What do Australia's property market trends mean for you?

Posted on: 17/08/2018

What do Australia's property market trends mean for you?

The RBA leaves interest rates at 1.50% in August 2018.

It's all over the news: big shifts in Australian property market trends. In the first week of August 2018, the Reserve Bank of Australia chose to keep interest rates unchanged at 1.50%. In this blog post, we'll give you an overview of Australia's current economic and property market trends, and how they might impact you as a homeowner, real estate investor or first homebuyer.

Australia's cash interest rate remains unchanged at 1.50%

Australia's economy is currently growing. Gross Domestic Product (GDP) annual growth rate is expected to be slightly above average at 3% in 2018 and 2019. Investments in public infrastructure - projects like Melbourne's Metro Tunnel and so on - are supporting the economy. Export of resources is also growing.

The impact of inflation on household income

At present, Australia's inflation rate is close to 2%. The forecast is for inflation to be higher in 2019 and 2020 than it is today.

Household income is growing, but it's growing very slowly. Average wage increases are at or below inflation, which means that household income has been flat in real terms since 2012. If you earn $65,000 and your annual wage increase is 2% this year, your income actually buys less than it did the year before. This puts financial pressure on households who have high mortgages.

What's happening in the Melbourne and Sydney property markets?

Australia's median sale prices have fallen for the ninth consecutive month. Sydney's median property price has fallen 0.3% in the last month, and 4.5% in the past year. Melbourne's median property price has fallen 0.4% in the last month, but has risen 1.0% overall in the past year, compared with 10% growth in 2017. For up to date weekly auction clearance rates, you can check CoreLogic Auction results, but the weekly weighted average is 46.15% in August 2018 compared with 80.1% in late 2017.

What is the "interest-only loan reset" that's been in the news?

Mortgage lending standards are tighter. Australian Prudential Regulation Authority (APRA, the independent regulatory body for banking) has tightened the rules for mortgages. Specifically, APRA has recommended that the percentage of a bank's total loans that can be "interest-only loans" should be capped at 30%.

Limiting the number of interest-only loans helps the banks manage their risk. Interest-only loans allow borrowers to repay only the interest, and defer paying the principal or capital during the fixed term of that loan. This allows buyers with less disposable income to get into the property market at a low repayment rate for a few years. At August 2018, new interest-only loans from the big four banks are now down to 15%, compared with 38% in March 2017.

This also means that homeowners with interest-only loans may soon come up for rate renegotiation. About 1.5 million households, or 30% of all outstanding national mortgage debt, will be subject to changing from interest-only to principal and interest in the next 3 years. If the average interest-only borrower was hoping to renew their mortgage and continue to pay on interest-only terms, but the bank refused and switched them to paying principal plus interest, the repayments would cost an extra $7000 per year. This is a significant increase for the average homeowner, and as a result, some financial commentators are predicting a property market crash in Australia similar to the sub-prime lending crisis in the US.

As an aside, if you haven't watched the movie The Big Short, do watch it. It's an entertaining and plain-language explanation of the conditions in the US property market in 2005 to 2007 that precipitated the GFC. Some Australian commentators are predicting a similar situation here in the next few years; others are saying it won't happen.

What do Australian property market conditions mean for you?

We've seen huge increases in Australian property prices in the past 10 years, with a national average increase of 41% since 2008, a 72% increase in Melbourne and a 79% increase in Sydney. This has been great news for homeowners and investors. Not so good for first home buyers who increasingly feel like they can't get a foot in the door.

However, recent property prices in Sydney and Melbourne have started to flatten, with some forecasts predicting a major decline in property prices over the next few years. The changes are uncertain, and each possible outcome will mean something different to every homeowner, investor and aspiring first homebuyer.

For aspiring first homebuyers

Lending standards for first homebuyers are tight. The percentage of interest only loans that banks can issue has dropped. New borrowers hoping to get into the market might soon find it difficult to secure an interest-only loan. However, there is competition between banks for owner-occupiers with a 20% deposit, because they are seen as a safer risk.

