Back to the Future for Victoria's Population Growth?

June 2018

As population projections become quickly out-dated, planners, policy analysts and the development industry must increasingly rely upon their own understanding of the dynamics of Victoria's population growth. The benefits flowing from lower interest and exchange rates have now largely been exhausted, and improving employment conditions in other states means that Victoria now faces a very different economic landscape to that of the past five years.

Victoria's population growth rate has reached 2.4% per annum, the highest since the post-war migration and baby boom period. This is slightly above the previous peak of 2.2%, just before the Global Financial Crisis pushed growth back down to 1.4% per annum. Can Victoria's population continue to grow at this rate, supported by new infrastructure investment and higher density housing? Are we in the midst of a population ponzi, as some suggest, that has only served to increase property values and suppress wage growth?

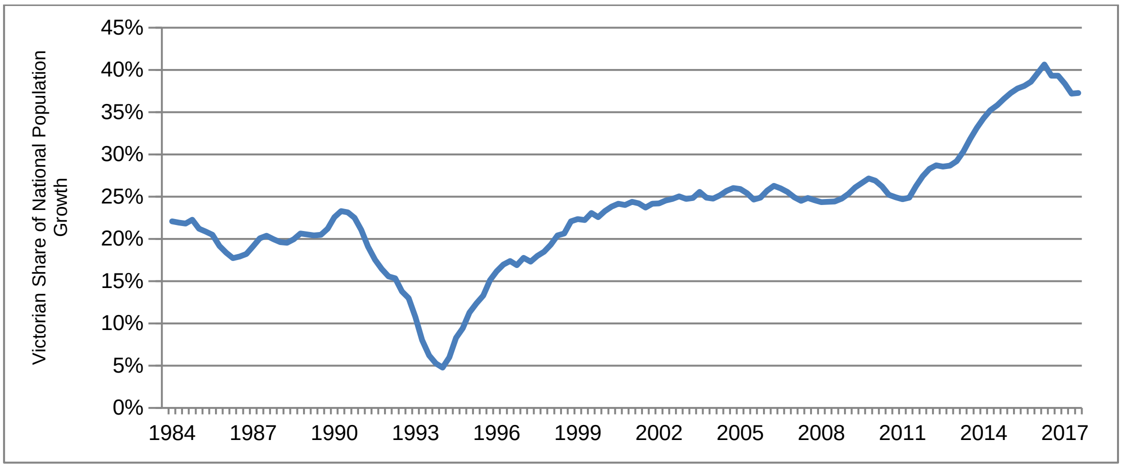
This Research Bite puts aside the emotive aspects of the population debate to objectively explore some recent and longer-term trends that provide a context for where Victoria's population growth may head in the future.

Victoria's Share of National Population Growth

Victoria's strong population growth reflects its appeal to new residents, who are a source of both labour and consumer demand that fuel economic growth. Queensland and Western Australia were the fastest growing states before the mining boom ended in 2012, resulting in a sharp decline in their growth and leaving Victoria to take the crown for the first time since 1942.

For three decades prior to 2012, Victoria's share of national population growth was remarkably stable at around 20%-25%. The exception to this was the early 1990s recession when its share fell to only 5% before recovering back to 25%. The reverse may now be occurring with the graph below showing that Victoria's share may have peaked at 40.6% in 2016, before trending downwards to its current level of 37.3%.

