PIPA ADVISER

ISSUE #25

For members of the Property Investment Professionals of Australia

PIPA launches public awareness campaign

Market change is in the air... or is it?

PROPERTY INVESTMENT PROFESSIONALS OF AUSTRALIA PIPA

IS YOUR PROPERTY INVESTMENT ADVISER QUALIFIED?

PIPA *mission:*

PIPA (Property Investment Professionals of Australia) has been formed by industry practitioners with the objective of representing and raising the professional standards of all operators involved in property investment.

The *PIPA ADVISER* is a quarterly title published four times a year by PIPA (Property Investment Professionals of Australia) www.pipa.asn.au

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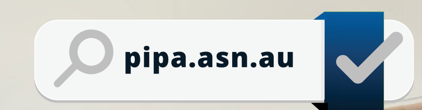
DON'T GET STUNG BY A SPRUIKER!

MAKE SURE YOUR PROPERTY INVESTMENT ADVISER IS A QUALIFIED AND TRUSTED PROFESSIONAL

CHECK CONNECT REVIEW



BECOME ACCREDITED AS A QUALIFIED PROPERTY INVESTMENT ADVISER (QPIA)

CALL (02) 4302 1624

An extraordinary year draws to a close

Welcome to the 25th edition of the PIPA Adviser – your industry e-magazine.

We have finally reached the end of a property year that we will likely never experience again in our lifetimes.

Reflecting on this time last year, there were signs that markets were set to roar in 2021 – and they certainly did that!

I can't remember a time when all capital cities and most regional centres experienced such booming market conditions at the same time.

By year's end, dwelling values nationally had recorded an annual appreciation of 22.2 per cent, the highest increase since 1989, according to CoreLogic, with some capital cities and regional areas posting price growth of 30 per cent or more.

However, there are signs that affordability issues are starting to impact the Sydney and Melbourne markets in particular, with supply also increasing in these locations as well.

Next year, we are likely to see more moderation in market conditions, with the more affordable capital cities set to have stronger results for longer.

The migration away from capital cities to lifestyle locations appears to be a trend here to stay, so many coastal regions have some more price uplift to come as well.

At a board level, this year has been a busy one for your association with plenty going on behind the scenes, including a record year for QPIA enrolments and PIPA memberships.

Border closures meant we only managed to hold one PIPA breakfast in Brisbane this year, but we are aiming to restart these events in Sydney and Melbourne next year.

I am also very pleased to announce that PIPA has invested significantly in a public awareness campaign to promote members as well as QPIAs to consumers and the wider profession.

The campaign is set to appear on a number of media sites in coming weeks. PIPA will also provide these advertisements to members, so that you can promote them on your own websites as well as via your social media channels.

As a part of this special project, the PIPA website is also being updated, to help drive more leads to members. Please keep an eye out for more information on all these initiatives soon.

I do hope that you and your families not only have a wonderful holiday season, but also the opportunity to have a well-earned rest after what has been an extraordinary year for everyone in our profession.

From all of the board, thank you for your continued support and we look forward to seeing you all in 2022.

PETER KOULIZOS
PIPA CHAIRMAN

PIPA is a regular commentator and expert source in property-related stories across the nation. Below are a selection of articles from recent months. For more articles visit the PIPA website.

Daily Telegraph+

Property advice: How many houses you need to own to comfortably retire

It's a question asked by almost every real estate investor and would-be landlord: what number of properties produces a wealthy retirement?

Read the article

Domain

'Bugging out": The new property investment trend for 2022

Investors in residential property will increasingly buy rental homes and opt to live there for periods over 2022 themselves, many experts believe.

Read the article

mortgagebusiness

Qld recorded highest interstate migrants during pandemic: REA

Queensland recorded the largest number of interstate arrivals out of all states during the first 12 months of COVID-19, according to a new report.

Read the article

new members

PIPA welcomes our newest members...

PROPERTY INVESTMENT PROFESSIONALS OF AUSTRALIA PIPA

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- QIN (STARLA) WANG, *Winspro*
- ASHLEY POLLERD, *AJP Town Planning*
- ANN PATERSON, *Ann Paterson Real Estate*

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Nothing to fear from rising interest rates

PETER KOULIZOS, Chair, PIPA Adviser

History shows that interest rates do not force property markets into booms or busts, rather it's often affordability, local economic conditions, consumer sentiment, or access to lending that does, according to new PIPA research.

My analysis of five periods of increasing cash rate movements since 1994 has shown that house prices continued to rise – sometimes significantly – even after rate rises of up 2.75 percentage points over just six months.

> *one of the main reasons for our booming market conditions is easier access to credit*

CASH RATE RISES AND HOUSE PRICE MOVEMENTS

Time Period	Dates	Cash rate increase	House price increase
0.5 years	June 94 – Dec 94	2.75%	1.1%
1 year	Sept 99 – Sept 00	1.50%	7.5%
1.7 years	March 02 – Dec 03	1.0%	35.7%
0.75 years	March 06 – Dec 06	0.75%	8.4%
0.75 years	7June 07- March 08	1.00%	8.9%
1.25 years	Sept 09 – Dec 10	1.75%	10.5%

Sources: RBA and ABS Residential Property Price Index

While the strength or weakness of property markets often had more to do with local economic conditions, including affordability considerations, the data shows that rate adjustments are never the sole underlying reason.