In a declining market, there's less FOMO pressure; first homebuyers can wait until they find the right home. First homebuyers need to make sure they have a big enough deposit and can afford repayments if interest rates rise. There is a risk of buying in a falling market and going into negative equity. If the value of a new property drops, the mortgage might be larger than the value of the home, which means the bank might not allow the owner to renew or refinance the mortgage at the end of the term.

Some real estate commentators are predicting a 3% growth in Sydney and a 6% growth in Melbourne, and up to 16% growth in Brisbane by 2021.

Harry Dent (a US commentator who predicted the 2008 US property crash) is predicting a crash by up to 50% some time between late 2018 and early 2020. This means that for aspiring first homebuyers who are willing to wait (and take the gamble on a crash), there could be epic bargains. But at the same time, we simply don't know what would happen to Australia's economy; such a crash in the property market could cause a full-blown recession and the collapse of major banks.

For homeowners

Homeowners who are planning to stay in their home for years, and can afford their principal and interest repayments even if interest rates rise a few per cent, are probably going to be fine. Most likely, they're going to hold tight, keep paying the mortgage, and see what happens. For homeowners planning to stay in the home, they might be able to ride through the trough and sell many years down the track when the market has recovered or grown.

Homeowners looking to downsize could be in the best position of all. They have the option to sell now at close to the peak, downsize to a smaller and less expensive home, and pocket the profit. Plus, the government has a new incentive to sell; an offer for downsizers over 65 to use the proceeds of selling their home to make a once-off deposit of up to $300,000 into their superannuation. The limit is per person, which means that couples could deposit up to $600,000 from the sale of their home. The scheme offers a tax rate of 15 per cent for such deposits, which could save eligible downsizers many thousands in tax.

Homeowners looking to upsize could have plenty of large homes to choose from thanks to the downsizers' scheme above. Upsizers are going to be buying and selling in the same market. The value of their homes has seen a big increase in the last few years, so they might sell at a profit. But at the same time, the value of bigger homes has also increased by a similar amount; and many say the gap between units and houses is widening. One option for "Upsizers" is to sell now while prices are relatively high, rent for a while, wait and hope for a drop in the market, then buy a bigger home after a decline in housing prices. To make this work, housing prices would have to drop significantly to work out even; enough to cover the cost of stamp duty, rent in the interim period (which could be a few years), moving costs and other costs. It's a gamble, as is always the case in the property market, but it could pay off for Upsizers if they get lucky with selling at a peak and buying in a trough.

For investors

Investors with fully-owned rental properties may be in a stable position. Victorian rental vacancy rates are low at 1.9% in Melbourne and 1.6% in Regional Victoria. This is good for investors because a low vacancy rate often means that rental competition is higher, which drives up median rental prices. However, in Sydney, rental vacancies are at 2.8%, a 13-year high, which could be bad news for Sydney investors who rely on high rental return to pay their mortgages.

Investors with properties on interest-only loans or high levels of debt might have taken on loans hoping for their properties to continue increasing in value. They might find they are not able to refinance their loans at an affordable rate, or that the rental income doesn't cover their new repayments. At this point, investors might choose to sell.

Investors looking to buy may find it more difficult to get a loan, after investor loan approvals have fallen by 29.7% from their peak . However, investors could be in a good position if they have high available equity or plenty of available cash to buy an investment property. If market values drop over the next few years, cashed-up investors could snag a bargain in a pricing trough.

Discover how Next Address can help you choose the best way to sell your home.

If you're keen to understand all the pros and cons of selling your home, and increase your chances of a positive experience and result, join our mailing lists.

Disclaimer: Any information contained in this blog post is general, and not to be considered financial advice. Do your own research on Australia's financial and housing trends. Speak to your financial advisor and mortgage lender before making any decisions about keeping, buying or selling a property.

https://nextaddress.com.au/blog/rba-leaves-interest-rates-on-hold-august-2018