

# Banking on Capital



**Actuaries  
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**30 August 2016 • Sydney**





National  
Australia  
Bank

Presentation to Actuaries Institute  
“Banking on Capital Conference”

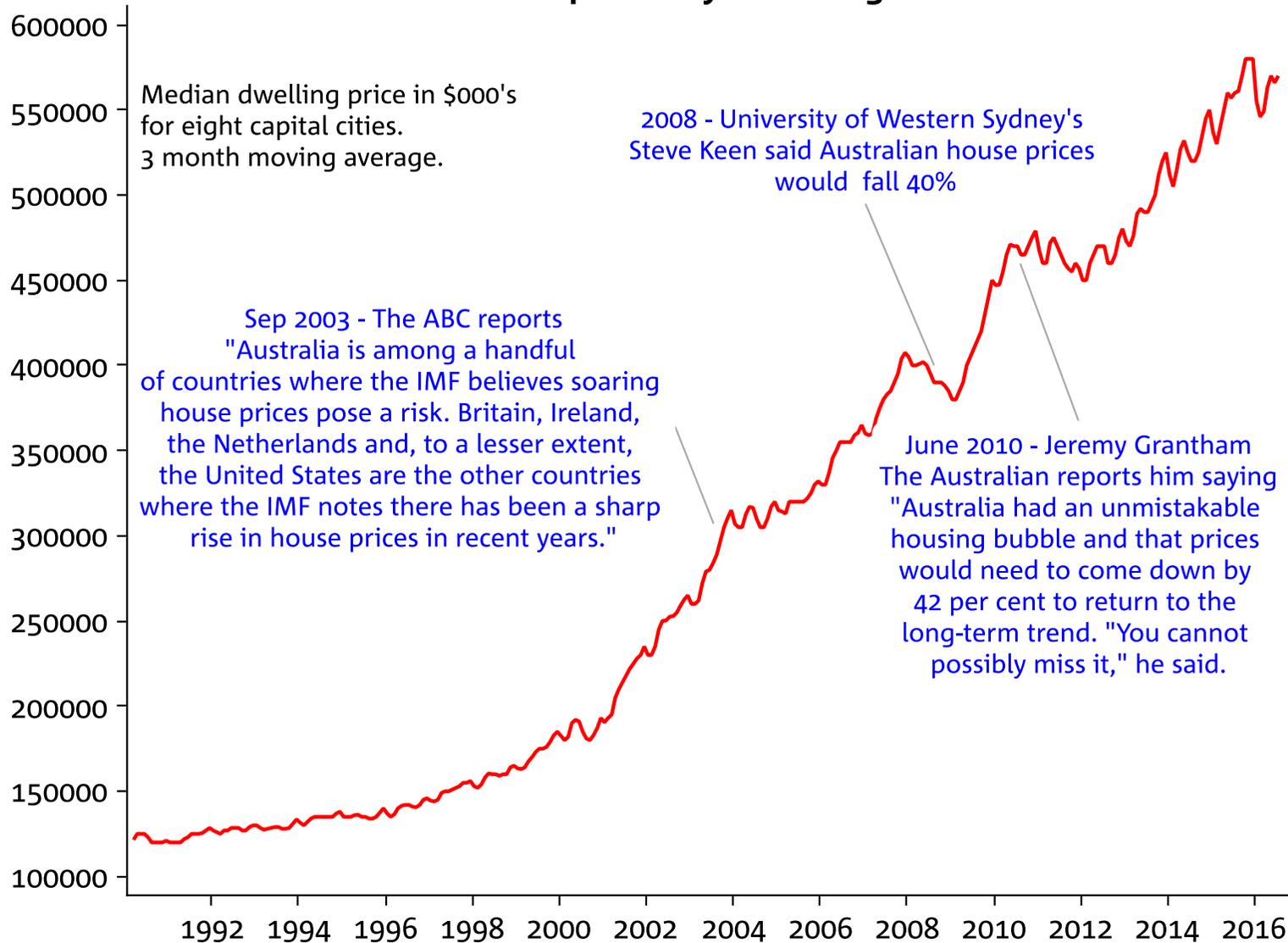
## Comments on Australia’s Housing Market

Peter Jolly, Global Head of Research  
September 2016



# Australia's housing doomsayers -

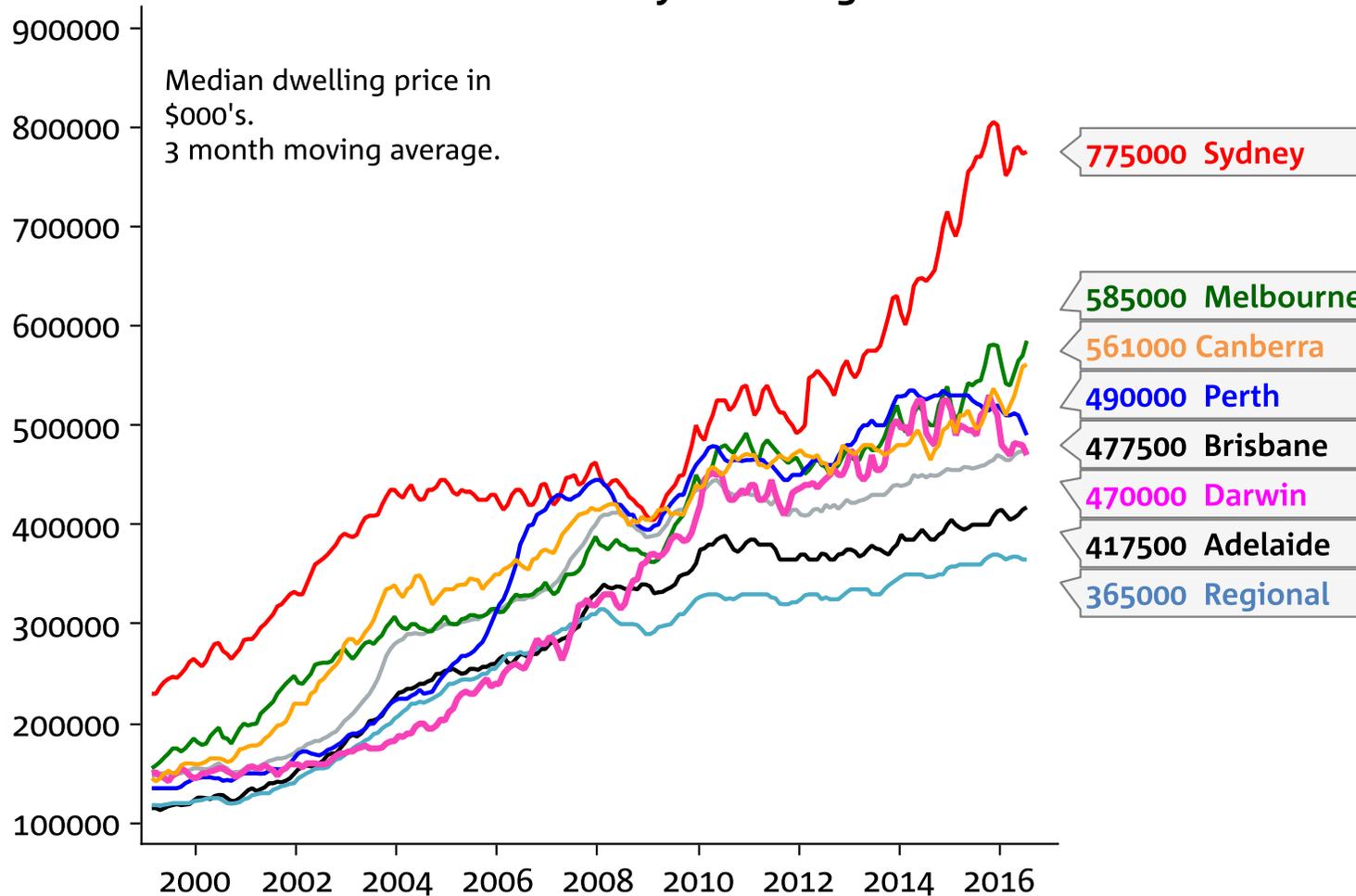
## Australian Capital City Dwelling Prices