There has been much conjecture over the past 18 months that record low interest rates are the singular reason why property prices have skyrocketed, when the cash rate was already at a former record low of 0.75 per cent before the pandemic.

There were clearly a number of factors at play, including some buyer hysteria I'm afraid to say, but one of the main reasons for our booming market conditions is easier access to credit, which was simply not the case two years ago when rates were also low.

At the end of the day, even when interest rates are low, as they have been for years now, if people don't have access to finance, it really doesn't matter what the cash rate is.

Some alarmist commentary is currently being peddled to seemingly scare people into thinking that when interest rates start to rise, property prices will automatically start to fall significantly.

Likewise, there appears to be some scare mongering about many borrowers not being able to afford their mortgages once rates rise by just one percentage point by using extreme levels of mortgage debt as examples.

The latest ABS Lending Indicators showed that the national average loan size for owner-occupier dwellings was $574,000 in September, which shows that the vast majority of people are not racking up massive singular mortgages of $1 million or more.

While we don't expect rates to rise for a year or two yet – and when they do, they are unlikely to ramp up rapidly – the monthly mortgage repayments on a $574,000 loan may increase by about $73 per week if the interest rate increased one percentage point or from three per cent to four per cent.

> *the national average loan size for owner-occupier dwellings was $574,000.*

It's vital to understand that new loans are already been stress-tested against much higher interest rates of about 5.65 per cent, so there is little to be gained by alarmist 'forecasts' that are just not supported by the data.

LOOMING RENTAL AFFORDABILITY CRISIS

New research has also found that the number of property investors active in the market remains below long-term averages and is likely to add further pressure to the availability of rental properties.

My analysis of recent lending data has found that from about 2007 to 2017, investors generally represented at least 35 per cent of the property market, however, for the past four years, their activity was constrained below this percentage due to the inequitable lending conditions at the time.

The volume of investors has been trending up over the past few months, but the fact that they were generally stuck on the sidelines for a number of years means there is a significant rental property deficit in most parts of the nation.

The tenant demand versus rental property supply imbalance had been worsening even since the over-zealous lending restrictions targeting investors came into effect in 2017.

According to SQM Research, the national vacancy rate's most recent peak was in December 2016, when it hit 2.9 per cent – a percentage representative of a balanced market place.

However, since that time there had been fewer and fewer rental properties available for tenants in most parts of the country because of the subdued numbers of investors in the market.

The national vacancy rate is now just 1.7 per cent, according to SQM Research, with some areas having rental markets that are critically undersupplied, such as Adelaide and Perth with vacancy rates of 0.6 per cent as well as Hobart on just 0.5 per cent.

This is happening during a period when our population is missing hundreds of thousands of new overseas migrants each year as well, with even Sydney's vacancy rate reducing to 2.7 per cent over recent months.

The reduction in rental property supply over the past four years was causing rents to increase strongly, which is creating financial and housing problems for many tenants.

Since December 2016, national weekly house rents have increased by nearly 24 per cent and national weekly unit rents have jumped by 20 per cent, according to SQM Research.

As we know, wage growth has been mostly stagnant over the same period of time, so how are people expected to find the additional funds that are required to lease a property?

With a new round of lending restrictions being introduced, it was time that all levels of government did more to provide accommodation for its population, rather than relying on investors to fund the majority of housing options.

Spending on social housing has been reducing for decades, plus affordable housing schemes seem to be here today and gone tomorrow, depending on which political party is in power.

The National Rental Affordability Scheme, or NRAS, could have helped to prevent the current rental affordability crisis, but it was axed in 2014 after just six years, and has not been replaced with any similar initiative as far as I am aware.

When the next wave of overseas migrants' lands here in coming years, where are they going to live? Migrant accommodation camps like the 1950s? Something needs to be done – and it needs to be done now. ◼

Market change is in the air… or is it?

KIERAN CLAIR
Co-Editor, PIPA Adviser

As we head into Christmas, many of us naturally begin the slow wind down to the holidays. We look for opportunities to gather and celebrate. Moments to mark the occasion of another year drawing to a close.

A chance to look back and ponder what's gone on in the previous 12 months.

To some degree, that's what's being reflected in the market as we approach the end of 2021.

Property stakeholders everywhere feel as if they're taking a little more stock and digesting the extraordinary run of value gains delivered throughout the past year.

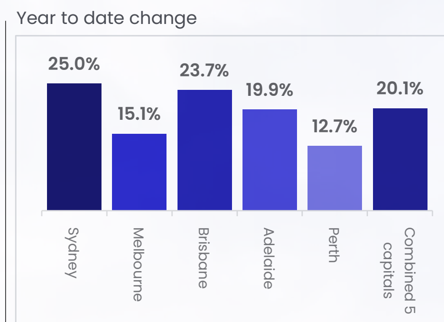
What have been the reasons for this strong uptick and how long can it be sustained into the new year?

