and Arden-Macauley precincts if these dwelling targets are to be met.

On 16 September 2013, the State Government released its proposals for the 240 hectare urban renewal project at Fisherman's Bend. The expectation is that some 5,000 apartments will be built in the next 10 years.⁴⁶

Clearly there is a head of steam behind the city's growth expectations. It is not just wishful thinking. The COM has invested in several substantial reports which evaluate the likely outcomes for job creation and residential relocation into the COM. They affirm the Melbourne story and thus the COM's responsibility to facilitate development. We explore these reports carefully, because they constitute the foundation stone of the COM's case that a further surge in apartment completions is needed.

The COM case for massive inner-city growth is unconvincing

The COM commissioned two consulting firms to advise it on the city's economic prospects. The first by ACIL Tasman puts some flesh on the widely disseminated claim that the COM is already a thriving knowledge city. The report is optimistic that the COM is well placed to contribute to the long-standing State Government ambition to make it a focal point of knowledge industries in Victoria. It

states that the COM already has recognized strengths in fields 'such as advanced manufacturing, biotechnology, creative industries (particularly design) event management, financial services' and so on.⁴⁷ It also has key 'World Class' assets including the Walter and Eliza Hall Institute and the University of Melbourne.⁴⁸

ACIL Tasman repeats the Florida thesis discussed earlier in the context of the Victorian Government's original vision for Docklands. It states that:

Melbourne has many of the attributes that Richard Florida (the leading international theorist on what attracts creative people to certain locations) believes the "the creative class" attaches much importance to, such as a vibrant and diverse street life; compact, distinctive and authentic neighbourhoods with a diversity of buildings; a finely meshed street pattern; and pedestrian-friendly public spaces.⁴⁹

The Report provides a good account of the kind of economy so many of Australia's leaders aspire to create, now that the impetus from the mining investment boom is waning. The hope is that the exports of services into Asia will fill the gap. Unfortunately, the Report does not document the COM's achievements so far. There are no case studies of successful start-ups, for example, in biotechnology. It does not acknowledge that the 'World Class' assets, including the Walter and Eliza Hall Institute are mainly academic research institutes almost totally dependent on Commonwealth and State government support. The Institute does indeed have a fine research record, but the revenue it generates from royalties or other commercial offshoots is minimal (just \$2.5 million in 2011).⁵⁰

This is not to knock these aspirations. It is vital for Victoria that new knowledge industries do emerge in the Asian Century. The point is rather that the aspirations expressed in the ACIL Tasman Report and the COM's own claims to be a knowledge city are a flimsy base for the COM's dwelling and population growth projections.

The second report commissioned by the COM was by SGS Economics & Planning (SGS). It is entitled, *Understanding the property and economic drivers of housing* and was released in January 2013. It offers an interpretation of the factors generating the surge in job creation in the city between 2006 and 2011. It argues that these factors will continue to drive job creation in the COM and that many of those attracted to these jobs will be interested in residing in the COM.

The SGS report shows that, over the thirty years 1961 to the early 1990s, there was little growth in employment in the CBD or in the COM. Thereafter, job growth was rapid, except for a slowdown in the early 2000s. As noted earlier, an unprecedented 46 per cent of all job growth in Greater Melbourne occurred in the COM over the years 2006-2011.

The report makes a convincing case that this job surge in the COM since early the 1990s was a consequence of successive Hawke and Keating Government economic reforms. They included the floating of the Australian dollar, the dismantling of restrictions on foreign financial firms operating in Australia and on international financial transactions and tariff reductions which forced Australian-based enterprises to compete in the international marketplace.

The result was a massive increase in trade, information and of commercial interchange with the global economy. SGS argue that Sydney and Melbourne have been the main beneficiaries of this process. They have provided the dominant sites for the international and domestic firms engaged in

this interchange. Also, their size has generated agglomeration effects which SGS puts great store on. These refer to the synergies and efficiencies which emerge when there is a high concentration of professional service firms clustered around the main domestic and international institutions in the service economy (like the big four banks and Telstra). According to SGS, these agglomeration advantages will become more pronounced as Sydney and Melbourne continue to grow.