Source: National Australia Bank, Macrobond

# Point 1: It is not a single housing market in Australia – Perth/Darwin prices falling.

## Australian City Dwelling Prices

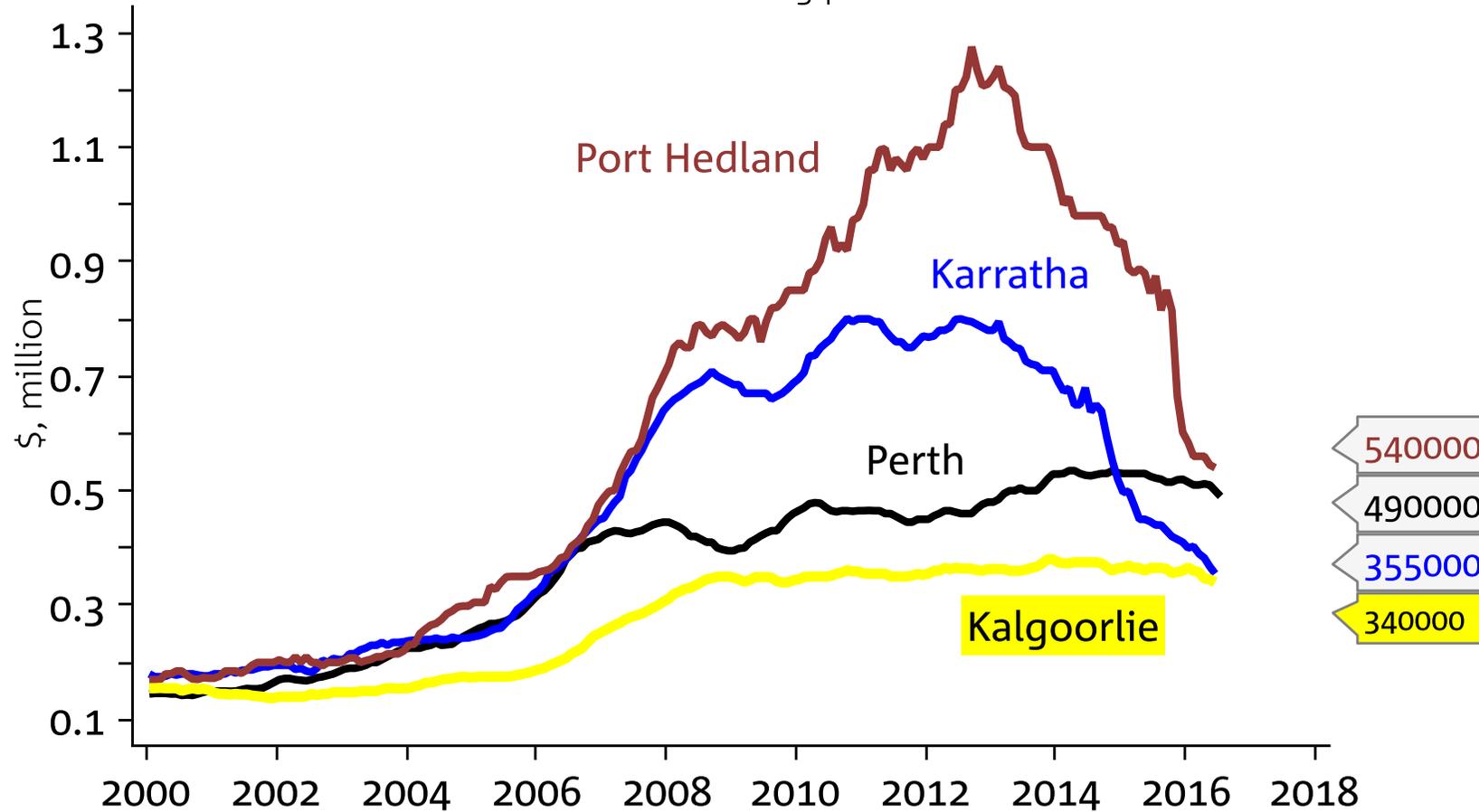


Source: National Australia Bank, Macrobond

- prices have fallen sharply in the mining towns where supply outstrips demand

## Resource town prices - WA

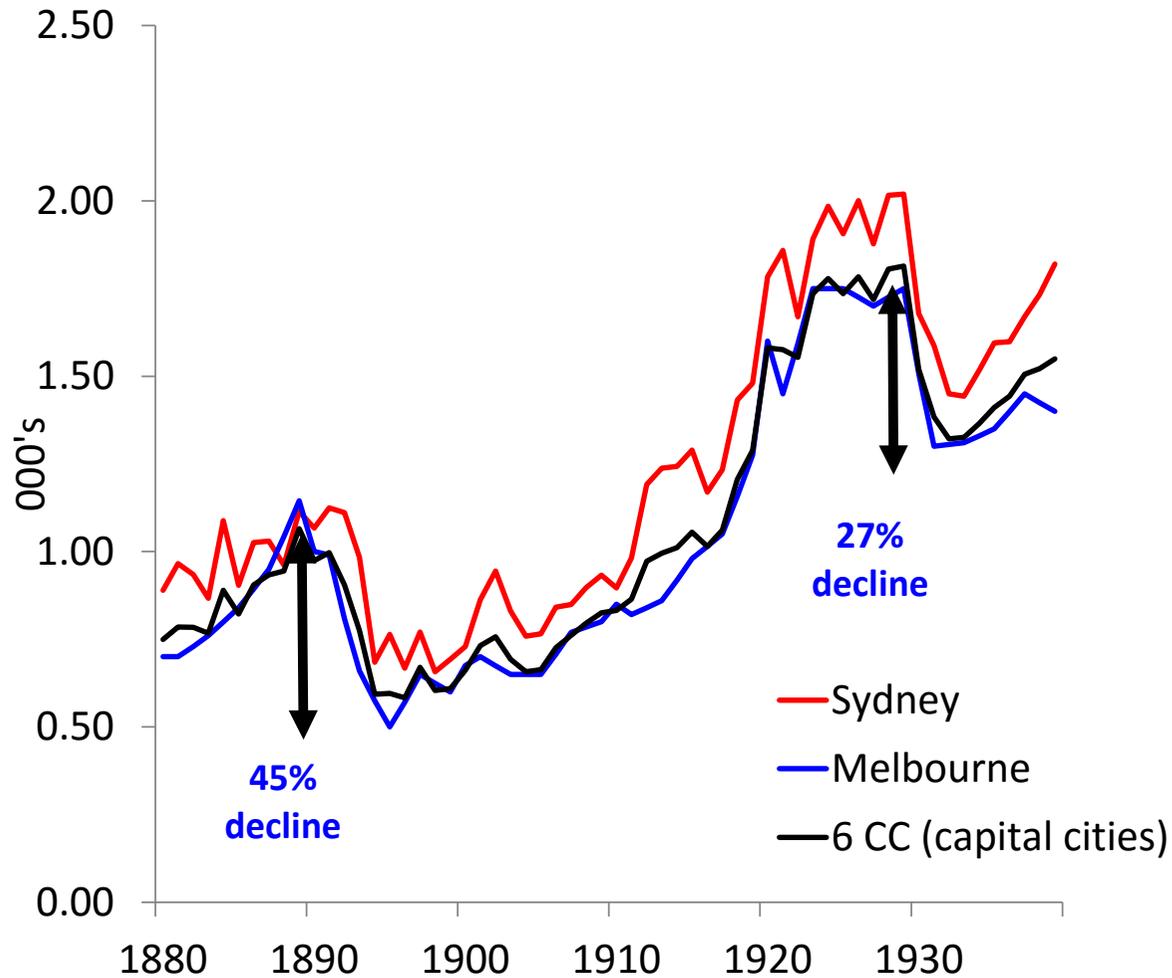
Median selling prices



Source: National Australia Bank, Macrobond

## Point 2: Australia's capital cities are not "special" and have had bubbles in the past!

### Australian Dwelling Prices a Century Ago



Source: Nigel Stapeldon

#### The 1890's Melbourne boom driven by:

- 1) rapid population growth - Greater Melbourne rose by more than 70 per cent from 283,000 in 1881 to 491,000
- 2) Stockmarket boom - '... Its most sensational phases were the speculative dealings of the big men in city land and in mining and "investment" shares'.