CoreLogic analysis (to 28 November) again shows just how far we've come in terms of property price rises:

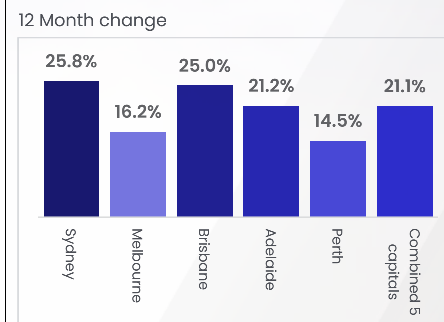
Capital city home value changes

Source: CoreLogic

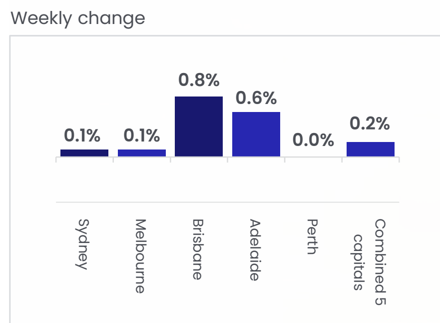
Year to date change



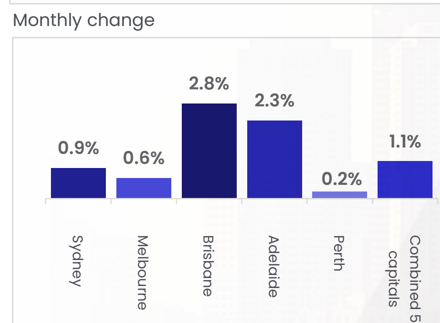
12 Month change



Weekly change



Monthly change



12 Month change

The data house's Home Value Index has seen a continued positive swing with a value increase of 21.1 per cent across the combined capitals over the previous 12 months.

But perhaps what's of greater interest is the monthly index chart. It reveals that despite a 1.1 per cent gain in values over the month of November, the national rate of growth is slowing.

What's behind this seemingly slight cooling of enthusiasm?

Well, it's likely a combination of factors has taken a little steam out of the FOMO kettle. APRA's moves to increase the serviceability buffer, combined with noises that interest rate increases may arrive a touch sooner than first predicted would all be at play here.

Also, let's not forget the drivers of our free market. Huge value rises tend to stimulate supply – more sellers come out, keen to cash in. That means we have probably seen more listings on the portals, particularly in our larger metro centres.

In addition, on the ground observers have suggested there's been a little less desperation (just marginally, mind you) at open homes and auctions.

Again, CoreLogic would tend to support this with their Market Monitors summary stating:

"Demand hasn't quite kept pace with the surge in auctions held, with the preliminary clearance rate continuing the softening trend evident since early October, slipping further this week, with 71.4% of the 3,471 results collected so far selling before, at or after auction."

> *2022 will continue to see rising prices.*

Despite this, Herron Todd White's Property Clock remained stubbornly bullish in September (the latest available at the time of writing)

So, what does this all mean?

Well, most smart analysts seem to agree 2022 will continue to see rising prices, but the gains will be a little less enthusiastic in many centres than was experienced in 2021.

There could also be a notable shift in the capital growth leaders board, with Sydney slipping back and smaller cities moving up as the year progresses.

Much of this hinges on how 2022 unfolds. A Federal Election, changing rules around finance, emergence from a pandemic, reopening of borders… there are still plenty of unknowns.

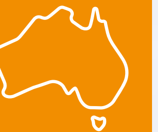
The one thing most of us would say with some confidence, however, is that Australian real estate remains the best possible asset to hold going into 2022. ▲

> *Australian real estate remains the best possible asset.*

National Property Clock: Houses

Entries coloured orange indicate positional change from last month.

Month in Review
September 2021



RESIDENTIAL

HERRON TODD WHITE RESIDENTIAL

25

Source: Herron Todd White

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NSW

Listing volumes were extremely tight during the lockdown period, which made it incredibly challenging for buyers to have any kind of real choice.

With such limited stock available it meant prices were consistently rising due to high competition.

During the last few weeks of early November, we saw a significant shift in market sentiment. The number of people at open houses has dropped off considerably and the number of bidders at auction has also dropped, which has seen the frenetic and exuberant bidding activity at auction fall away.

This is being reflected in the auction clearance rates for the last couple of weeks dropping from above 80% down to around 70% level. Vendors that wanted to capitalise on the peak of the market have missed their chance, but the good news for buyers is that

there is now significantly more properties coming on the market.

I don't expect to see a sudden drop in prices but more a stabilisation as the balance is slowly restored to the market. Because of the lockdown period dragging on so long this year, we are seeing a strong run up of auctions all the way to the week before Christmas and, in fact, we'll see a peak number of auctions over December.

Once our borders are fully reopened and there are significant flows of tourists, expats, and others coming to our shores, I expect to see a significant rise in rents and predict there'll be a rental crisis within about two years as we are not building enough properties to satisfy future demand.

Sales agents will be looking forward to the Christmas season for a rest in what must have been a record year of sales volumes.

The property market is likely to kick off with a reasonable momentum in mid-January as many vendors will be keen to get their property plans into motion – and buyers can capitalise on rising stock volumes.

Rich Harvey
Founder & CEO,
Propertybuyer

VIC

Melbourne does feel like a city in social recovery. Our State Government "have-fun-in-the city" stimulus offering diners a 30 per cent rebate off their bill has even a dreary Tuesday feeling like a party.

