HOME TRUTH

JULY 2016

Welcome to HOME TRUTH, a monthly synopsis of Brisbane's quality property sales and leasing markets. Beyond our usual content, this edition in our Election Observation we look at what the outcome will mean for property markets.

The Brexit vote and our own political mess shows just how right Churchill was in saying 'Democracy is the worst form of government, except for all the rest'. Einstein was equally prescient with 'Only two things are infinite, the universe and human stupidity, and I'm not sure about the former'.

ELECTION OBSERVATION

'Embarrassment of choice' ruled the federal election where it seemed even having clearly scraped the very bottom of the barrel it was a struggle to find enough names to fill the new extended and very unimproved roll.

The aptly named 'toilet' roll rolled on that long (which must have cost a fortune and many forests) that many who didn't vote early and took the time to genuinely study the (lack of) form may have missed the 6pm cut off deadline.

It's length however was inversely proportional to the depth of its talent pool, so shallow was it admission of The Raving Lunatic Party may have beefed it up. Could it be given the company they were considered too mainstream?

Even taking the safest route of staying above the line, I ran out of conscionable options very early and by number six was in real trouble such that I had to settle for the lesser of many evils, someone who shall remain nameless but who possesses some rather unfortunately initials (and no, not BS) or vote informal so Derryn you owe me one.

The government of course could get rid of the loonies quickly and forever by just removing the $2.30 bounty per vote that everyone gets regardless of who from or who to. To do that though would require extricating their own snouts from the same trough, their's the biggest by sheer weight of numbers so take it that won't happen.

We do have a belated election result now, Labor quietly conceding defeat while loudly declaring themselves winners. How do you do that by the way, when you have just suffered your worst primary vote in decades (punishment for one lie or too many or perhaps just simply too many too recently - which makes you wonder what the magic number is that tips one into pathological territory).

The coalition may have won more at this election than they realise because despite Labors poor showing, the union heavies want their man to stay leader and what they say goes. Under policy introduced to try to limit Labor's endemic self-harm, it has only a few more days to sack him before he becomes untouchable right through til the next election.

Not wanting to get too political (though accepting [even though many won't] that political fortunes dictate economic fortunes dictate property fortunes which is why we can't ignore the subject however worthy it is of such ignorance), spare a thought for your average Jo on Struggle Street this election who due to poor communication felt the choice was between privilege, poison, protectionism or plain pottiness. Little wonder so many went potty!

With that off my chest, what does the election outcome mean for the property market?.

Well first (second and third) and foremost, the result means the wholesale deconstruction of negative gearing (and therein the deconstruction of property values as well as the jobs of 100,000's of construction or construction allied workers) is off the radar, at least for now (and probably for much longer if anyone is smart).

From purely property and economic perspectives, the result means that the country has dodged a very large bullet, and more than just an early return to traditional Labor anarchy which while always harmful to the economic fortunes of the country, is always entertaining and very financial rewarding for those for whom money genuinely has no smell.

Whilst we may never know just how costly to property values, construction industry jobs, and to the country as a whole Labor's platform re-election policy of removing the three decade old tax advantage of Negative Gearing from more than 95% of properties and 100% of other investments that currently apply might have been, we can be confident given it proved such an electoral disaster that it will likely be abandoned forever (of course without anyone admitting what a monumental blunder it was) and it will be a 'brave' party that chooses to take that cudgel up again.

As we have stated previously, whilst we don't hold a position on whether or not the introduction of negative gearing was a good thing, we hold a very clear position given how dependant upon it this nation has become over its 30 plus years, that getting rid of it in part or in full, instantly or progressively, would be a very bad thing.

Not only does it hold up the property market, it has become the very foundation for the whole construction industry which driven by negative gearing has grown to become Australia's biggest employer, responsible for 1 in 4 jobs.

So tax incentivised property investment is to continue and will therein continue to shore up existing property values.

But it won't be the same, or at least the effects over the next 30 years will be very different from those of the last.

That is because we have now (reluctantly in the case of the RBA) entered the ultra-low inflation and interest rate environment or age that has been the norm for the rest of the developed world for some time and we expect ours too to be far more than a temporary visit with 10 Year Bank Bill Swap Rates now at a historic low 2%, still higher than our trading partners but the prognosis from here is clearly more down than up.

Whilst the extent of tax breaks provided by negative gearing vary with people's individual circumstances, generally they diminish as interest rates fall.

More generally, a more strategically visioned and investment friendly government will also soften the threatened oversupply driven price slide in investment apartment product (whose prices would have been quite literally smashed to smitherines had Labor had its way).

The property market not unlike the country overall will benefit from a further period of stability but it's not going to be plain sailing by any stretch of the imagination. Whilst Australia still boasts many of the fundamentals that have made it the envy of the rest of the world for most of the last 100 years (and not just those in the ground), our fortunes are today interwoven and therefore subject to those of China, our biggest export market. and through China to the EU (China's biggest customer) and therein everything that becomes of Brexit.