"The crash began in 1891. Land values fell to levels around one half their boom levels.

#### *The exact trigger for the crash is unclear...*

...Nonetheless, its general nature is fairly clear.

From the end of 1887 many reputable banks restricted their lending for land purchase substantially....

...fundamental factors were beginning to affect the bubble. The huge amount of land that had been brought onto the market meant that rental yields were depressed.

Furthermore, the low rental yields combined with high leverage meant that speculators were experiencing increasing cash flow problems."

Source: "Three Australian Asset-price Bubbles", John Simon, RBA Conference, 2003.

# What is an asset bubble?

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**Charles Kindleberger**<sup>1</sup>, of “Manias, Panics, and Crashes: A History of Financial Crises” fame said in 1987

*“A bubble may be defined loosely as a sharp rise in price of an asset or a range of assets in a continuous process, with the initial rise generating expectations of further rises and attracting new **buyers—generally speculators interested in profits** from trading rather than in its use or earning capacity.”*

In their book “This Time its Different”, **Reinhart and Rogoff** noted

*“If there is one common theme to the vast range of crises we consider in this book, it is **that excessive debt accumulation**, whether it be by the government, banks, corporations, or consumers, often poses greater systemic risks than it seems during a boom.”*

**Glenn Stevens** ever usefully concurs<sup>2</sup>

*“It is not so much the asset prices, in my view. It is the debt; it is the leverage behind it. My guess is that if you have an asset bubble in, say, some new exotic art, and there is no borrowing, it is not going to do a lot of damage to the economy.”*

A few weeks ago in the WSJ he expanded “You care, of course, whether asset prices seem divorced from their fundamentals. That’s often in the eye of the beholder. But the thing you most care about is if there is a lot of borrowed money behind the assets”.

1. in the New Palgrave: A Dictionary of Economics, 1987

2. RBA Governor Glenn Stevens, FRIDAY, 20 FEBRUARY 2009 and then again in an interview with the WSJ, August 17 2016.

## A more useful definition of “Toil and Trouble”

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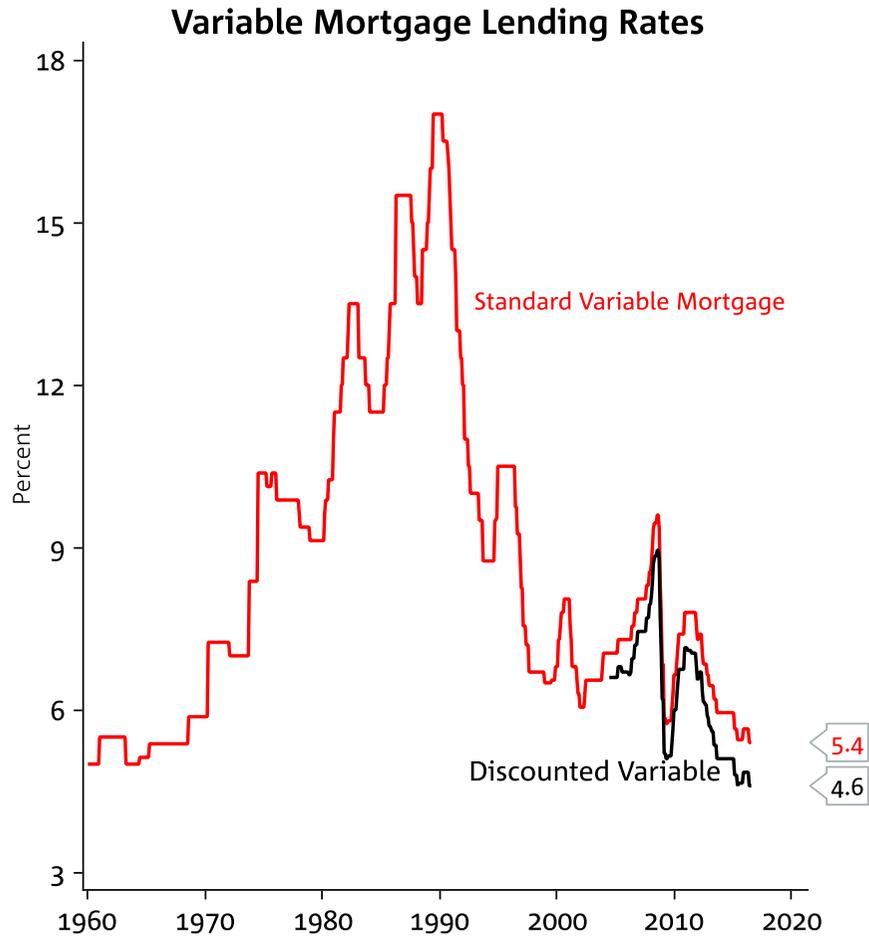
1. An sharp rise in an assets price to above its fundamental value
  - For housing, factors to consider include: demand/population, supply of dwellings, valuations, mortgage rates.
2. Driven by excessive debt accumulation with poor lending standards
  - Factors to consider include: credit growth; bank lending standards, household financial health, including employment and income growth.

## What has driven dwelling prices higher in Australia recently?

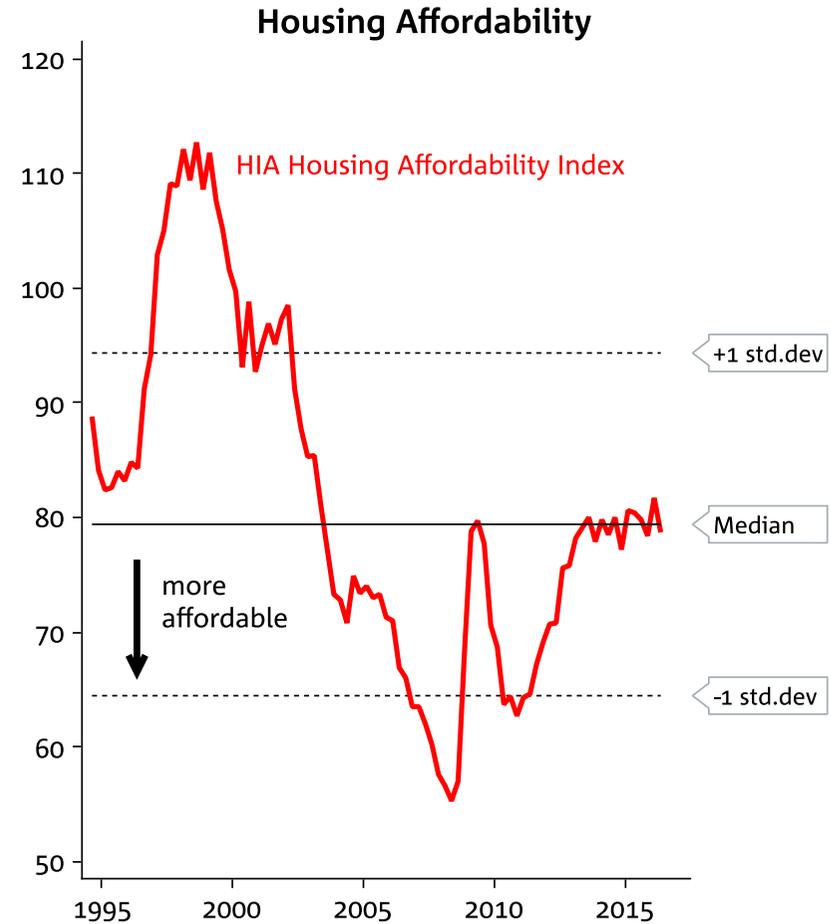
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1. Low mortgage rates and improved affordability
2. Foreign Demand
3. Population growth had previously outstripped supply of dwellings – less true now