Our property market, however, needed no stimulus at all. As restrictions eased, agents' regained the ability to take buyers through properties. As we exited out of a long, grim winter our market continued to defy earlier predictions.

Houses have continued to soar in value, with many buyers suffering heartache in the face of strengthened competition. Even the prudential regulator's efforts to calm the rate of asset price growth hasn't really dented buyers' ability to spend hard.

Stock on market numbers, (including apartments) remains tight – although late spring is showing signs of a slightly eased buyer/seller ratio, given listings are abundant and quite condensed as vendors make up for lost time.

We can anticipate a tougher January for buyers

with agents exhibiting a dogged determination to sell their stock by Christmas

as they head into a much-needed summer break.

And this time, we can expect our property market to be dormant for the first half of January. Not a single soul in the industry feels like working through Christmas this year.

Cate Bakos
Buyers advocate,
Cate Bakos Property

QLD

The Brisbane property market is bucking the national trend, gaining further price growth momentum in recent months.

Over the last quarter throughout the city

we have seen property price records being broken

every weekend.

CoreLogic data shows that sales volumes have increased 51.5 per cent over the 12-month period to October 2021 in Brisbane.

Total listings are still down -31.1 per cent compared to 12 months ago, but there is hope with new listings up 11.2 per cent in the four weeks ending October. With the current buyer demand, we will need to see a much higher level of listing activity before our market finds its equilibrium level again.

Across the quarter, Brisbane house prices have increased 7.1 per cent compared to unit price growth of 3.3 per cent. This provides an indication of the market segment that is in higher demand right now throughout the city.

We have seen houses outperform units in terms of monthly growth in Brisbane every month since September 2020. The median house price in Brisbane is now $731,392 and the median unit price is now $437,086, both at record highs for our city.

There is still a lot of FOMO in the Brisbane market. Some buyers are taking big risks just to be competitive with their offers on properties that become available for sale.

The pace of the market is still very fast and at this stage we are not expecting to see any slowdown in buying conditions, based on the number of buyers we are observing throughout the city.

It is a good time to off-load poor quality properties as there seems to be a buyer for every property, but buyers need to be prepared to compete for quality assets – there are simply no bargains in Brisbane right now.

Melinda Jennison
Managing Director,
Streamline Property Buyers

SA

The South Australian market continues to grow strongly. According to CoreLogic, over the last 12 months Adelaide's dwelling values have increased by 20 per cent and the rest of South Australia has grown a very healthy 16 per cent.

Regional South Australia has experienced a significant increase in demand as evidenced by the huge decrease in median days on market – from 111 days to 52 days!

This growth in both regional and metropolitan South Australia is set to continue. The restrictions on the South Australian borders have been lifted and the influx of people into the state has been phenomenal.

Due to this increase in demand, you can

expect to see rents and property prices rise significantly

especially in the next quarter.

If we look beyond the next three months, the South Australian property market continues to look good for a couple of reasons. Firstly, the increase in population from interstate and overseas migration will continue. Secondly, South Australia has some of the most affordable property in the country and it is gaining the attention of many interstate investors and those wishing to relocate to cheaper areas, even though their work might be based in another state.

Peter Koulizos
PIPA chair, (Program Director of the Master of Property, The University of Adelaide)

WA

We continue to see strong performance from Perth's residential property market as we approach the end of 2021, with historically low sales stock and sustained buyer demand continuing to place upwards pressure on property values in investment-grade suburbs.

Data from the Real Estate Institute of Western Australia shows that listings for sale have now almost halved from their peak of 16,969 in November 2015, with just 8513 properties listed for sale according to October weekly averages.

At the same time, Perth remains one of the most affordable capital city markets across Australia to purchase property. This, combined with the second highest rental yield across the nation at 4.4% (CoreLogic), is underpinning a rise in interstate interest in the Perth market, especially with the Sydney and Melbourne markets facing increasing affordability concerns.

Looking forward, the need to fill WA's high number of job vacancies – which stood at 52,100 in August according to the Australia Bureau of Statistics – is set to place further upwards pressure on demand when interstate borders reopen. Combined with continued low levels of stock and the state's rise in mining activity, this is resulting in a strong outlook for the Perth market in 2022.

Perth remains one of the most affordable capital city markets across Australia

Damian Collins
Managing director,
Momentum Wealth

TAS

Tassie real estate is the gift which keeps giving. Over the past seven-years, a standard house or apartment in Hobart has increased by 120 per cent, miles ahead of the second-placed capital city, Sydney (75 per cent for houses and 45 per cent for apartments), and nearly three-times higher growth than Brisbane (45 per cent for houses, five per cent for apartments).

Local owner-occupiers, particularly upgraders, continue to be the dominant buyer demographic. According to the most recent data from REIT, buyers from the mainland only represented 18 percent of sales over the 12-months ending September 2021. Sales to investors was a low 19 per cent.

Both Launceston and Burnie had a later start to their cycle

Each location produced circa 60 per cent growth over the last five-years, better than every capital city and they are still roaring. And rents are going nuts.