Victoria: Share of National Population Growth

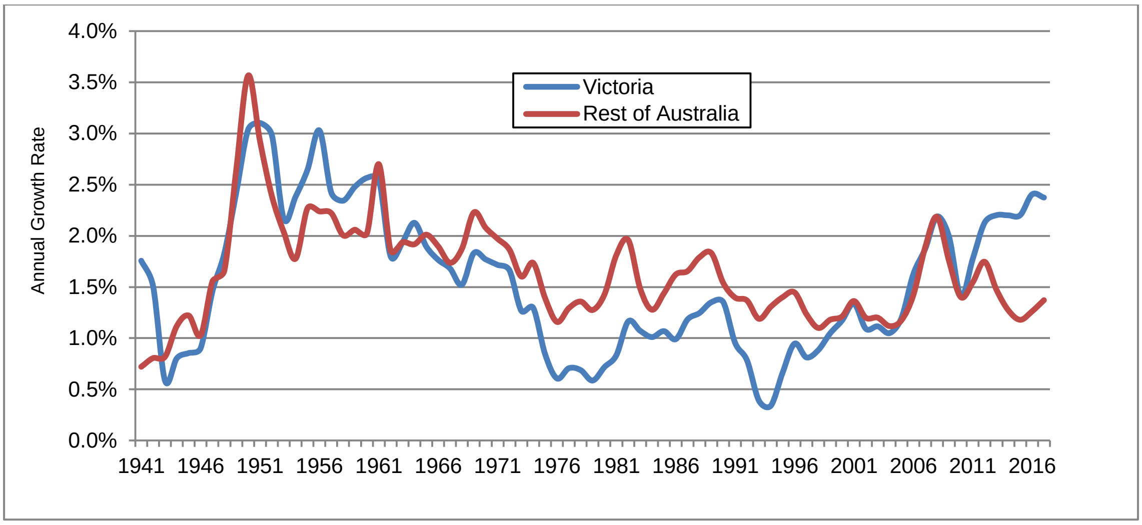


Source: ABS

Based upon Australia's current population growth of 395,000 persons per annum, if Victoria's share were to continue to fall back to 25%, state population growth would decline from the current 147,500 persons per annum to 98,900. This would represent an annual growth rate of 1.6%, which is generally consistent with Victoria's 30 year average of 1.4% per annum. It should also be remembered that both New South Wales and Queensland have recently been growing at around this rate.

Therefore, a slowing in Victoria's growth rate to 1.6% per annum may simply represent a rebalancing of population growth between the three eastern states. As the graph below shows, Victoria's recent strong population growth has far exceeded that of the rest of Australia, something which has not occurred since the 1950s. Unless this can be explained by a major structural change in the Victorian economy on the scale of the post-war manufacturing boom, this growth may merely have been an aberration brought about by a combination of events elsewhere.

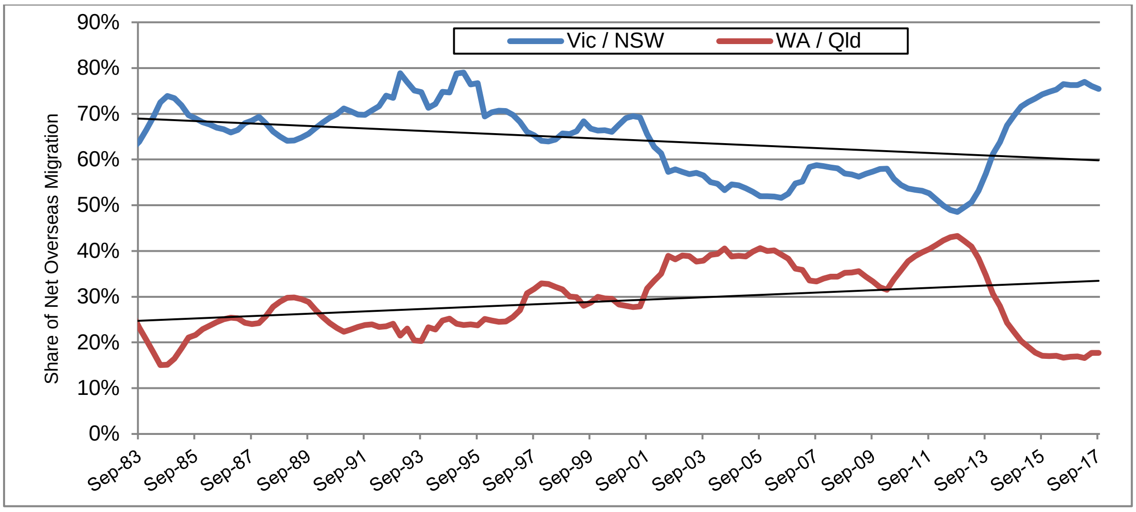
Annual Population Growth Rate: Victoria vs. Rest of Australia



Source: ABS

So why has Victoria experienced such a sharp increase in its share of national population growth? Given that Net Overseas Migration (NOM) currently accounts for the majority of the state's population growth this is a good starting point. The following graph shows the share of NOM accounted for by the resource states of Queensland and Western Australia compared to the non-resource states of Victoria and New South Wales. Since the end of the mining boom in 2012, the share of NOM accounted for by Victoria and New South Wales has increased from 50% to almost 80%. However, for the two decades prior to this, there was a downward trend in the combined share of these two states.