# Mortgage rates lowest ever helping to keep affordability around average



Source: National Australia Bank, Macrobond

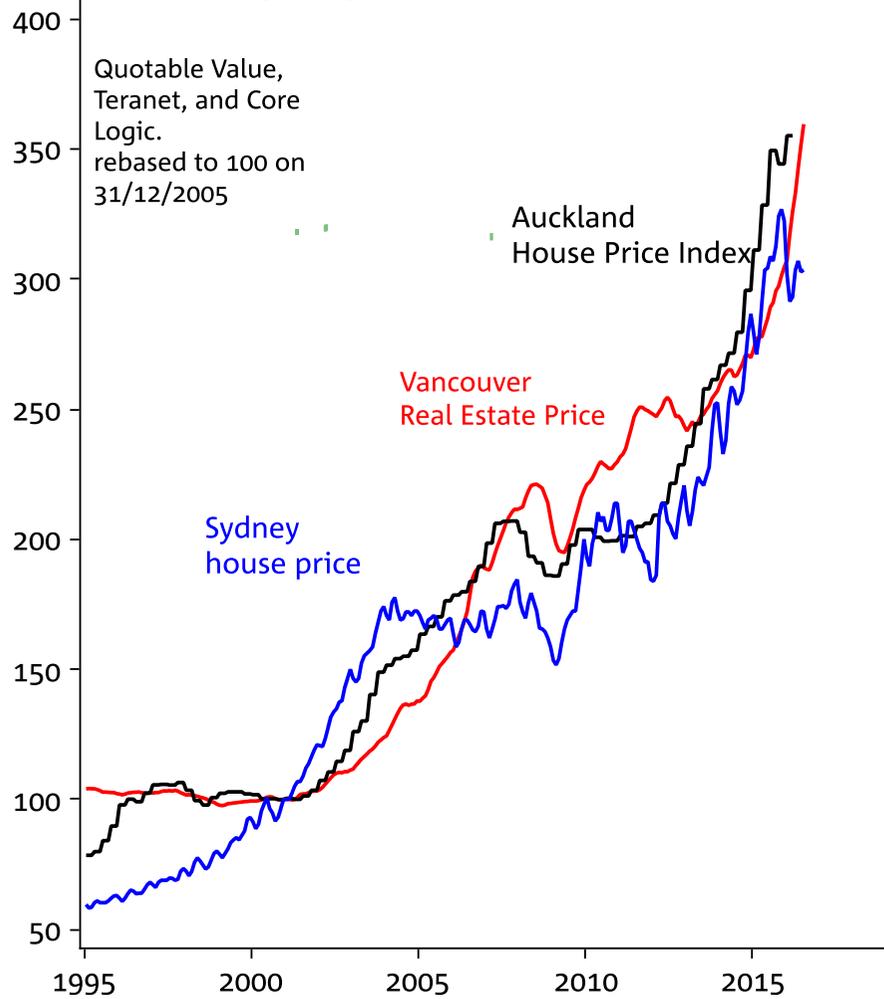


Source: National Australia Bank, Macrobond

The HIA affordability index uses median house prices, median income and mortgage rates

# Countries favoured by Chinese buyers – Cities on the Pacific Ocean.

## Auckland, Sydney, and Vancouver House Prices



Source: National Australia Bank, Macrobond

## Top 10 Countries for Chinese Buyers

#	BY VIEW	BY ENQUIRY
1	US	US
2	Australia	Australia
3	Canada	Canada
4	New Zealand	New Zealand
5	Thailand	Thailand
6	UK	UK
7	Japan	Japan
8	Spain	Spain
9	France	Singapore
10	Singapore	Germany

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Source: Juwai Data, Q1 2016

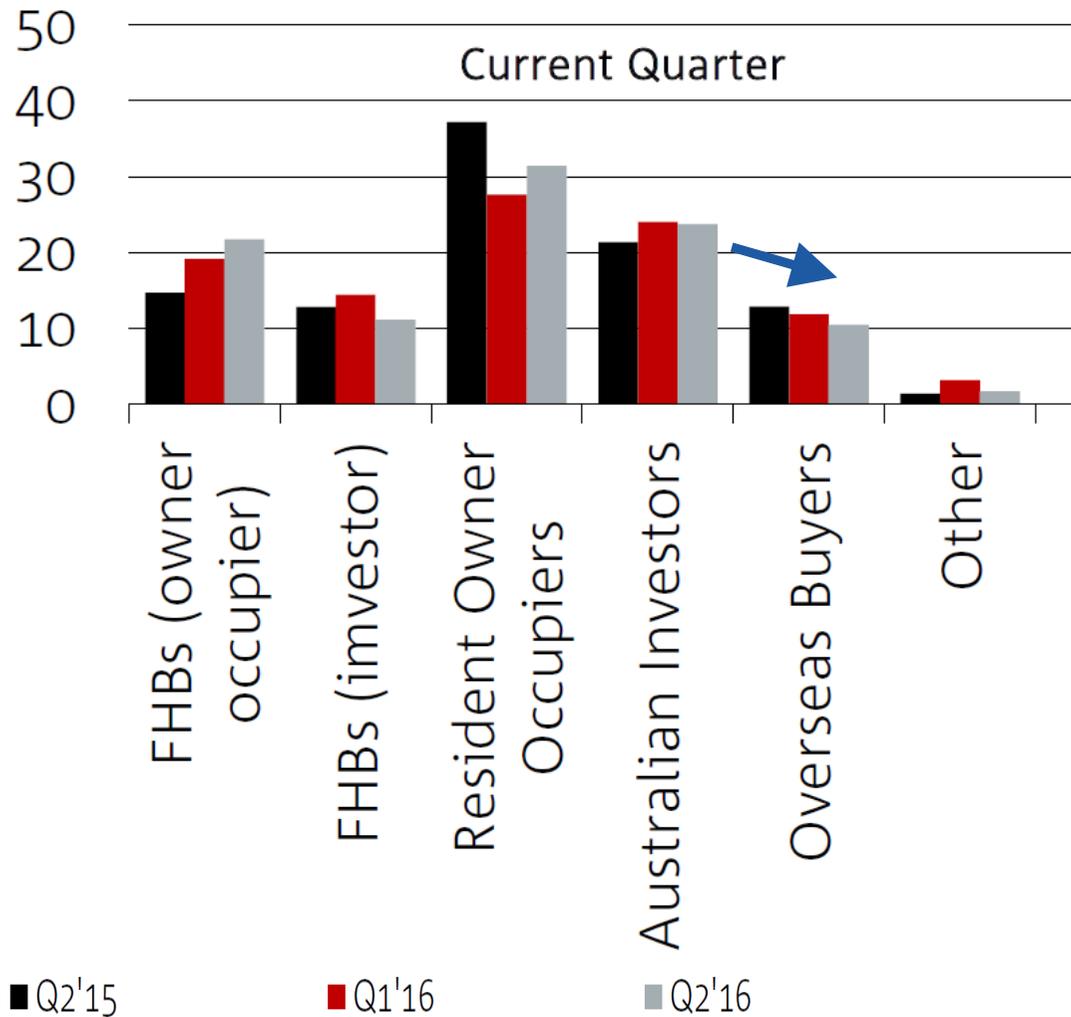
## Top 10 Australian Cities Viewed by Chinese Buyers