There will of course be any number of other curve balls.

Back to the positives, the market will appreciate early positive action to reign in our debt (not that we may get to hear too much about it, if there is one thing the coalition has learned, if you are going to be economically responsible, keep it quiet – they are certainly not going to get any support for necessary spending cuts from across the chamber).

'Genuinely' skilled and otherwise appropriately credentialed migrants when looking at which country to make their future home also like the idea of responsible and stable government so expect a renewed spike in their numbers to help future demand.

MARKET BRIEF

SALES:

~ Enquiry Levels – Low
~ On Show Attendances – Low to Moderate
~ Listing Activity – Low
~ Negotiating Activity – Low to Moderate
~ Conversion Index – Low to Moderate
~ Auction Success Rate – Low
~ Disparity Index* - High 15%

* The Disparity Index is the general difference between what buyers and sellers feel property is currently worth

LEASING:

~ Enquiry Levels – Moderate to High
~ Listing Activity – Low
~ Take-up Rate – Moderate

MARKET DETAIL

SALES:

The market barely broke out of a pending election induced crawl through much of June, the uncertainty of its outcome weighing heavily upon very marathon election campaign weary shoulders.

Towards the end of the month the market did get a welcome second wind (probably through the market having simply decided to get on with life regardless) but that too took a hit with the delay in declaring a clear winner.

The marathon poll slowed Auction clearance rates but as we belatedly emerge from the other side of what has been a particularly disruptive market disruption, expect the pent up demand from it to cause the market to bounce back with vigour. It certainly won't wait for Spring to do so, at least not in Brisbane.

Last month's picture here was mirrored in capital cities which also experienced markets that slowed markedly into the depths of the election campaign. They should also rebound out of it now the election is over not in the case of the colder capitals, not as lustily as we warmer souls here.

With or without the debilitating effect of the election, the mass oversupply of investment apartments is taking a toll on all markets with it now official that almost all apartments bought of the plan in eastern seabord capitals over recent years are worth less than their purchase prices, and in Melbourne's case, quite substantially less.

Sydney has shown the least apartment price softness of all the capitals registering only single digit percentage losses. Brisbane hasn't fared quite as well as Sydney but far better than Melbourne though it is worth remembering that we are further back in the supply pipeline than they so there may be further disappointment down the track yet.

The Brexit happened as we know despite the bookies giving it odds of 8:1 against, odds ironically very similar to those of a political change here. I will leave it up to your political persuasion to determine who was the smarter.

As won't surprise some, there was a palpable stunned disbelief by the outcome of the poll mixed with a certain regret among more than a few that they may have acted hastily as they wonder where to from here. More on that below.

Still overseas but more oriental, contrary to what you may be hearing (or reading), the mainland Chinese continue to shun our property like the plague. There are several contributing factors to this major rebalancing of the market which we also expand on below.

Benchmark interest rates remained on hold as expected for a country in election mode (limbo). The pause though is only temporary. As we have been confidently predicting now for several years since it became obvious to us (and I would have thought to Blind Freddy) just how big an economic hole 'we' (meaning incompetent government) had dug for ourselves, we are heading for zero or lower benchmark interest rates.

In confirmation of that now almost certainty, over recent day the 10 year Bank Bill Swap Rate (BBSW) hit a record 10 year low of just 2.07%, this some 66% (or 2/3) down from where it was in 2011 (just 5 year's ago).

The economy could do with some stimulation so we live in hope that once the electoral dust settles, the government stops trying to fool the fools and states publicly and emphatically just how much of an economic mess we really are in. That will free the RBA up to do what it should have done 4 years ago and cut interest rates to zero sooner rather than later (assuming they can temper their view on whether average Australia can be trusted with 0% rates).

LEASING:

Unlike the sales market, the federal election didn't lay a glove on the leasing market.

Generally the market hasn't just continued as normal throughout the campaign, it has done so through winter which is quite unseasonal, at a pace that we would more normally associate more with the the low shoulder leasing months of Spring and Autumn than with the depths of winter itself.

Where we are now seeing clear softness however is at the very upper end of the leasing market, in the $1,500 - $3,000 pw market, where prolonged economic sufferance is starting to take a toll on people's paying capacity.

Whilst the effect is being tempered somewhat by the strength of the economic downturn driven tendency over recent years to lease rather than to buy, cash is more king today than it has been for decades.

We are still waiting for the apartment supply tsunami to hit. We can see it on the horizon but it is moving very slowly (but ominously and inexorably).

PROPERTY ECONOMICS

HOMEFILE – We have a new government which is largely the same as the old one (albeit I suspect one a bit wiser).

The HOUSING HOLOCAUST (and construction industry implosion etc) that would have been consequent to Labor's planned wholesale deconstruction of negative gearing is not going to happen, nor too so soon a repeat of Labor's signature administrative anarchy (as exciting [and financially rewarding for insiders] as such total disarray can be).