State Share of Net Overseas Migration - Resource vs. Non-Resource States



Source: ABS

Victoria's share of NOM has fallen from a high of 36.8% for the year to June 2016, to 35.4% for the year to September 2017 based upon the latest ABS figures. Should this share continue to decline to the levels recorded in 2012 of around 23%, the contribution of NOM to Victoria's population growth would fall from the current level of 88,500 persons to only 57,500. This alone would result in a slowing in growth by 0.5% per annum.

While there is debate around the level of Australia's permanent migration intake, the number of temporary skilled visa holders in Australia has fallen noticeably from over 105,000 in 2014 to the current 85,250, largely reflecting the end of the mining boom. While this fall has been mainly confined to the resource states of Queensland and Western Australia, the number of temporary skilled primary visa holders in Victoria has also trended down from a peak of 23,600 in 2015 to 21,600 today.

Victoria now appears to be facing a reduced share of both national net overseas migration and total population growth, which suggests that the recent period of historically strong growth may be coming to an end. This shouldn't be a surprise given that this growth coincided with a number of unique economic events including, the end of the mining boom which freed up workers for the non-resource states, a weaker exchange rate making manufactured and other exports more competitive, and historically low interest rates that supported a housing boom in Victoria.

Economic Cycles and Population Growth

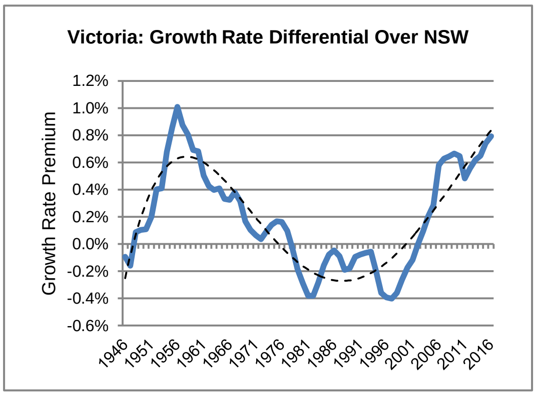
Population growth is influenced by a wide range of economic, social and lifestyle factors. For example, the relative economic performance of the states and their ability to provide employment opportunities. Industries tend to be concentrated in particular states or capital cities with mining largely in Western Australia and Queensland, manufacturing in Victoria and New South Wales, and finance and professionals services in Sydney and Melbourne. Therefore employment opportunities and population growth within each state tend to reflect the economic cycles of these industries with flow-on impacts through the local economy.

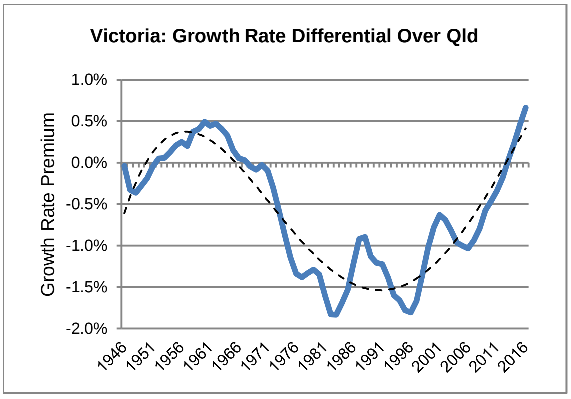
Lifestyle factors may also influence migration flows between the states with Melbourne's growing reputation as the world's 'most liveable city' coinciding with net interstate migration increasing by around 15,000 new residents per annum since 2012. Whether Melbourne's increased appeal is able to be maintained in the future is yet to be tested.

Given the complexity of various economic cycles and the mobility of Australia's population to take advantage of employment, lifestyle and housing opportunities, it is useful to look at longer-term patterns of population growth that provide a context for Victoria's future growth. The following two graphs highlight the differential between Victoria's five year moving average population growth rate and that of New South Wales and Queensland, and the strong cyclical pattern that characterises each.

Victoria's population growth rate has previously only exceeded that of New South Wales by more than an average of 0.2% per annum over a five year period in the lead up to the Global Financial Crisis, and before that during the immediate post-war period. Similarly, Victoria's growth rate has typically been well below that of Queensland.