- 1 MELBOURNE
- 2 SYDNEY
- 3 BRISBANE
- 4 ADELAIDE
- 5 PERTH
- 6 GOLD COAST
- 7 CANBERRA
- 8 CAIRNS
- 9 NEWCASTLE
- 10 AIRLIE BEACH

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Source: Juwai Data, Q1 2016

## Foreign demand for residential property now slowing

### Share of Buyers for New Developments



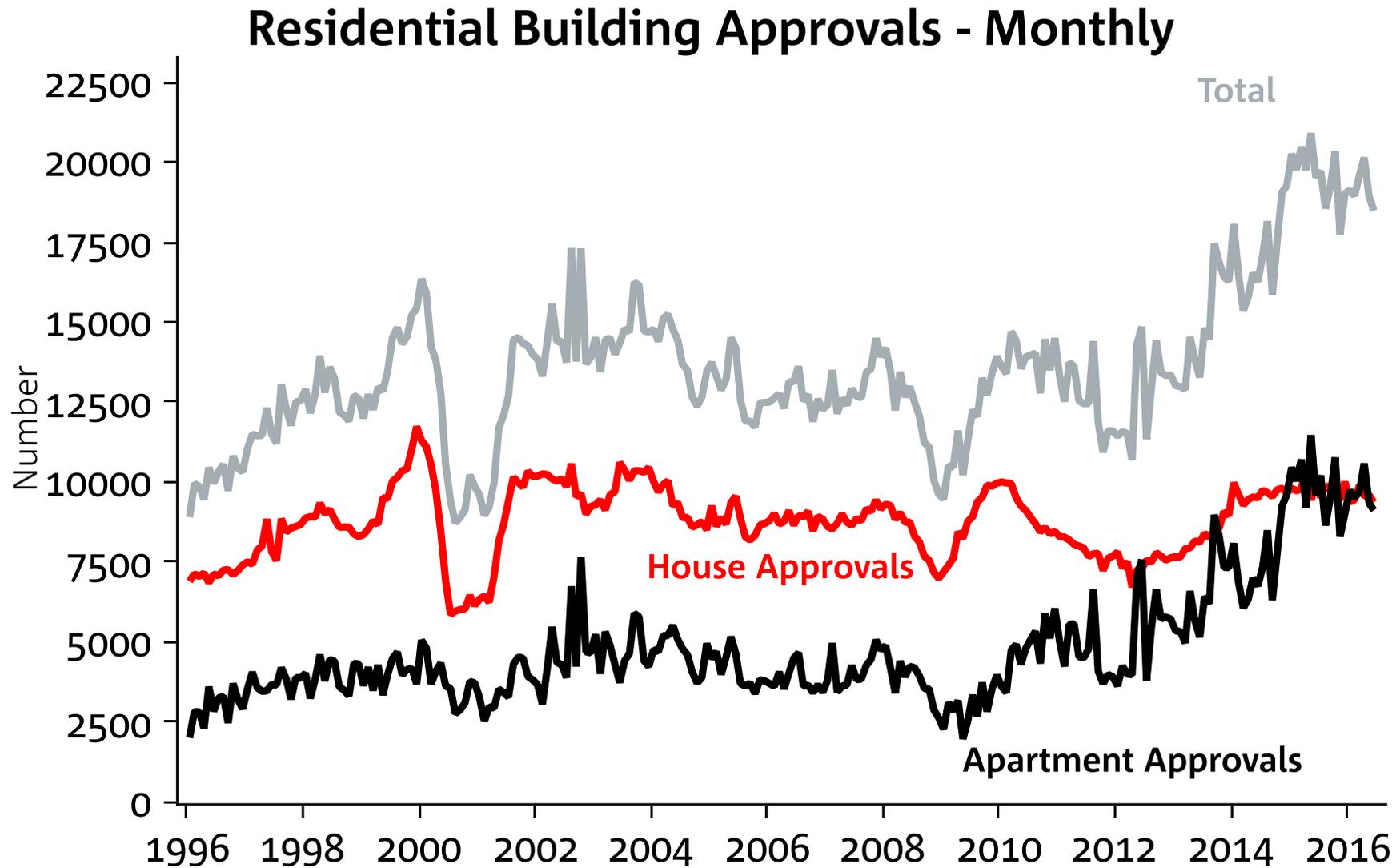
Commonwealth Government is administering foreign buying rules more strictly – foreigners can only buy new dwellings

A number of banks no longer provide mortgages to foreign buyers

State Governments “cashing in” on foreign buyers with extra stamp duties for foreigners, 0.5-1.5% absentee surcharge in Victoria and a 0.75% land surcharge in NSW

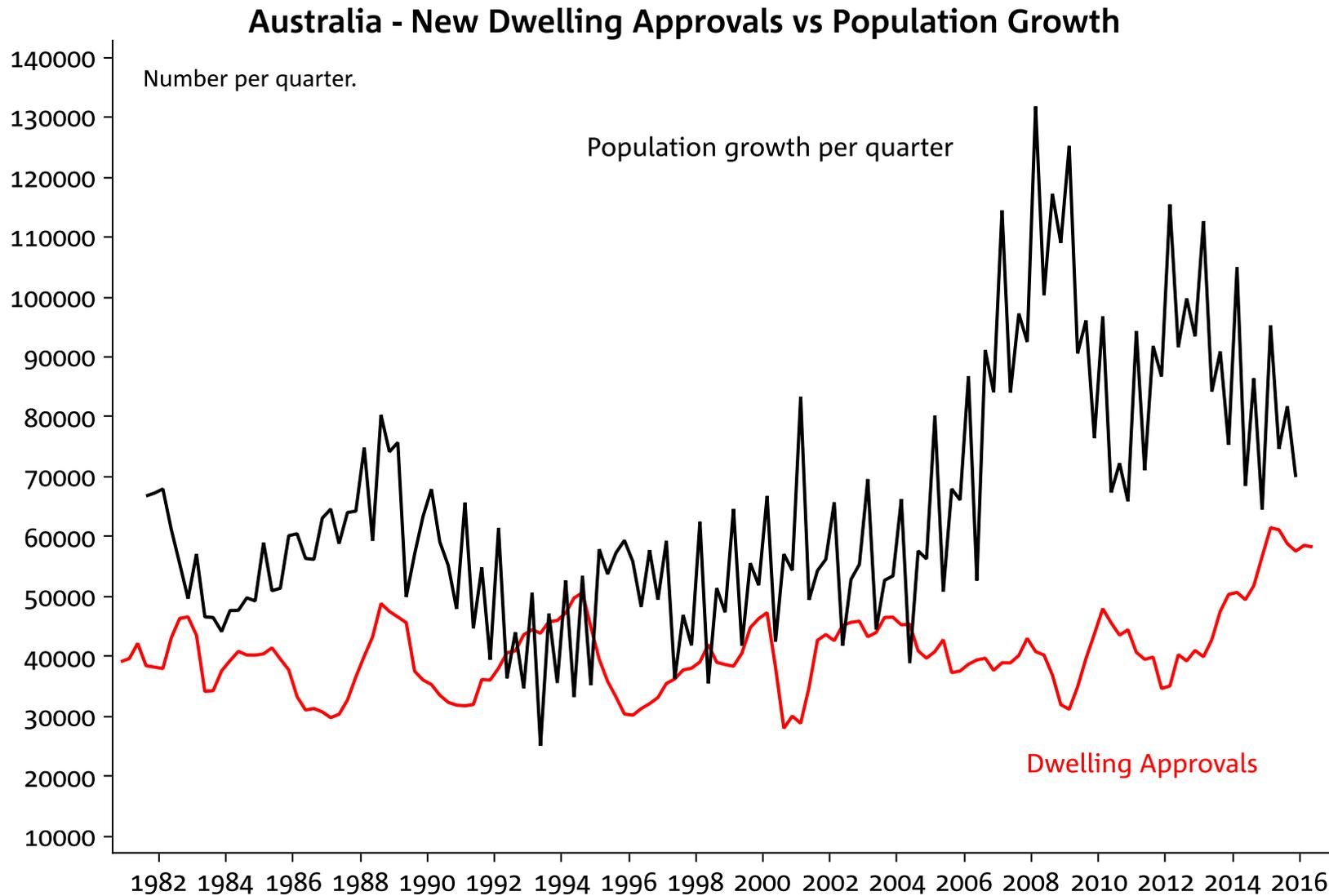
Source: NAB Residential Property Survey

There has been a significant lift in supply of dwellings - especially of apartments.