Though to some degree in Sydney's shadow, Melbourne has done relatively well in recent years because it has provided more space for office expansion (Docklands), much cheaper rents than are available in Sydney and improvements in ease of access to the CBD (CityLink and the Ring Road), again by comparison with Sydney. SGS argue that:

For Melbourne, the ongoing shift in global trade is likely to mean continued growth of the knowledge intensive and Advanced Business Service sector. This is one key area in which Melbourne is internationally competitive... Given Melbourne is a location with high liveability and a highly skilled work force, it is very likely it will continue to be an attractive location for such firms in the long term, provided, of course, the city can maintain the competitive strengths inherent in its urban quality and functionality.⁵¹

Interestingly the SGS report does not play up the 'knowledge city' factor. It merely suggests that, with continued growth in the finance sector and associated professional services, this will attract more professionals and in the process generate demand for a range of supporting services in retail, cafes etc. SGS goes on to say that: 'The amenity that this creates will also attract some firms e.g. creative architecture/ IT/ start-up firms into the surrounding areas.'⁵² The operative word is 'some'.

The SGS report is much thinner on the prospects of the additional workers it believes will work in the COM deciding to reside in the COM. It asserts that the 'shift towards inner city living is likely to continue'.⁵³ It cites international evidence that well paid knowledge workers like to live in 'dense urban environments and large cities, reside in well-established knowledge communities and seek cultural and education opportunities as well as affordable housing'.⁵⁴ But, there is no probing into whether the kind of apartment stock being added to the COM will be attractive to these knowledge workers. Nor does SGS grapple with the recent evidence, cited above, that only a minority of the extra persons employed in the COM were resident there by 2011.

The weak point in the SGS report is that it does not substantiate its argument that the COM is now 'internationally competitive' in the provision of services.

The COM has undoubtedly benefited from its role as a financial mediator between Australia and the rest of the world. But, the main impetus to employment in the COM in recent years has been the provision of financial and professional services within Australia which are linked to Australia's rapid economic and population growth during the 2000s and the increased income of most its residents.

Employment growth in the COM has already diminished, with the peaking of the mineral investment boom and the overall slowdown in the Australian economy. As credit growth has slowed, the big banks and finance enterprises are no longer taking on new staff. Rather, some are looking to augment their profits by aggressive outsourcing and offshoring. As a consequence, the Melbourne office market is softening. According to BIS Shrapnel, Melbourne faces a 'bleak' two year period.⁵⁵

One indicator is that the net absorption of office space in the Melbourne CBD contracted slightly in the year to July 2013.⁵⁶

There is reason to believe that there will be no rapid revival of the housing and consumption boom of the 2000s. As a number of economic commentators have pointed out, during the commodity price boom of the past decade, nearly half of the increase in Australian residents' real income came from the improvement in Australia's terms of trade.⁵⁷ As a consequence residents were able to buy more imported stuff per Australian dollar than before.

This source of real income growth has come to an end with the slump in commodity prices and decline in the value of the Australian dollar. Maybe it is just a short-term phenomenon. Nonetheless, its impact will be significant while it lasts because, if the terms of trade do continue to fall, the impact will be felt as a contraction of real income. The outlook, according to the Australian Treasury, is that Australia's terms of trade will decline steadily over a prolonged period to 2029-30.⁵⁸ If this is the case, one major source for the property boom of the 2000s, according to the Reserve Bank and other authorities quoted earlier, will diminish. This is the increase in real household income which made it possible for households to take on high levels of mortgage debt and the mortgage payments resulting.

If SGS is correct, the situation will be rescued by Melbourne's 'internationally competitive' knowledge-intensive industries. However, the recent record is not encouraging. The education industry has been by far the largest exporter of services in Victoria. This derives from the expenditure of overseas students on fees and expenses while in Australia. The COM has been an important site for this industry, not just via enrolments at RMIT and Melbourne University but also by branches of regional universities, notably Central Queensland University. It has also been a focus for TAFE institutions offering hospitality courses. At its peak in the late 2000s, there was a string of kitchens and hairdressing salons in the COM providing such courses. Most are now gone. As noted earlier, enrolments in the higher-education sector have also declined. The export of education-related services from Victoria, which peaked at \$5.5 billion in 2009-10 have since been estimated to have fallen to \$4.4 billion in 2011-12.

Official estimates for the export of telecommunication and business services from Victoria indicate that the level is low relative to NSW and declining. The peak year for the export of business services (which includes legal, accounting and management consulting as well as architectural, engineering and scientific services) was in 2008-09 when they reached \$1.93 billion (compared with \$4.4 billion in NSW). After falling sharply in 2009-10, they have since increased to \$1.87 billion in 2011-12.⁵⁹

We conclude that there is no convincing case that the COM will repeat the jobs boom of the period 2006-2011 in the medium term. If this is the case, it is unlikely that this important driver of demand for apartments will continue as in the recent past.