Record low resale supply, record low rental supply, eight consecutive quarters with the state economy ranked number one by CommSec, online real estate enquiries from mainlanders currently through the roof, borders re-opening... Tasmanian real estate is a very rare and treasured commodity.

Looking ahead to 2022, whether there are a couple of interest rate rises or not, money will remain dirt cheap for years to come. Tassie's economy will continue to lead the pack and internal migration will crank up.

Screw what the banks and economists have said, we anticipate property prices will grow by a further 20 per cent or more!

Simon Pressley
Head of Research,
Propertyology

pipa profile

***Sam Ponte** heads up Logic Property Group, was previously a financial planner, and recently completed his QPIA as well*

CAN YOU PLEASE TELL US MORE ABOUT YOUR BUSINESS?

Logic Property Group has one purpose and that is to help 5,000 people live a life on their own terms by 2030 Australia wide.

We exist to serve the everyday Australian with their retirement planning. Through our proven process we mentor and coach our clients through a long-term strategy. This allows them to successfully build a profitable property portfolio in order to generate a passive income so that they can gain back the time they spent working in their nine to five job.

Time is our greatest asset, and we give our clients their time back through our mentoring program to do what's important to them i.e.: spend time with loved ones, pursue "that" business idea, see the world – whatever it is we help our clients end up with more "choice."

We don't sell property; we help our clients buy the right property that is inline with their values and objectives. Property investment is not a one size fits all business, so there needs to be a high level of understanding about your client before an investment vehicle is considered.

HOW LONG HAVE YOU BEEN A PROPERTY INVESTMENT PROFESSIONAL AND WHAT WAS YOUR PATHWAY INTO THE PROFESSION (INCL. OTHER CAREERS)?

I have been assisting clients in their investment property journey professionally since 2015.

I've always had a love for investment properties as I purchased my first property at the age of 22, my parents always encouraged me to save to buy a property.

I was a financial planner for 14 years and grew my business over a 10-year period and sold it in 2018, so I've always had the passion and love to help people generate wealth to live a life on their own terms sooner rather than later.

> ***We exist to serve the everyday Australian with their retirement planning***

WHAT ARE SOME OF THE HIGHLIGHTS OF YOUR CAREER THUS FAR?

Oh, there has been so many good things happen in my career thus far which I am very grateful for, to name a few:

1. The average client in my business owns three investment properties.

2. We have 27 clients approaching their desired retirement age and income within the next two years.

3. Building a successful financial planning business and selling it.

4. Being accepted as an advisory by Aspire network, which provides all the support when it comes to planning, property research, IT, process, property sourcing, tech, code of conduct and ongoing support to make sure we provide the very best advice and property to our clients now and into the future.

WHAT WERE SOME OF THE MAIN REASONS FOR BECOMING A QPIA?

The main reason for becoming a QPIA is to hold the highest qualification our industry has. As a passionate property professional, I feel that if you truly love what you do, you should do the work in order to uphold the highest standards in your profession. For me, that is having the QPIA status.

HOW DO YOU BELIEVE BEING A QPIA WILL SUPPORT YOUR CAREER?

I feel it will stand out to prospective clients knowing they are in trusted hands.

It will also give other professionals confidence that their clients are in the right place, receiving the highest level of care, and receiving qualified quality advice that is in their best interests.

WHAT ARE SOME OF THE REASONS WHY YOU JOINED PIPA?

I wanted to be part of the number one leading association of the property industry. I also love everything PIPA is about and love what they stand for.

WOULD YOU RECOMMEND OTHER PROPERTY INVESTMENT PROFESSIONALS BECOME MEMBERS OF PIPA? WHY?

Yes, definitely, to be provided with up-to-date information from some of the best in the industry, to ensure you are performing at the highest level and in-line with PIPA's guidelines. They are just so down to earth and really are an amazing group.

HOW DO YOU SEE PROPERTY MARKETS PERFORMING IN YOUR PROPERTY INVESTMENT LOCATIONS? WHAT ARE SOME OF THE OPPORTUNITIES AND/OR HEADWINDS IN YOUR OPINION?

So far all of our locations have outperformed our clients' expectations and, moving forward with a strict due diligence matrix that our research team uses, I'm quite confident that our property recommendations will continue to provide the result our clients seek. However, some things are out of our control – with prudent planning we give our clients the best chance of success.

WHAT'S NEXT FOR YOUR BUSINESS IN THE NEXT 12 MONTHS AND BEYOND?

We will begin to ramp up our social media/digital footprint and begin opening up for seminars and broaden our audience in order to help more people start their investment journey and keep redirecting people into the right direction of retiring earlier and in better financial shape.

> ***I've always had the passion and love to help people generate wealth***

JOHN HAWKINS
Senior Lecturer, Canberra School of Politics, Economics and Society and NATSEM, University of Canberra

RBA says it's a W-shaped recovery, with housing one of the few concerns

The Reserve Bank has used Friday's quarterly assessment of the economy to declare that lockdowns have "delayed but not derailed" Australia's recovery.

It says economic activity probably contracted 2.5% in the three months to September, but the December quarter (the one we are in now) will regain most of what was lost, leaving the economy recovering much as it would have were it not for the mid-year lockdowns.