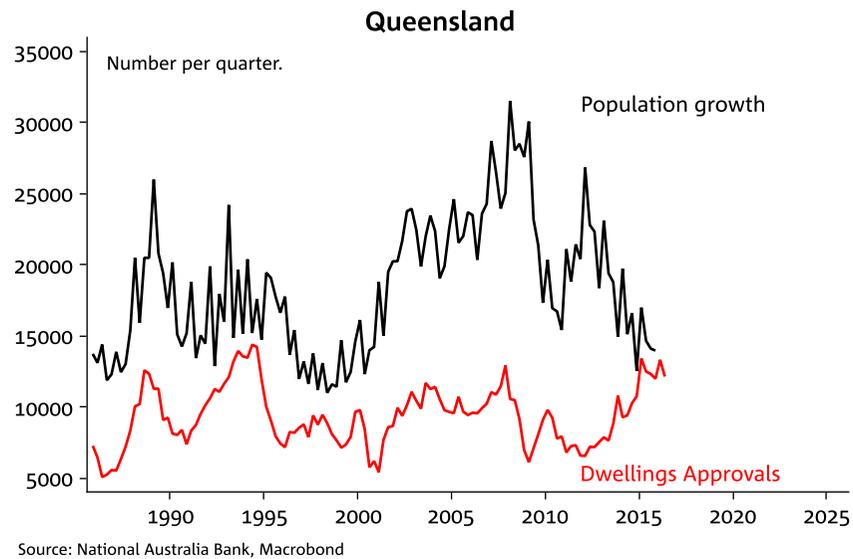
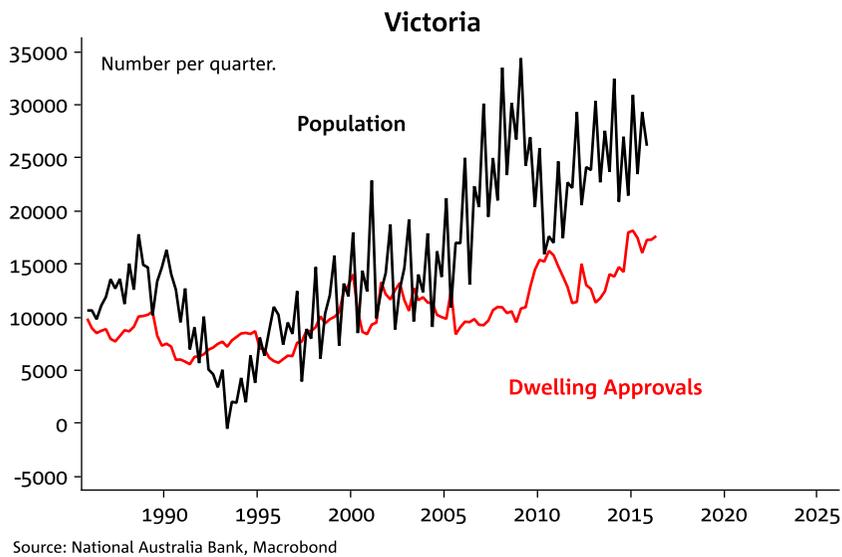
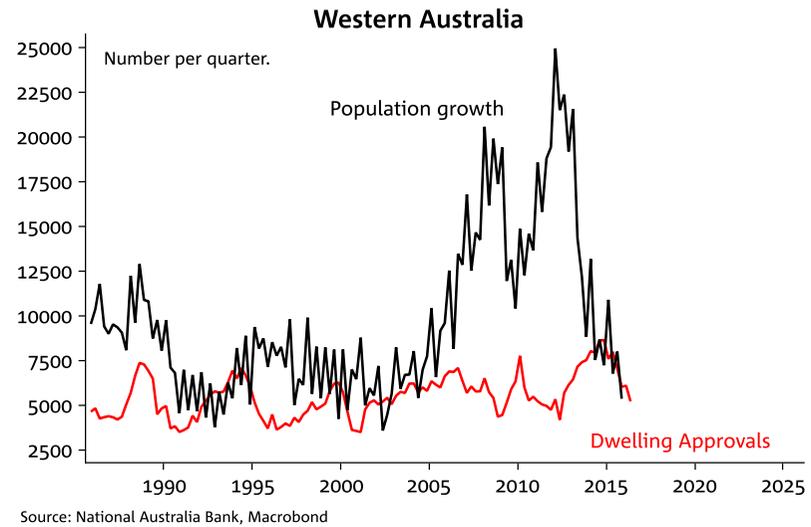
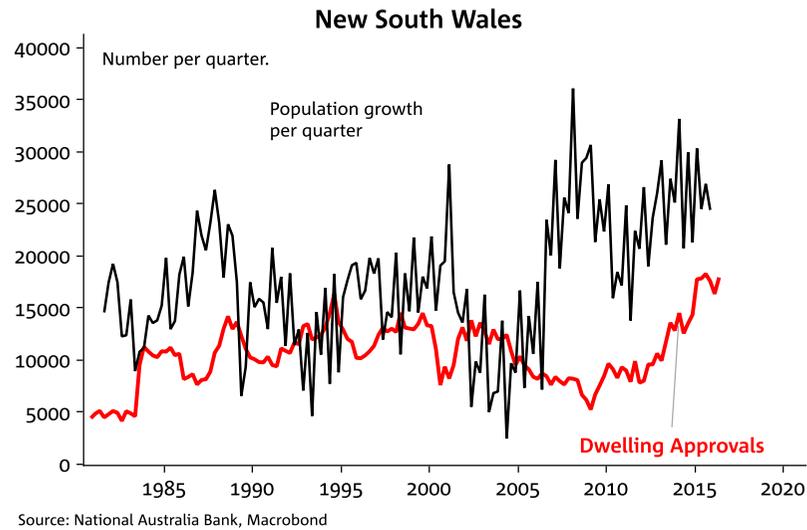
Source: National Australia Bank, Macrobond