This will be received well by a property market severely tested by both a seasonal downturn and from more of an investment perspective being besieged by APRA's unprecedented market intervention requiring banks to keep more capital in reserves that caused them to firstly greatly tighten up their lending criteria and then to stop recognising overseas income in assessing suitability to lend to Chinese wanting to purchase Australian property the effect of which has been to virtually wipe that sizable sector of the market off the map.

Testament to that, a new residential tower going up just a couple of hundred metres from our central offices which had 70% presales at the end of last year (exclusively to mainland Chinese buyers) has had close to zero activity since. According to the agents representing its sale, the silence from the Chinese is deafening.

The ever resourceful Chinese have wasted no time setting up mezzanine or second tier lending facilities to fill the massive void left by the banks departure but as these are as yet largely untested nor widely known and operate at much higher interest rates than banks (because they onsell money borrowed from banks), they are proving incapable of catching or even slowing the fast falling investment apartment market (as evidenced in Melbourne's price rout – and to a lesser degree our own, and our supply hasn't peaked yet….).

A further obstacle to be put in the market's way is the recent decision by the ATO requiring all sellers of property (commercial and residential) priced $2million and over to have a tax clearance certificate in place before settlement, failing which the buyer is required to hold and thereafter remit 10% of the purchase price to the ATO. I wonder if they have been talking to APRA. More regulation, it's just what the market needs (not).

SINOFILE – As touched on above, and particularly in Queensland, the mainland Chinese that had started to have a real impact on our market are presently missing in action.

Word from on the ground in China is that they are choosing the path of least resistance and of most promise for their current investment strategy which it seems does not presently include Australian property (or at least not to the degree it did 1 or 2 years ago when they single-handedly drove the Sydney and Melbourne property markets).

We are also still reliably informed that the money printing continues at pace in country, driving up domestic inflation as well as property prices. Expect some of that to flow our way in due course.

As touched on last month, the recent decision to open up Chinese student visas to include junior schooling has given the investment property sector some much needed heart. Just how enthusiastically the Chinese embrace this major shift in policy will determine just how much of an impact on the market it makes. As an aside, the Chinese themselves see the decision as quite a landmark one, and one they are quite in favour of.

EUROFILE – The political blood-letting runs waist deep in the old dart following the Brexit vote (boosted latterly by the exit of key Brexit protagonist Nigel Farage who has bolted for the same door as Boris Johnson though in this case seemingly on his own volition) but the economic fallout and flow on impact on property will take a lot longer to show its 'very considerable as a minimum' full force.

Already it costs 15% less for foreigners to buy property in the UK than it did two weeks ago, indeed this multi-trillion pound property devaluation was achieved in just the space of a couple of hours on Britain's Brexit Black Friday (though not everyone calls it that, though more today than on the day of the poll, this a message to us all).

Once Great Britain will have a new prime minister within the next two days to oversee the Brexit, though interestingly once who doesn't want to go. Could a second referendum be on the cards?

With Brexit going ahead, the bottom for British property values won't be known until the real in country price falls start to show. This will take some time given the way the market operates, certainly years but possibly even decades. Whilst the extent of the falls may be tempered by a plummeting pound already at record lows against the USD and still in relative free-fall as some hope it will, they will categorically not be anywhere near fully offset by it.

It will be interesting to see where those who dump their British property holdings go next. If they stick to property, the US may be a preferred candidate or even Canada (despite both having socialist governments in situ which are traditionally not an investors friend).

Less likely despite the close proximity will be anywhere in the EU given it is in for a very rough time over the next few years at best and a complete fracturing at worst.

Even less likely is anywhere in South America or Africa, particularly South Africa which is doing its level best to render itself a failed state in sympathy with some of its equally or even more colourful neighbours.

With nowhere to go, the money might just go under the mattress. It will certainly earn more interest there than in an increasing number of banks around the world who charging you for giving them your money to use.

EN-GLOBO WATCHING BRIEF

TAILWINDS: Lower AUD | Comparative Advantage of Brisbane House Prices | Cheapening Finance
HEADWINDS: Mining Meltdown | Moribund State Governance | Unstable Federal Governance | RBA Intransigence
CROSSWINDS: China Slowdown and Military Muscle Flexing | Eurogeddon | Global Race to the (currency) Bottom
CRYSTAL BALL: 0% Benchmark Interest Rate | 60c AUD | Yuan Devaluations | QE (money printing) here at home

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PROPERTY INVESTMENT

- BUY Inner or Near Ring Brisbane Housing
- SELL Investment Apartments anywhere (assuming you still can)
- SELL Melbourne, Perth, Darwin anything (particularly Investment property)
- HOLD Sydney Inner and Near Ring Housing
- HOLD off buying anything mining industry reliant for at least the next decade (or boom, whichever comes first)
- HOLD off buying anything coastal for the foreseeable future unless lifestyle is more important than money

That's it from me for this edition of HOME TRUTH

Warm Regards,

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