Houses vs Units

Thoughts and Opinions by Dr. Tony Hayek

Over the years, I have come across a number of misconceptions in and around the property industry. So essentially, what we have been trying to do with our Thoughts and Opinions papers is 'demystify' these pre-defined ideas and bring clarity and balance to key topics.

Typically, people have pre-conceived ideas about property in relation to certain locations, types of property, age, value and cash flow. More often than not, there is no merit or logic behind the thought, it is simply something they have picked up along the way and the thought process has just stuck.

One of the key 'myths' we come across is that you should only invest in house and land as opposed to units. So let's address this theory.

The first thing to do when addressing this theory is to look at the numbers to get a feel for how different property asset classes are actually performing. We have compared data from the Real Estate Institute of Australia which show the difference between price growth in houses and units in Australia between the end of 1997 and the end of 2009. This is detailed in the graph below.

Australian Median Growth Rates Houses vs Units

Source: Real Estate Institute of Australia, Blue Wealth Property

As the graph shows, houses and units have grown at similar rates over the last 13 years. The median Australian house price grew from $183,100 to $458,100, which represents 150.24% over the 13 year period. The median Australian unit price increased from $153,200 to $373,700 or 143.93% over the same period. At the beginning of the decade, houses performed considerably better and did again in 2003, with units outperforming slightly since the middle of 2003. As RP Data reported, it does seem as though "units are no longer houses' poor cousin".

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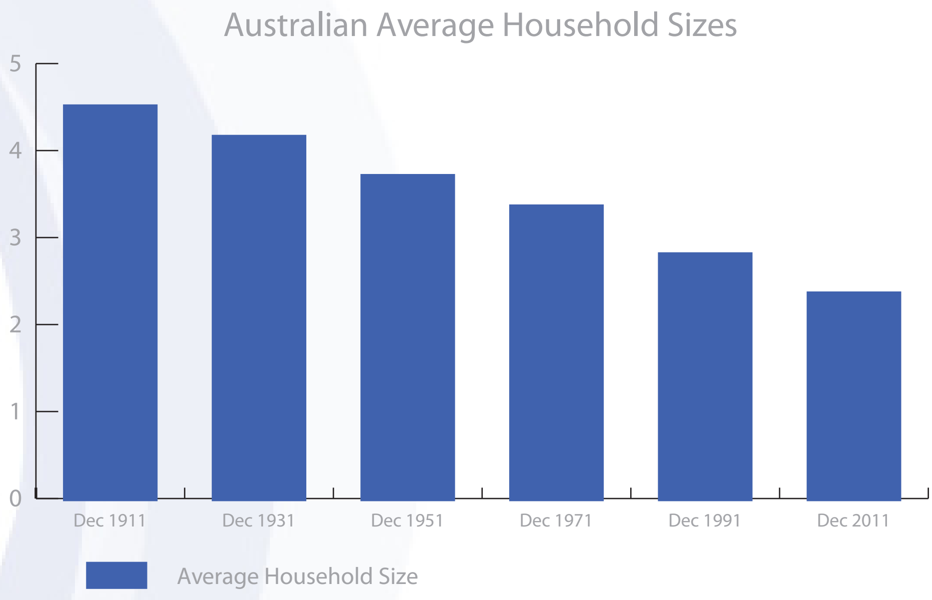
The data clearly shows that there is no significant difference in the growth rate between houses and units in Australia. So given this information, how do we work out what type of property we should be investing in?

If we know that houses and units grow at almost the same rate, we should be basing our decision on what is driving the value of the property rather than the type of property itself. This is consistent with the idea that something is only worth what someone else is willing to pay. On a property-to-property basis, the most common demand driver is the demographic of the area.

Over the past 20 years, there has been a large shift in Australia's demographic. The most important change we are seeing is the long term decline in average household sizes. The graph below shows a significant decline in household sizes every 20 years for the last 100 years. In 1912 there were 4,733,359 people in Australia, this was an increase of 300,390 persons or 6.7% on the previous year. There was an average of 4.5 people in every household, thus there was an extra 66,753 dwellings demanded in that year. In 2009, there were roughly 22,065,700 people in Australia, an increase of 451,900 people on the previous year. There was an average of 2.53 people in every household in 2009, thus there was an extra 178,616 dwellings demanded in that year. This represents a growth of 167.5% in the number of dwellings required to house Australia's population.



Source: Australian Bureau of Statistics

This has an enormous effect on housing demand because as the population grows, there will be a compounded effect on housing demand. For example, in 1911 let's say the population increased by 1,000 persons in Australia. When the average household is 4.5 persons, this means that the new population would demand an extra 222 houses (4.5 people x 220 households = 1,000 extra persons). For arguments sake, if the population grew by 1,000 people today, (the current average household size is 2.53), this would create demand for an extra 395 houses. This is an example for how demographic change effects housing demand.

Household make up is also changing drastically. The most compelling trend we are seeing is the increasing number of people living alone. This is part of the reason we have seen units perform well in recent times. In 2001, there were 1.8 million Australians living alone, and according to the Australian Bureau of Statistics' Household and Family Projections, this figure is expected to increase by between 57% and 105% by 2026.

To give a few examples of this, consider the demographic groups such as the "Baby Boomers" and "Generation Y" and how they have changed the dynamic of property demand in Australia. The "Baby Boomers" are increasingly downsizing to smaller dwellings as they come into their retirement years, this has changed the demand for properties in many pockets across Australia, examples of this include Cabarita and Breakfast Point in Sydney's inner west. Generation Y has placed increasing demand on inner city apartments in "grunge" type areas close to transport in capital cities such as Brisbane, Melbourne and Sydney. As an example of how preferences change over time, consider projects developed close to train stations 20 years ago. For those of you who can remember that far back, you would recall that there was negative stigma around having trains so close to home. Nowadays, the transport-oriented developments are in ever-increasing demand. As a result, units in these areas have outperformed average growth rates.

Being familiar with statistics such as a suburb's median age, average income, average household sizes is crucial in trying to establish what type of property to purchase. This will allow you to maximize what that "somebody" is willing to pay come time to sell.

So back to the main question: Houses or Units?

The answer is simple. It depends on the market! There are some markets where the argument for houses is strong and others where a unit investment is a smarter decision. The main thing you need to understand when making this decision about property types is how the demographic in the area will affect the demand on the property you are purchasing now and in the future. Every time I add another property to my portfolio, I ask myself the same question: "What will the world look like when I come to sell this property?"

The amount of money you make on a property is directly related to the number of people that will want to buy your property when it comes time for you to sell it. The more competition there is for your property the better the result will be. Therefore, the more information you have on a market's demographic trends, the better equipped you are to make decisions today and benefit tomorrow.

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