# Dwelling supply and demand nearing balance



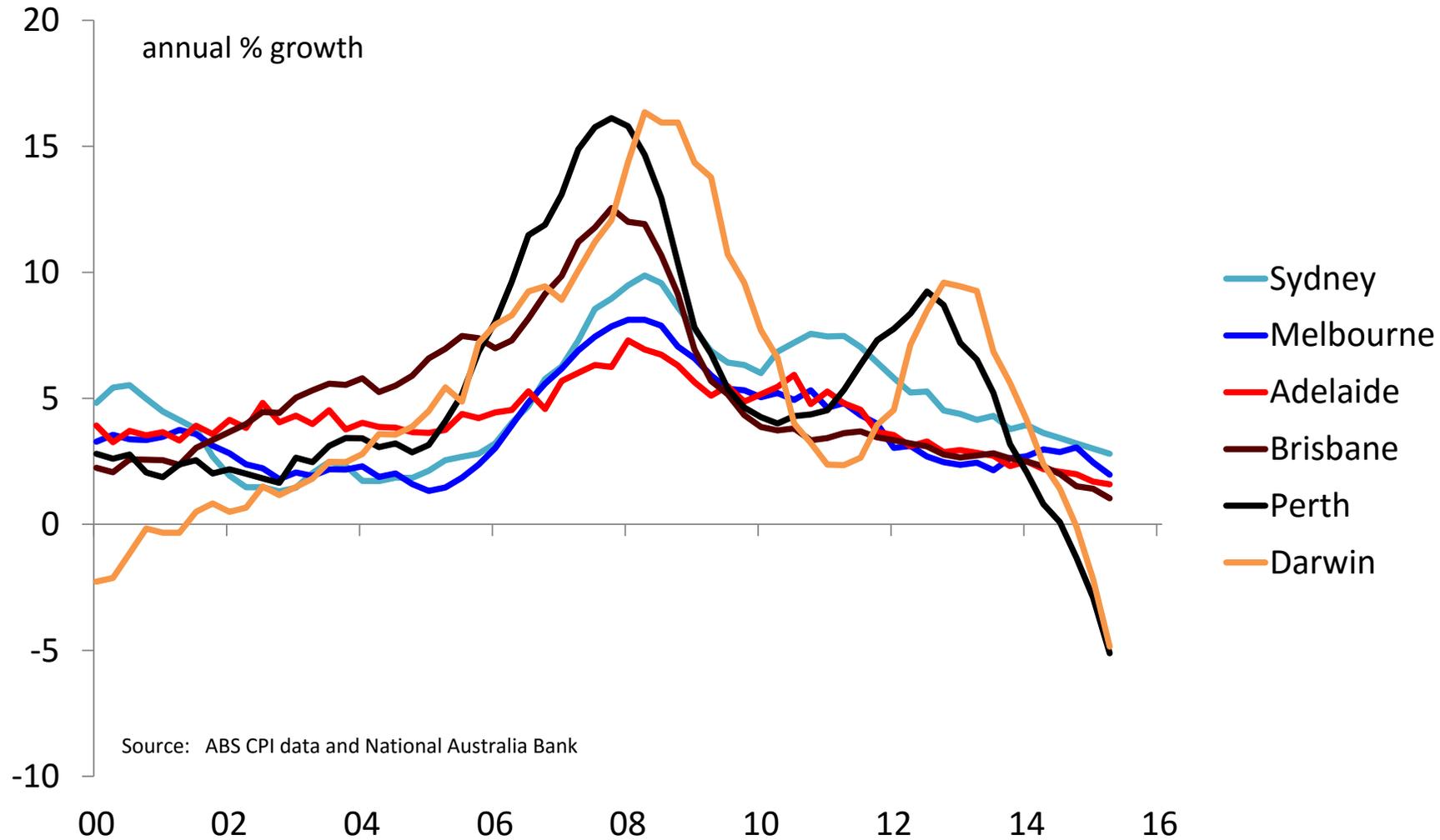
Source: National Australia Bank, Macrobond

# Supply-demand gap by State – NSW and Victoria OK. Over-supply in WA and QLD.

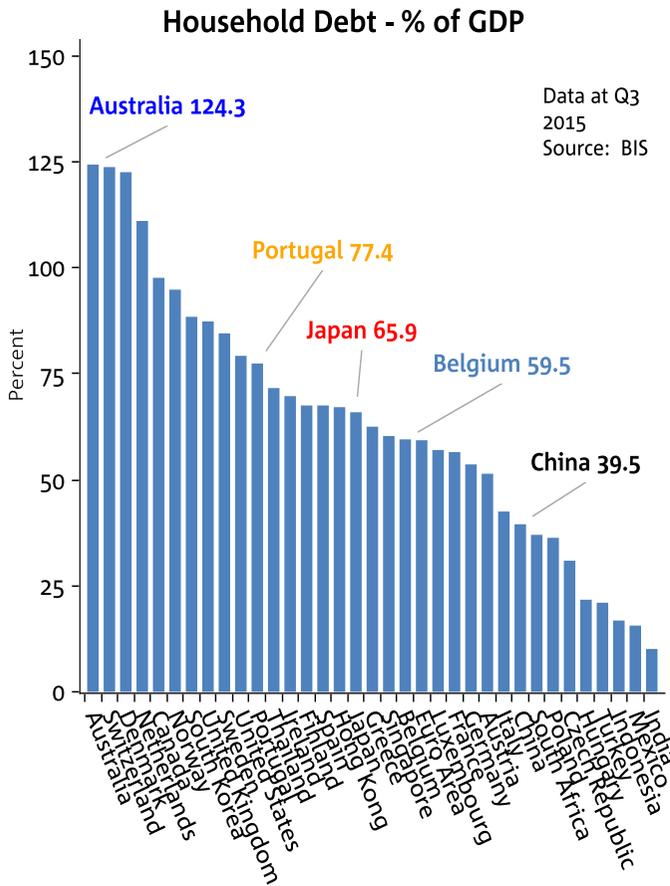


Rental growth slowing most places – a clear sign that supply has caught demand.