We conclude the warnings by BIS Shrapnel and others are correct. The massive number of apartment completions to be completed from already released projects plus those soon to be released by overseas developers in the CBD and vicinity is far more than is likely to be needed.

Why worry about an apartment glut?

Apartments are crowding out offices

The State Government wants to make central Melbourne the hub for growth in knowledge intensive industries. It made progress in this direction in the 2000s when, as we detailed earlier, some 46 per cent of all the net growth in jobs in Greater Melbourne occurred within the COM. Most of these jobs were in financial services and other business services.

If this surge is to continue there will be a need for a parallel growth in office space in the CBD and vicinity because employers in these industries like to locate around like firms. This raises the question, as Robert Papaleo of CKC has pointed out, about the extent to which apartment building in the CBD is threatening the city's office market.⁶⁰

In order to quantify these concerns we compared the likely scale of office completions in the CBD and Docklands over the years 2013 to 2015 with that of apartments in the same locations. Data on the former were drawn from the Property Council data base and the latter from the CKC apartment data base. The total completion of office space in square metres over these three years is expected to around 350,000 square metres (well down on the level of recent years). In the case of apartments, some 12,650 apartments will be completed in the CBD and Docklands over the years 2013 to 2015. At around 75 square metres gross per apartment this will amount to some 950,000 square metres. This is three times the floor space for that expected for office completions.

This imbalance will worsen in 2016 and perhaps later because of the number of apartment proposals in the pipeline by foreign developers. By contrast there are few office projects mooted because of the recent downturn in office space usage in the CBD and Docklands, noted earlier.

This situation will change when the economic cycle turns and developers look to build new office space. When they do they will face a situation of diminishing potential sites because of the apartment boom. For example, as we show below several city blocks in the north west of the city which could provide a logical extension of the Bourke Street office precinct will soon be occupied by apartments.

Poor apartment quality

The COM is highly articulate when expressing its aspirations for the type of housing it wants to be built within its jurisdiction. The emphasis is invariably on diversity and sustainability. For example, its *Future Living Discussion Paper* states;

Our housing should enable people to live close to their jobs in environmentally sustainable buildings. To meet these needs, our housing must be affordable, support diverse communities and be good quality.⁶¹

This is not what the apartment boom is delivering, as is extensively documented in the *Future Living Discussion Paper* itself.⁶² The Paper draws on the COM research noted earlier about the trend towards small one-bedroom apartments. It also notes that 'Nearly two thirds of new housing over the last ten years was in developments of over 200 dwellings, particularly in the central city'.⁶³ It includes an assessment of the quality and amenity of the apartment stock built over the past six

years. Only 16 per cent was considered to be 'good', 48 per cent 'average' and 36 per cent 'poor'. This evaluation reflected design problems. 'These related to small apartment sizes, lack of apartment choice, dominance of car parking, poor internal amenity (light, ventilation and privacy) amongst other deficiencies'.⁶⁴ For example, 'Nearly a quarter of apartments incorporated a bedroom with no windows which 'borrowed' light from the adjacent living areas'.⁶⁵

The COM has also made its priorities clear regarding its streetscape and aesthetic standards for apartment towers in its Capital City Zone (which includes the CBD, Docklands and Southbank). They include the need for towers to be set back from street frontages and well-spaced to equitably distribute access to an outlook and sunlight.⁶⁶ Developments should minimise wind tunnelling. They should ensure that car parking above ground level avoids a poor interaction with the street. Entrances, windows and balconies fronting onto the street should allow opportunities for neighbourhood interactions.⁶⁷

The towers being built and proposed hardly meet these criteria. The forest of high-rise buildings to be located at the western end of the CBD near Southern Cross Station, illustrate the point. If all the projects approved go ahead, this end of the city will be transformed into a stark, tower filled cityscape. The map shown below, which draws from an *Age* newspaper analysis published late in 2012, indicates what is to come.⁶⁸



These towers offer little in the way of setbacks or offsetting public space. This can be seen from the developer's image of what the Upper West Side Melbourne project (No. 7), which fronts on to Bourke and Spencer Streets, will look like on completion.



The three towers shown are a part of the four tower complex which will comprise the massive Upper West Side project. They will result in some 2,500 apartments. The image shows the Bourke Street frontage. The severity of the interface with the street is evident, as is the likelihood of resulting wind tunnelling. The project will include an acre of open space with 'high quality landscaped space'. However, this is to be located on the podium above the street and well away from public access.

