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Party still going for property investors

Experts say it's very unlikely property prices will calm down this year, writes Nigel Bowen.

Key points

- In most states, house prices are still increasing.
- Strong demand indicates this will continue.
- Interest-rate increases won't shock the market.
- Unit oversupply is only a moderate risk in Brisbane and Melbourne.
- Flat wage growth, unemployment are risks to the housing market.
- Confidence is at a two-year high, according to the ANZ Property Council Survey.

Attend a dinner party or barbecue and you won't have to wait long to hear the resident bear explain why the party is over when it comes to investing in property: interest rates must rise, inner-city apartments will flood the market and the big unknown of the years, the impact of US policy.

But the experts we've spoken to resist this explanation, retaining a bullish view of the Australian property market.

The party continues

"Do you need to do some more research and be more cautious than was the case in 2013?" asks CoreLogic Asia Pacific research and analytics head Tim Lawless. "Absolutely. We're almost five years into the cycle and Sydney dwelling values have risen by 60 per cent over that time. But markets such as Canberra and Hobart are showing an accelerating growth trend as well as offering comparatively healthy yield profiles.

"Our research shows 70 per cent of Australians still think it's a good time to be buying property," adds Lawless. "Counter-intuitively, almost the same amount – 67 per cent – said the market was vulnerable to a significant correction. But I'd argue those concerns are overblown."

Sydney and Melbourne prices are still moving up, says Martin North, principal at research firm Digital Finance Analytics, a consultancy for banks and financial services companies.

"Granted, there are regional differences and markets such as Perth and the Northern Territory are going sideways or a little backwards. But there is still a lot of demand that will cause prices to rise, if a little more slowly than previously, for the next 12 to 24 months."

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Tim Lawless, CoreLogic

Interest rates won't end it

"Some of the very cheap rates that were around have now gone," observes North. "Rates are going to rise over the next 12 to 18 months, but it will happen slowly. Buyers can still get a great deal if they lock in rates now for the next three to five years."

The Reserve Bank of Australia is still focused on stimulating the broader economy and keeping the Australian dollar low, observes Lawless.

"The RBA is also aware household debt is at high levels and households are sensitive to a higher cost of debt. So I'd be surprised by anything other than slow and moderate increases."

Neither will oversupply

"People aren't wrong to be worried about the inner-city unit markets in Brisbane and Melbourne, but the crunch is still a way off," Lawless says.

"Most of those apartments are pre-sold before construction commences. The problem arises 18 to 24 months later when settlement comes due. Buyers expect some on-paper capital gain but they may start seeing an on-paper loss. That can then lead to them forfeiting their deposit and the developer needing to resell that stock."

He predicts non-settlement risk will peak in late 2017 in the epicentre of supply nodes.

"Think Southbank, the Docklands and the central business district in Melbourne and the inner north and inner south in Brisbane," Lawless says. "It's the undifferentiated stock that's most at risk. Properties targeted towards owner-occupiers, with quality fixtures and fittings and a decent developer behind them should be safe havens."

North concurs, saying he's modelling for falls in inner city Brisbane and Melbourne.

"But it is falls of a few per cent only, not drops of 20 per cent," he says. "There's enough demand in Sydney that I'm not modelling any falls in price for units there."

The housing market in 2017 (//www.youtube.com/v/SAevJap8t2I?t=20s)

(3:40 min)

Nor even The Donald

While it's impossible to predict global events, North doesn't see any immediate causes for concern.

"Something such as a US-China trade war would take time to play out and even if it did occur, it may have a negligible or even positive impact on the Australian economy," he says. "What is more of a worry is flat wages and the possibility of unemployment rising. Australians aren't used to having static incomes. If, on top of that, unemployment began to creep up property owners could start having trouble making repayments, especially given lenders have been tightening up lending criteria."

While he acknowledges that Trump has introduced uncertainty into the equation, Lawless points to the fact that he's been moderating his positions since winning the presidency.

"He's probably constrained in what he can do in any event," Lawless says. "Even if he did, for example, slap a 45 per cent tariff on Chinese goods, that may prompt the Chinese to stimulate their economy with all sorts of benefits for Australia."

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According to the latest Australian Bureau of Statistics figures, national investor lending for residential housing to the value of $12.49 billion was approved in October 2016. This was 1.5 per cent higher than September 2016.

"Other asset classes are still offering little in the way of returns so I'd expect property to remain in favour," Lawless says. "Anecdotally, it appears to be popular with lots of different investors, from mums and dads to self-managed super funds. A trend that looks set to gather pace throughout 2017 is younger people renting where they want to live and buying an investment property somewhere more affordable."

For his part, North expects investment properties to continue to be going strong into 2018.

“There’s life in the old dog yet,” he says. “New construction stats may come off a little and interest rates may go up a bit. Nonetheless, the tax effectiveness of negative-gearing offsets and capital-gain benefits, which is underpinning the investment market, is unlikely to change. This is why there is such strong demand and aligns with recent capital growth. So it’s looking like everyone will remain hot to trot in 2017.”

This optimistic view of the property market is echoed in the ANZ Property Council Survey for the first quarter of the year, released January 12. Confidence rose to a two-year high, supported by stronger expectations of economic growth, capital values, and forward work schedules.

Much of the improved outlook was driven by the residential sector with house prices returning to double-digit annual growth rates across Sydney and Melbourne, while auction clearance rates have steadily increased and now sit only a fraction lower than last year’s peak. Investors have also returned to the market.

“Sentiment in property markets across New South Wales, Victoria and the ACT sits around record levels, in line with the transition away from mining-led growth,” says ANZ chief economist Richard Yetsenga. “A stronger non-mining economy means that we believe the RBA’s easing cycle is over, and we expect rates will remain on hold this year.”

While Western Australia continues to feel the negative effects of declining mining investment, the outlook for Queensland’s property market looks to have bottomed, and is embarking on a tentative recovery.

The survey also found that businesses nationwide now expect interest rates to increase over the coming year.

“This reflects both the RBA being at the end of their easing cycle, as well as tighter funding conditions,” Yetsenga says. “But as of yet, there is little sign that the likelihood of higher funding costs is having an adverse impact on the property sector.”

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