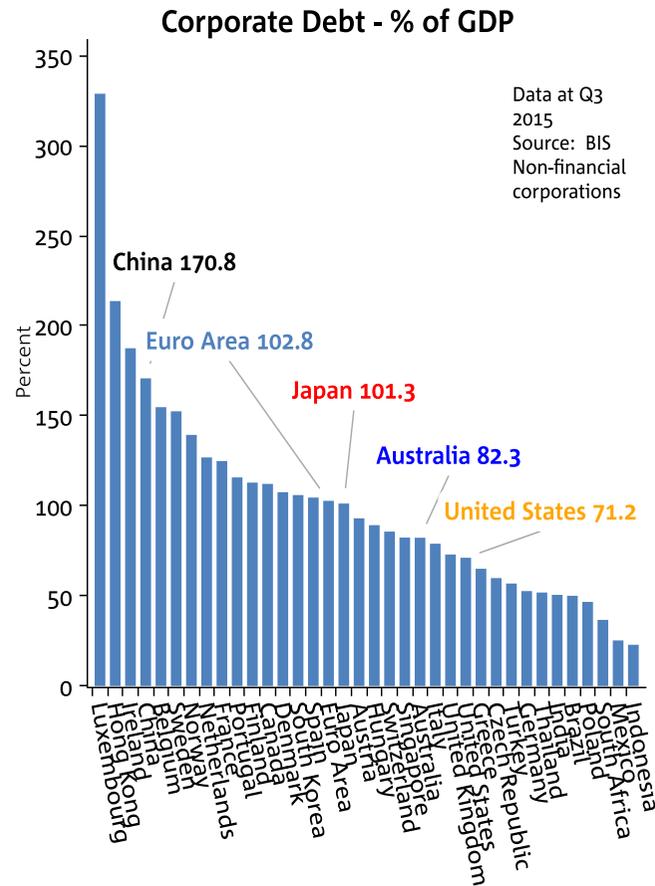
## Residential rents by city



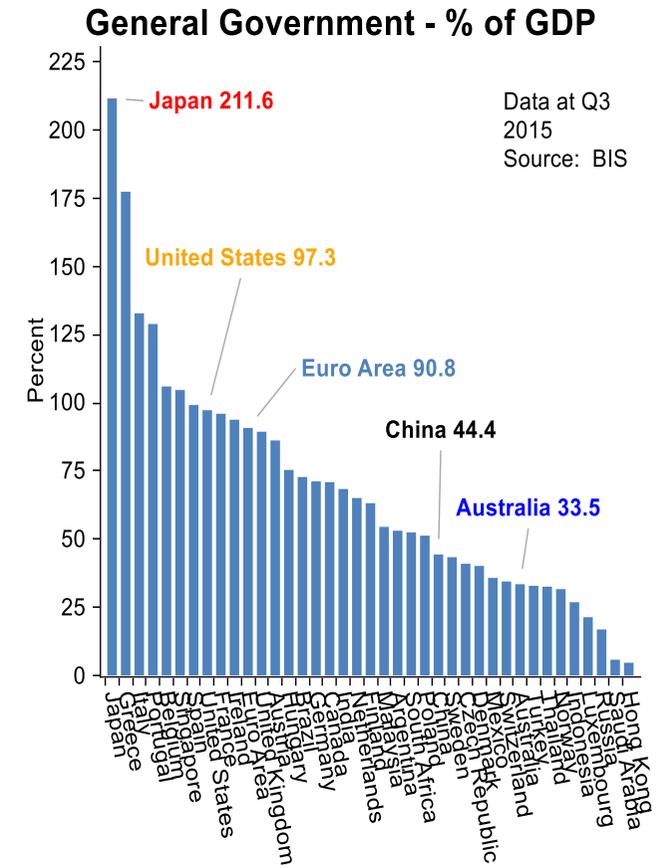
# Financial health: Australia's household debt is high which makes them vulnerable to a shock. In comparison, corporate and government debt is modest.



Source: National Australia Bank, Macrobond



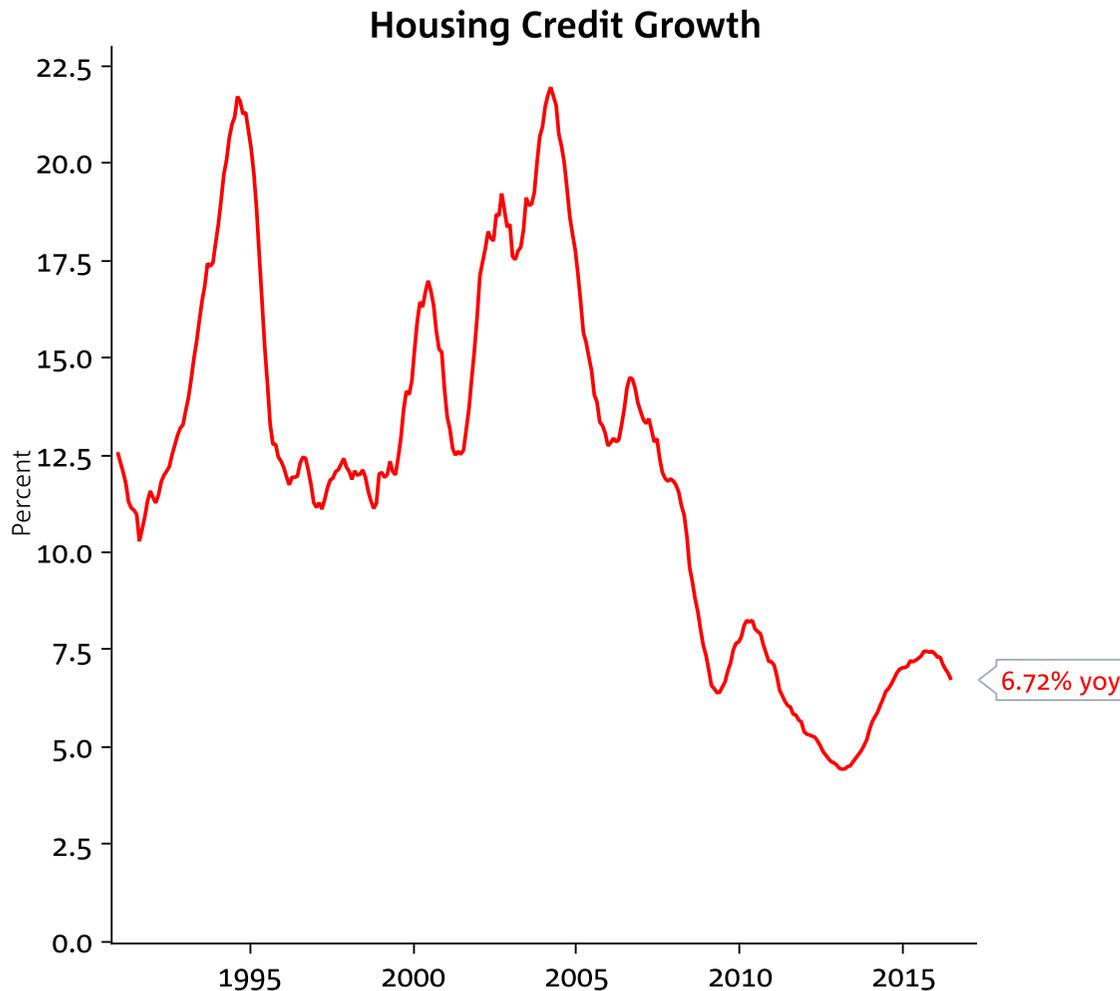
Source: National Australia Bank, Macrobond



Source: National Australia Bank, Macrobond, BIS.  
Includes central, state and local government debt.



Even so, mortgage credit growth remains modest overall and mortgage lending standards for ADI's were tightened from late 2014 .



Source: National Australia Bank, Macrobond, RBA.

**9 Dec 2014**  
**APRA outlines further steps to reinforce sound residential mortgage lending practices**

“In the context of historically low interest rates, high levels of household debt, strong competition in the housing market and accelerating credit growth, APRA has indicated it will be further increasing the level of supervisory oversight on mortgage lending in the period ahead.”

## Conclusion - Housing to cool appreciably and Units to fall in price

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- Low mortgage rates, foreign demand and a slow supply-side response all supported higher dwelling prices in some Australian cities in recent years
- Some of those supports have weakened:
  - prices/valuations are higher
  - The under-supply of housing has closed and in some markets is entering over-supply.
- At the same time, mortgages lending standards have tightened

### **NAB's view on housing**

- Our expectation is that the housing market will cool appreciably
- National house price growth of 0.5% is expected in 2017.
- Unit price are expected to decline of nearly 2% over 2017 – more where over-supply is acute.
- We continue to hold the view that residential property prices are unlikely to experience a severe 'correction' without a trigger from a shock.

## NAB House/Unit Price Forecasts – y/y%.

Hedonic House Prices							
	2011	2012	2013	2014	2015	2016f	2017f
Capital City Average	-4.0	-0.5	9.9	8.4	7.8	5.1	0.5
Sydney	-2.6	1.3	15.2	13.4	11.5	8.6	0.2
Melbourne	-4.4	-2.9	8.5	8.4	11.7	6.1	0.4
Brisbane	-7.0	-0.5	5.3	5.2	4.3	4.0	1.9
Adelaide	-3.8	-0.8	3.0	4.5	-0.3	3.5	1.7
Perth	-3.4	0.6	10.2	2.1	-3.8	-5.5	-3.5
Hobart	-8.8	-0.5	2.9	3.3	-1.6	8.5	1.7

Hedonic Unit Prices							
	2011	2012	2013	2014	2015	2016f	2017f
Capital City Average	-2.6	0.5	9.0	5.1	7.9	3.6	-1.9
Sydney	-1.3	2.3	11.6	8.3	11.3	7.2	-1.5
Melbourne	-3.2	-2.5	8.7	1.1	6.9	0.6	-3.5
Brisbane	-2.0	-3.5	3.5	1.2	1.8	1.7	-1.8
Adelaide	-8.0	-0.5	0.6	2.5	1.4	0.2	0.5
Perth	-5.4	3.3	6.3	1.9	-3.5	-7.2	-5.0
Hobart	-5.6	4.2	-5.1	5.9	8.6	9.0	0.6

SOURCE: CoreLogic; NAB Economics

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