Upper West Side is a project of a major Asian developer, the Far East Consortium, which is based in Hong Kong. Its CEO, David Chiu, whose major projects are located in mainland China, says he is confident about the market for his Melbourne apartments. He thinks that the 'increased time that workers must take to get to work' with public transport and road congestion in Melbourne will add to 'the greater attractiveness of finding accommodation close to the city'.⁶⁹

Some of the apartment projects released are stylish, especially when viewed as individual buildings portrayed by an artist. Most are little better than dog boxes, with jazzy adornment tacked on to the building façade. Those buying off-the-plan may imagine panoramic views across the Bay. Things change however, when banks of these towers are built. They obscure each other's view. They collectively create a great wall, like that emerging along Spencer Street. When complete, the overall effect would surely dissuade parents with young children from taking up residence. Where could children play? Where is the open space or other community facilities? Who is going to pay for such facilities even if there is a will to provide them?

Infrastructure deficiencies

The original advocacy for a residential presence in inner Melbourne included the argument that such development could take advantage of underutilised transport and other infrastructure (unlike new estates on the fringe). We are long past this point. The surge in new apartment buildings and subsequent resident numbers is now putting serious strain on existing infrastructure, as in the case of open space referred to above.

Part of the problem is that the Municipal Councils responsible for community facilities are starved for funds. The State government reaps the stamp duty revenue from new projects, but provides negligible support for the municipalities in question. For their part, the project developers are

required to pay very little by way of infrastructure levies, either for public open space or as contributions for community facilities, transport, drainage and other infrastructure.

Open space

The Subdivision Act 1988 does provide for an open space levy. This may be met through a land or cash contribution (up to five per cent of site value of the land on which the project is constructed). The levy does not vary according to the number of apartments that are built on the site. Nor is it 'linked to municipal open space policies and strategic plans that identify the open space needs of growing populations in inner and middle municipalities.'⁷⁰ The amount raised is so small that it is rarely used to actually purchase land for open space. It is typically used to augment facilities or access to existing open space.

By comparison, Councils responsible for administering new subdivisions in outer suburbia can levy open space requirements for such subdivisions. Currently, under the State Government's Growth Area Authority, which administers all planning for new subdivisions by way of Precinct Structure Plans (PSPs), developers must provide 10 per cent of the land included in their estate for public open space.⁷¹

Community facilities and other infrastructure

The situation is even worse for other infrastructure in inner-city areas. Most Councils do not charge any levy at all. The results are becoming obvious in locations where apartment projects are concentrated. For example, in Stonnington, the Council is being left to cope with the consequences of the intense high-rise apartment development in its Forrest Hill precinct. This is a small area between Toorak Road and Melbourne High School which adjoins the railway line to the southern suburbs. The South Yarra station on Toorak Road is the main transport facility. The towers in this precinct will be familiar to those approaching the city along the Monash freeway before it reaches Punt Road.

The apartments themselves rise like a thick forest. There are no setbacks from the narrow streets they front. The residents have easy access to the amenity of the Toorak area, including the nearby Botanic Gardens. But, even this access is becoming problematic because of traffic congestion in and out of the precinct and because South Yarra Station is struggling to cope with peak demand.

The Council put its case to the State Government in January 2013.⁷² It complained that the State Government had received in excess of \$22 million in Stamp Duty charges since 2010, but had contributed little to the area's new infrastructure needs. These include the upgrading of the Station and the provision of extra open space, which the Council believes could be accomplished by developing the South Yarra railway siding (on the other side of Toorak Road from the station entrance).

The COM approved a Development Contributions Plan for the Arden-Macaulay and City North urban renewal areas (discussed in more detail below) in February 2012 and for the Southbank urban renewal area in 2010. The contributions cover only a small proportion of the infrastructure costs the COM anticipates it will have to pay for. The charges to be levied are very low, barely \$3,000 per dwelling in the case of the City North area.

Again, by contrast, the charges for new subdivisions within PSPs on the suburban fringe are much higher. They are currently around \$20,000 per block. The amount is set according to costings for the land and construction needed for active recreation (sporting ovals), passive recreation (such as walking tracks) and community centres. The latter must include facilities for kindergartens, maternal and child health centres and community meeting places.⁷³ This is not to imply that all is well with infrastructure provision on the fringe. Rather, this information is intended to serve as a reminder that the apartment boom is creating its own infrastructure crisis.