Taken together with last year's descent into recession and quick bounce back it paints a picture of a W-shaped recovery, even on what the Bank has graphed as its "downside" scenario.

As a sign of emerging confidence it points to an increase in the number of people prepared to change jobs because they are looking for something better or different.

It says this is partly a bounce back from the start of the COVID recession when workers appeared to put plans they might have had to change jobs on hold.

The Bank is concerned about property markets at home and abroad.

It says the possible collapse of the large and highly leveraged Chinese developer Evergrande might "lead to a significant slowdown in the Chinese economy".

Average home prices have reached fresh highs in most Australian cities.

It says while interest payments have declined by around one percentage point of disposable income since March 2020 because of lower interest rates, the financial system faces risks associated with high and rising household indebtedness.

While it says mortgage rates will climb, and while financial market pricing implies quite rapid increases in the Bank's cash rate, it doesn't expect to lift the rate until 2024 (which is the year after Governor Philip Lowe's term is due to end, raising the prospect of him completing his seven-year term without once lifting rates).

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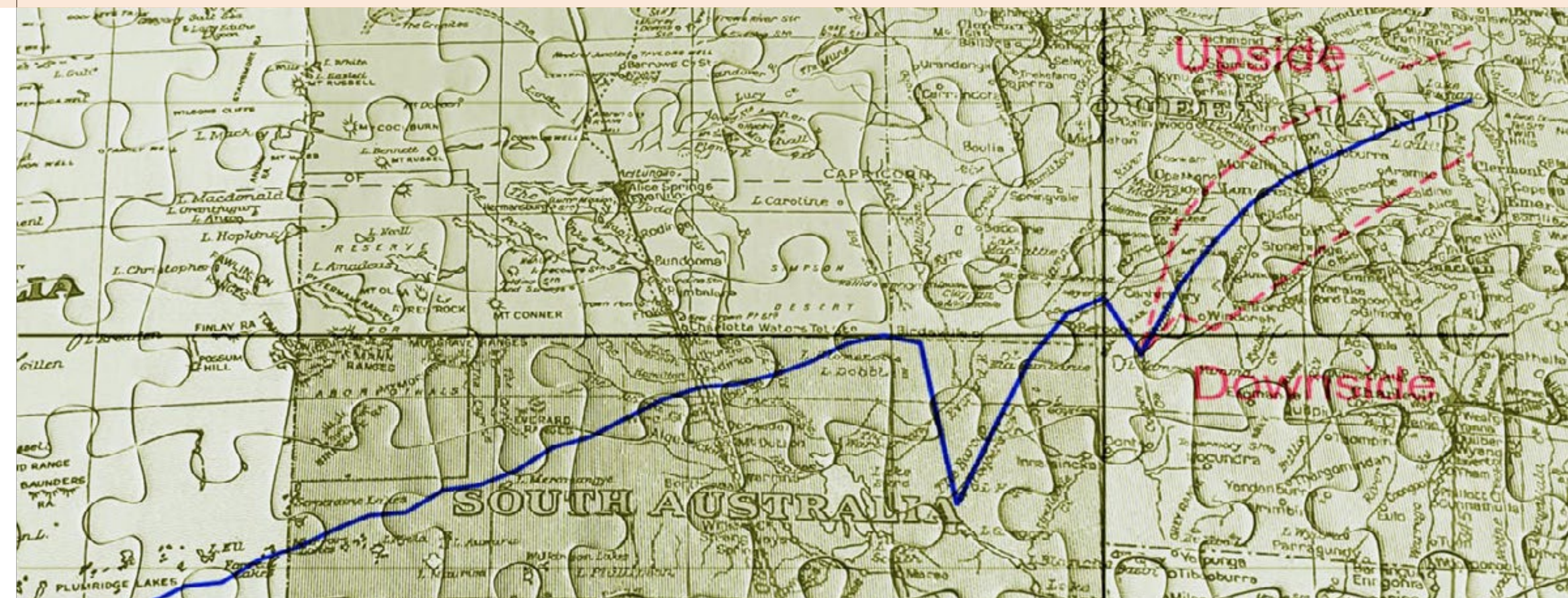


The Bank has consistently said it will "not increase the cash rate until actual inflation is sustainably within the 2–3% target range".

It has also said it is not enough for inflation to be merely forecast to be within the range, creating a high bar for action.

Although at 2.1% over the year underlying inflation is the highest it has been since 2015, it is still towards the bottom of the Bank's target band.

Inflation weaker than it looks

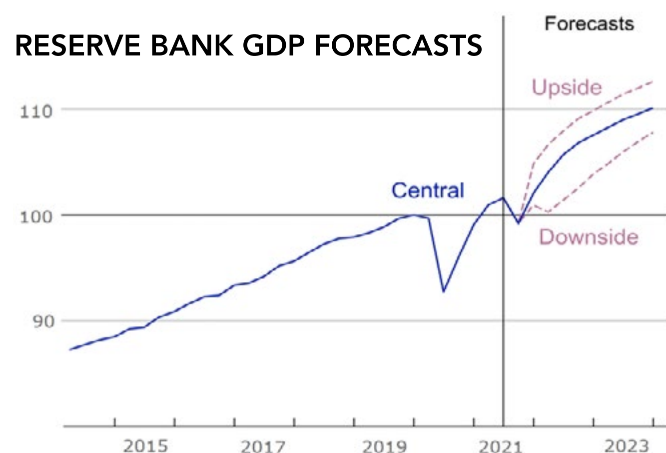
And the rate reflects some temporary factors. Some of it is due to the rebound in petrol prices as demand has picked up as people have returned to work, something that won't continue.