Victoria: Annual Population Growth Rate Differential Over NSW / Qld (5 Year Moving Average)





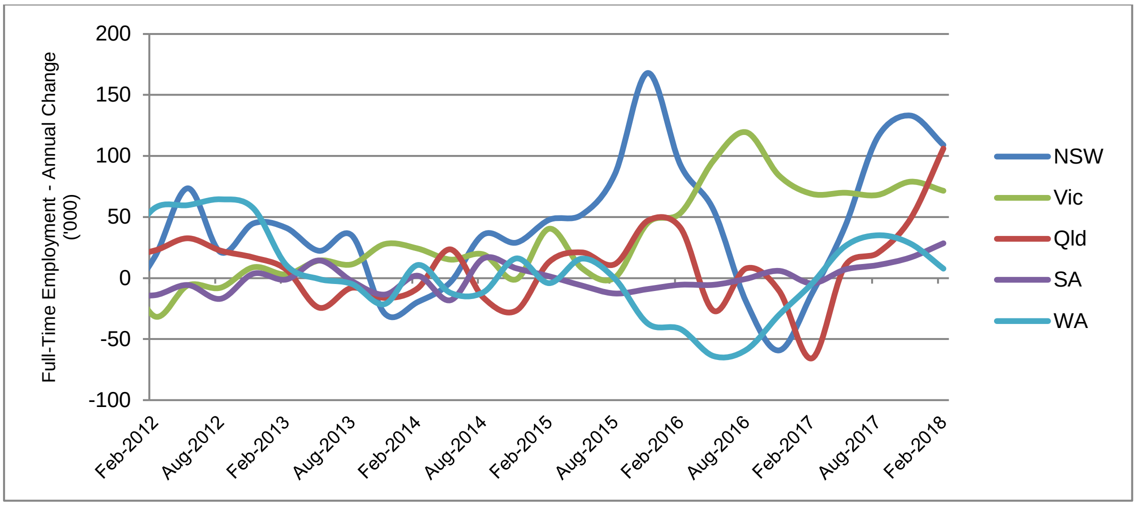
Source: ABS

The margin between Victoria's population growth rate and that of both New South Wales and Queensland is now higher than any time since the 1950s. While it is too early to suggest what this may mean for Victoria's longer-term growth, economic indicators should be closely followed for signs of a potential peaking in population growth. If Victoria's population growth has reached a turning point, then it may lose ground to both New South Wales and Queensland over the coming decades.

Employment

The strength of a state's economy and the creation of new jobs is a key determinant of sustained population growth. As the graph below shows, annual growth in full-time jobs in Victoria surged after 2015, at the same time as jobs growth weakened in New South Wales, Western Australia and Queensland. After peaking at 120,000 new full-time jobs in 2016, annual employment growth has since fallen back to around 70,000 per annum in Victoria, with both the northern states now experiencing strong growth. The smaller mainland states have also shown a resurgence in employment growth with South Australia recording its highest since 2010, and Western Australia now experiencing positive annual jobs growth.

Full-Time Employment: Annual Change ('000)



Source: ABS

Overseas migration patterns are beginning to reflect changing employment opportunities between the states, with Victoria's share of net overseas migration slipping by 1.4 percentage points from its peak in 2015-2016. This fall has been largely due to Queensland increasing its share by 1.7 percentage points from 10.8% to 12.5% over the same period.

Similarly, Victoria's annual net interstate migration peaked at 18,560 in the year to March 2017 before falling to 16,925 for the year to September 2017, which also reflects the impact of improving employment opportunities in other states. While New South Wales continues to lose residents at an increasing rate, both South Australia and Western Australia are experiencing a stabilisation in the rate at which they are losing residents. Queensland is experiencing its highest level of annual net interstate migration for ten years and now exceeds that of Victoria.