Urban renewal

As noted, the COM is in the process of rezoning the City North and Arden-Macaulay areas for more intensive urban renewal. The COM's forecast is that employment in the City North precinct will grow by 5,438 and the resident population by 6,762 between 2011 and 2031. Job growth in the Arden-Macaulay precinct is expected to be 10,931 and the number of residents to grow by 10,146 over the same twenty year period.⁷⁴

These two areas currently comprise consist of relatively low-density dwellings, many with heritage value. The City North area (which includes the district between Melbourne University and the northern edge of the CBD) is described by the COM as featuring, 'Wide streetscapes, simple architectural forms, a consistent and fine grained built form, an existing laneway network, charming parks and a number of heritage buildings.'⁷⁵ These are exactly the kind of neighbourhoods Florida's creative class are thought to prize. However, if the pattern in the CBD is repeated, they will soon have to cope with high-rise apartment blocks. This is also true of Arden-Macaulay, where the urban renewal plan specifically allows for high-density apartment blocks in areas formerly zoned for commercial and industrial purposes that adjoin the area's existing low-rise residential neighbourhoods.

The COM's aspirations for these areas are admirable – in the sense that they emphasise preserving their best features and the enhancement of their community assets. The problem is that the COM cannot enforce these aspirations.

State Government control of high-rise apartment projects

The COM's *Future Living Discussion Paper*, makes it clear that its planners disapprove of the current crop of high-rise apartment projects. Their Director of City Design, Rob Adams, has warned that the city centre could become 'Hong Kong but without the spectacular setting' if the 104 tall towers now approved for construction in central Melbourne are built.⁷⁶

Even if the COM Council was persuaded to oppose projects future proposals, this would have little impact on the current development pattern. The COM does not have the authority to determine the outcomes of proposals for buildings of 25,000 square metres or more. This power is held by the Planning Minister, Mathew Guy. Most of the towers proposed for the COM are this size. They must be referred to the State Government Department of Transport, Planning and Local Infrastructure (DTPLI). The Minister for Planning makes his judgement after considering his DTPLI officers' advice.

Neither this advice, nor the reasons for the Minister's decisions are revealed to the public. On coming to power the LIB/NCP Government scrapped a committee set up by the previous Labor

Government, under which the government and the COM jointly assessed developments with a gross floor area larger than 25,000 square metres.⁷⁷

Currently, when considering projects of four stories or more in height the DTPLI 'refers' to the Victorian Guidelines for Higher Density Development. However, the 'high level objectives' stated in these Guidelines do not include 'specific and measurable outcomes'.⁷⁸ Nor is there any requirement that the project be submitted to a Design panel. According to the COM, a Victorian Design Review Panel has recently been established, but only looks at a 'relatively small number of larger schemes of state significance'.⁷⁹

The DTPLI does have experts look at each proposal, and they can include COM officers. But, the latter's engagement is purely advisory. The COM's role is mainly confined to negotiation with the developer at the inception of the project. It also provides some guidance on detailed planning issues in the final approval process.

As a result, there has been little to stop the Minister of Planning, Mathew Guy, from giving the green light to apartment block projects, whatever the misgivings of the COM or the interested public.

The Minister's view is that such is the anticipated growth of inner Melbourne, that it would be a dereliction of duty on his part if he did not facilitate such development. Otherwise, the city could be caught short – with dire consequences for the city's progress. This is a message that goes down warmly with audiences of planners and developers, as one of us experienced recently when challenging the Minister about the grounds for his optimism. This stance cloaks the Victorian Government's main concern, which is to facilitate the apartment construction boom while it remains one of the few industries in Melbourne that is flourishing.

Conclusion

Melbourne's high rise boom is extraordinary. It has already transformed the city's skyline. It is inevitable that this will intensify over the years 2013 to 2015 because at least another 39,000 apartments will be completed during this time.

The State Government is anxious for the boom to continue because it will keep cranes on the horizon at a time when growth from other economic activities has slowed. The current slow-down in office construction has accentuated these concerns. In the absence of new policy, it is likely that apartment towers will spread from the CBD via urban renewal into the adjoining inner city suburbs.

For some, the transformation of the skyline is exciting. Towers like Eureka on the south of the river can be seen as symbols of the city's vitality. To others, who are beginning to find their voice, these towers are a blight on the city's liveability. As these towers aggregate, they are creating severe walls of concrete and glass, sometimes relieved superficially by tacky facade decoration. Such gaudy additions do little to conceal the underlying reality.