The Bank expects underlying inflation over the course of 2022 to be 2.25%. Although well above the previous forecast of 1.75%, it is below the mid point of its target.

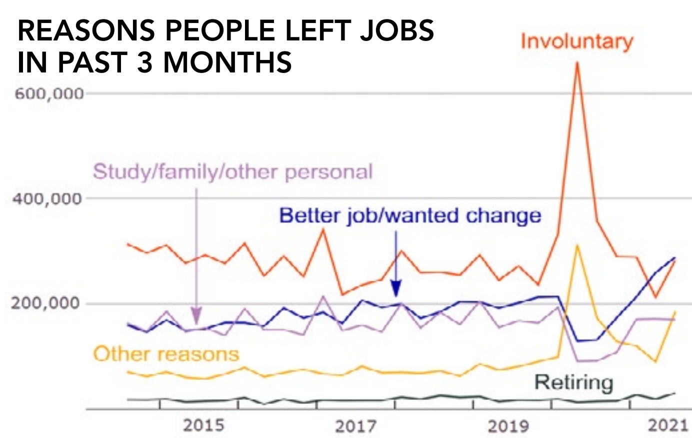
It doesn't expect inflation of 2.5% until 2023, suggesting no rate hike until then.

The labour market outlook is little changed from the Bank's August statement. It expects unemployment to fall to a historic low 4.25% by the end of 2022 and then to 4% in 2023.

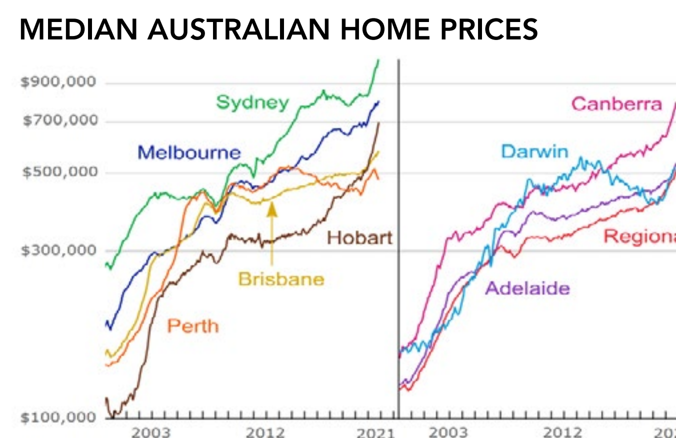
Even then, in 2023, it expects only modest wage growth of 3%, doing little to support the sustainably higher inflation it says it would need to see before it lifts rates.



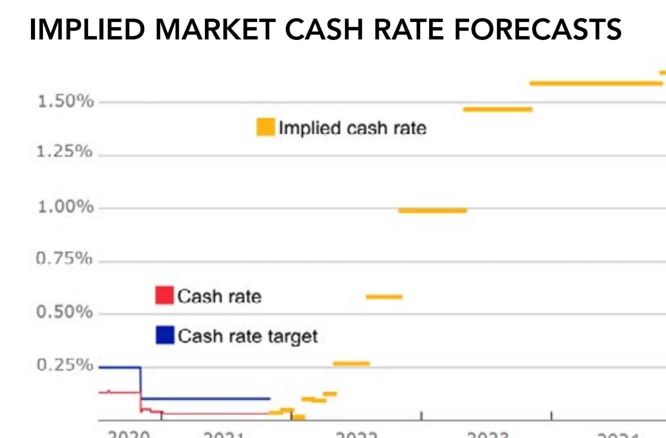
Index numbers, December 2019 = 100. RBAABS; RBA



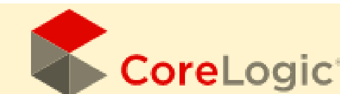
Source: RBA, ABS



Seasonally adjusted, log scale. CoreLogic,RBA



Bloomberg; RBA

This article was originally published on  Read the original article

Making sense of macro-prudential changes

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The past few weeks have seen mounting speculation around what changes could be coming for the housing lending space. The Council of Financial Regulators, which includes the banking regulator APRA, flagged the need for sound lending standards to be maintained, with signs of "some increased risk taking" appearing in mortgage lending.

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Examples of a more risky debt and lending environment have been trickling through various data releases over the past few months. RBA data shows housing debt-to-income ratios reached record highs for owner occupiers at 102%, annual housing credit growth (5.6%) is outstripping income growth (1.6%), and APRA data shows a higher than usual concentration of new loans on high debt-to-income ratios.

It became increasingly clear that 'macro-prudential' intervention (policies aimed at securing financial stability) was a case of 'when', not 'if'.

Wednesday's announcement from APRA outlined changes to the way lenders assess new borrower's ability to service a mortgage. Essentially, banks would be expected to test whether a borrower could repay a mortgage, if the mortgage rate is three percentage points higher than the product rate on offer. APRA advised the buffer should be implemented by the end of October 2021.