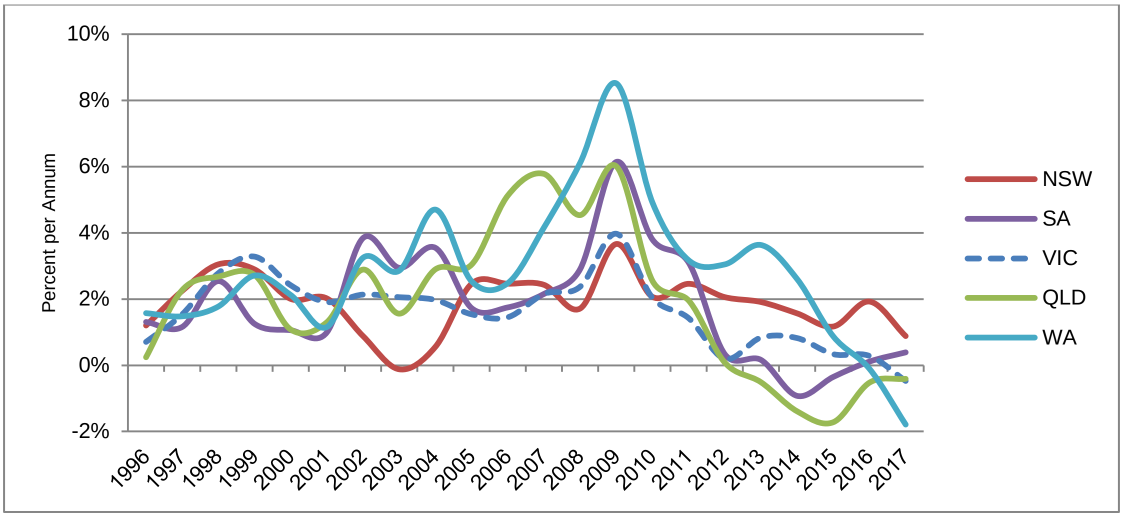
With improved employment conditions in other states, Victoria faces increasing competition for new residents. Although the historical net migration of Victorians to Queensland has been virtually eliminated over the past decade, there is now the potential for this to be resurrected if employment opportunities continue to strengthen in the Sunshine State.

Household Disposable Income

The Victorian economy, as measured by gross state product, grew by 3.3% in 2016-2017 with only the Northern Territory and the ACT growing at a faster rate. This follows on from 2.5% in 2015-2016 which was the highest annual growth rate since 2005 and has naturally coincided with strong population growth. However, while this indicates Victoria's productive capacity may be growing, it is not a measure of the economic well-being of Victorian households and therefore the state's likely appeal to new residents.

Real household disposable income per capita indicates the extent to which economic growth is flowing through to households. The following graph shows average growth in this measure over the preceding three year period. While all states experienced a slowing in growth as a result of the global financial crisis, Queensland and Western Australia have been most impacted by the ending of the mining boom. However, Victoria is now experiencing a slowing in per capita household disposable incomes, averaging negative 0.5% over the past three years which is on par with Queensland and below that of both New South Wales and South Australia.

Real Household Disposable Income per Capita (3 Year Moving Average)



Source: ABS

Variances in the growth of disposable household income across states reflect the impact of employment conditions and therefore the potential for migration between states. Differences in housing costs may however also influence the pattern of interstate migration. Victoria is experiencing declining household disposable incomes combined with high housing costs. This contrasts with Queensland and to a lesser extent the other smaller states, which are now experiencing improved employment growth and have significantly lower housing costs. Hence we may potentially see a scenario whereby the strong net interstate migration into Victoria over the past five years is reversed.

What Lies Ahead

Population growth has been a key driver of the Victorian economy through generating demand for housing, retail goods and business services. This has been reflected in the retail and construction sectors accounting for one-third of employment growth since 2013. Any slowing in population growth may impact significantly upon Victoria's retail sector given that real per capita spending has already stagnated. Further softening in house price growth may also impact upon the perceived wealth of households, consumer confidence and households' willingness to spend.

Reduced demand for housing will impact upon overall construction activity as well as housing affordability, potentially making medium density housing such as townhouses a more attractive alternative to apartments as underlying land values continue to soften. Unfortunately, any population induced slowing in demand for housing will exacerbate the current weakening in Melbourne's residential property market and the impact of tighter lending practices following the current banking royal commission. The residential development sector will have the opportunity to increase its focus on the owner-occupier segment of the market through smaller, higher quality, apartment projects. Similarly, there is already a shift amongst developers towards commercial office development.

Given that the retail and construction sectors have been major employers of Victoria's growing population, any slowing in these sectors may have wider flow-on impacts through the economy. Hence, while the Victorian government's program for major infrastructure projects may address congestion issues, it is likely to have an increasingly more important role in supporting the state's economy.

Planners, policy analysts and property developers will increasingly need to understand the implications of slowing population growth for the Victorian economy, land use patterns and development opportunities in order to ensure a gradual transition to an expected lower growth environment. Weaning Victoria off high population growth may be a challenge, but not one which it and other states haven't faced before.