To make matters worse, the apartment surge is creating an infrastructure backlog, which neither the COM nor the other inner-city municipalities, where they are concentrated, have the financial capability to rectify. The situation is akin to that said to exist in outer suburban fringe estates. Yet, our analysis shows that developers have to pay far more in developer contributions to open space and community facilities than is the case for those putting up apartment towers.

The impending apartment oversupply is a consequence of developer and investor led priorities. These priorities result in projects which maximise the number of apartments on the site. This means apartment towers predominantly comprised of small apartments suitable only for singles or couples who, for the most part, are likely to be transients.

This outcome is far from the original vision of those responsible for promoting a balance of work and residence in inner Melbourne. The investment in the city's amenities was intended to make Melbourne 'the place to be'. The residential aspect was supposed to be based on medium-density living, which would attract a diversity of households. The aspiration was to create an ambience where the so called 'creative class' would be encouraged to live and work in the city and thereby contribute to Melbourne becoming an internationally-competitive knowledge city.

This idea was probably always a myth, in the sense that the 'creative class' is more likely to move to locations after the establishment of knowledge industries than the other way around. Nevertheless, there are plenty of examples of cities where knowledge industries flourish along with exciting inner-city neighbourhoods. If this is to happen in Melbourne, it will not be in the locations dominated by high-rise apartment blocks. It is more likely to occur in the fringe areas of the CBD which are slated for 'urban renewal' as in the City North precinct.

A couple of overseas examples will help make the point. One is the U.S. west coast city of Seattle. Seattle's population is just over 600,000. Thirty years ago it was a decaying city, down on its heels. Microsoft arrived in 1979. Thereafter, the computer design industry took off with hundreds of start-ups flourishing in an industry cluster initially feeding off Microsoft. Now, the downtown areas of Seattle are described as follows:

People stroll along lively streets dotted with eclectic bookstores and bodegas specializing in artisanal goods. Throughout the city, gourmet restaurants and new cultural venues have taken over abandoned structures of surface parking lots.⁸⁰

Seattle is subject to growth pressures. But, it accommodates these with very strong controls aimed at ensuring the existing 'funky' ambience is protected. It is a similar story in Portland, which is also located on the west coast of the U.S., in this case in the State of Washington. Portland has a population of 2.2 million. It too, features a cluster of hi-tech industries, including start-ups, which originally took off after the computer chip giant Intel, set up in the city in 1976.

Portland is famous for its emphasis on ecology. 'It regularly makes popular top ten lists for most green and eco-friendly cities and for good reason.'⁸¹ It is well-known for its path-breaking initiatives which date to the 1970s, aimed at curbing urban sprawl. Its downtown areas have been renewed, free from freeway dominance. Now, 'liberated from concrete, the downtown houses microbrewers and cutting-edge restaurants and has become magnet for aspiring musicians, artisans and techies.'⁸² Like Seattle, the city carefully controls the development of the city to ensure it does not lose this setting.

The investment in Melbourne's inner city amenities is being squandered on the high-rise apartment industry. Inner Melbourne is being transformed by an apartment industry whose beneficiaries are developers and investors who increasingly reside overseas.

What will the city be left with? As the projected increase in apartments hits the market, one consequence is likely to be improved rental affordability. This may be considered a bonus. Our analysis has shown that between 2006 and 2001 there was a surge in the number of residents who live in the COM and work in adjoining suburbs. This dormitory function is likely to accelerate as the stock of apartments mushrooms. This is hardly an ideal outcome. The new residents are likely to be less affluent transients forced to accept accommodation in tiny apartments because of high housing prices on the fringe of the CBD.

The State Government and the COM want to make the CBD and surrounds the hub of a knowledge intensive industry cluster. Yet property development within this locale is being dominated by apartment projects. This could threaten the opportunities for the expansion of further office space.

The day of reckoning will come when investors wake up to the reality of an apartment glut. Elsewhere in the developed world, pundits have pondered how the circumstances that led to various property bubbles to burst were allowed to proceed. In time, there will be similar reflection in Melbourne.

The implication is that the apartment industry should be slowed down. Future permits should only be issued for projects which meet the design standards proposed by the COM. The urgent priority is to slow down the approval process. Before any further projects are approved, they should be subject to public input and they should be evaluated according to whether they meet the COM's planning guidelines. Mr Guy should exit the approval process – at least until after the proposal has surmounted the public and COM hurdles. To the extent that expansion is permitted, it should reflect the original vision of medium-density housing catering for a variety of households.

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