Importantly, major banks already have a required buffer of 2.5 percentage points in the serviceability assessment process, which was introduced in 2019, or a minimum interest rate level to assess serviceability (also known as a 'floor' rate), which averaged 5.09% across the major banks in June.

FIGURE 1. HOW DOES SERVICEABILITY ASSESSMENT CHANGE FOR OWNER OCCUPIERS AND INVESTORS?

	Average floor rate for major banks*	2.5% buffer	3.0% buffer	Change in serviceability rate
Average owner occupier mortgage rate (2.36%)	**5.09%**	4.86%	**5.36%**	0.27%
Average investor mortgage rate (2.72%)	5.09%	**5.22%**	**5.72%**	0.50%

*Average floor rates from the major banks were sourced from Rate City as of June 2021

This includes a proactive increase to the floor rate of 15 basis points from CBA in June. Banks must use whichever rate is higher to assess serviceability, which plays in to the subtle targeting of this new recommendation from APRA.

Because owner occupier mortgage rates are lower than investor rates, these changes may actually have more impact on the investment segment of the market. Additionally, as APRA notes in their announcement, investors tend to be more leveraged in their borrowing behaviour and may be carrying additional housing debt which would also be subject to the increased serviceability assessment.

Figure 1 compares the change to interest rate assessment based on the current average mortgage rate for new owner occupier loans (which was 2.36% through August) and investor loans (2.72%).

Using the average owner occupier rate as an example, APRA's announcement would mean borrowers could need to demonstrate the ability to repay a mortgage with an interest rate of 5.36%. But given floor serviceability rates would have been pretty close to these levels anyway, the measure is not as drastic a change for owner occupiers, with the hypothetical showing an increase in assessment rates of 27 basis points from 5.09%, to 5.36%. This is opposed to a 50 basis point rise for investors. Owner occupier borrowers may be more likely to be assessed on the buffer rate under these changes, rather than the floor rate.tend to be more leveraged in their borrowing behaviour and may be carrying additional housing debt which would also be subject to the increased serviceability assessment.

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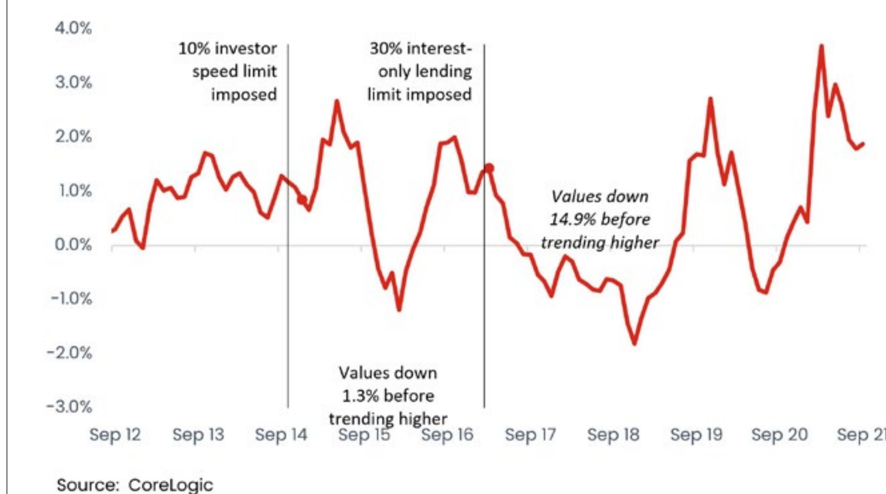
But even in this scenario, the mortgage rate buffer going from 2.5 to 3.0 percentage points seems like a subtle approach to financial stability and will likely only impact at the margins of borrowing demand.

Perhaps this is also a lesson learned from the relative shock created to the housing market in 2017, when new interest only mortgages were limited to 30% of new housing lending. A chart of monthly housing market movements across Sydney against previous macro-prudential measures can be seen in Figure 2.

Housing market values experienced a peak to trough decline of -8.4% off the back of macro-prudential changes in 2017 at the national level. The decline was sharper across heavily concentrated investment markets like Sydney (-14.9%) and Melbourne (-14.1%). This subtler change to lending conditions is far less likely to move the housing market into negative territory, and APRA estimates the typical maximum borrowing capacity would only be reduced by about 5%.

FIGURE 2. MONTH-ON-MONTH CHANGE IN DWELLING VALUES, SYDNEY



More to come?

While APRA's announcement may seem like it won't have much impact on demand for credit, it is worth noting that this may not be the end of macro-prudential changes. A lot of focus has also been on high 'debt-to-income' ratios – a statistic expressing a borrower's pre-tax income divided by their total debt levels.

In his letter to lenders, APRA Chair Wayne Byres flagged that if new mortgage lending on high debt-to-income ratios remained at high levels, it "would consider the need for further macro-prudential measures". It has also been stated by the regulator that implementing a limit on high debt-to-income ratios is "operationally complex".

Therefore, while the announcement may seem like a subtle change to housing lending conditions, there may be more tightening to come as the Council of Financial Regulators monitors trends in housing credit and household debt. ◪

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