Brisbane House Price Forecast

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Summary

Australia participated fully in a relatively synchronised global house price bubble. Abundant cheap credit is believed by most observers to be the primary cause of these asset bubbles. Australian house prices are the most expensive in the developed world, based on price relative to earnings, so there must be specific reasons for our supposedly egalitarian society holding this title. The most important factors are considered to be Australians' penchant for risk taking together with Federal government policy frameworks, especially taxation, supportive of risk taking (i.e. speculation) in housing markets.

With the credit crisis causing the withdrawal of easy credit, the house price bubble is now deflating around the world. In some markets it can be characterised as having "popped". House price indices in some US cities have dropped by around 30% within 19 months of peaking. There are clear indications that Australia's house price bubble has begun deflating – e.g. the Brisbane property market has clearly been under pressure since April 2008. This will begin to show up in house price and other data in mid- to late 2008.

Given that the causes of the bubble formation and deflation are consistent with the US, and because the property bear market is most advanced in US markets, future Brisbane house price movements were forecasted by modeling based on US house price movements. Historical data (from ABS and Case Shiller) shows that Brisbane's house price bubble was, indeed, spectacular – the presumptive peak in March 2008 was firmly between the peaks reached by the Case Shiller 20 US city index and those of Los Angeles and Miami (two of the biggest boom US cities).

Forecasting suggested that Brisbane house prices may decline by 17% between March 2008 and December 2009 to reach a median price of $350,443.

Subsequent house price movements were modeled out to March 2016 by modeling past price behaviour after Brisbane property booms and likely impacts of Federal government policy initiatives – e.g. the possible removal of investor\speculator incentives such as negative gearing and capital gains tax concessions. The modeling suggests that house prices will trough around September 2011 at a median price of $294,000 (a 30% decline from peak).

If maintained, the investor incentives will cause another "mini" bubble around 12 months prior to the first participants gaining access to the First Home Savers Accounts (FHSA). In this mini bubble, house prices are forecast to rise by $66,750 (more than the likely average FHSA balance). Consequently, affordability will continue to impact first home buyers and the bubble will fade out to March 2016.

However, the central forecast is that the Federal government, following the taxation review, will cease these investor incentives because they are shown to be ineffective and damaging through their impact in causing bubbles and maintaining a speculative premium in our house prices. Modeling of this forecast suggests that house prices will form a solid base over a few quarters post September 2011. Prices will bounce off their lows over couple of quarters in late 2012/early 2013 due to first home

buyer activity after first participants gain access to their FHSAs. Price rises are then roughly inline with inflation from 2013 out to the end of the modeling period at March 2016.

Under both scenarios, the median price is $334, 224 at March 2016, the end of the forecast period. If Brisbane wages increase at the rate of 4% pa, at March 2016 the Brisbane house price to income ratio will be 4.43, 10% higher than in 2001! However, over the very long term, beyond the forecast period, affordability will continue to improve for first home buyers as baby boomers sell down their assets through retirement. The continual supply of existing housing on the market should have a downward impact on Brisbane house prices over the next several decades.

In conclusion, this study and its forecasts show that poor Federal government policy has been, and will continue for a long period to be, damaging to the needs and aspirations of everyday Australians, and "working families". That very much includes the less sophisticated investors that joined the boom late, thereby transferring their current and future wealth to the earlier "smart money" investors. And that is precisely why the current Australian federal government must finally take action and get rid of these ineffective taxation policies which promote, and provide an opportunity for spruikers to aggressively promote, Australian houses as speculative assets. They are our homes not casino chips!

Introduction

Australia has participated fully in a relatively synchronized global house price bubble.(1) The breadth and synchronicity of the bubble, across most developed countries and on different continents, suggests that there were some major causative factors in common. Perhaps the greatest global factor was a concomitant credit bubble, emanating from over zealous investment bankers in Wall Street bundling up mortgage debt in complex instruments to sell to investors who accepted very low risk premiums, resulting in plentiful cheap credit around the world. The Bank of International Settlements in its most recent report supported this view (BIS 2008) [http://www.bis.org/events/agm2008/ar2008o.htm].

It is clear that the bubble "popped" in the US in June 2006, with the Case-Shiller 20 City Composite Index exhibiting a roughly 17% decline over the subsequent 19 months to February 2008. The synchronicity of that peak across the 20 individual city indices, which in turn make up the 20 city index, is quite amazing – 11 of 20 cities peaked ± 2 months of June 2006. UK housing prices have also peaked in the last 12 months. And there are early but explicit signs that Australian housing markets peaked in early 2008 with house price declines likely to be evident in data from mid-2008.

That Australia's house price bubble has begun to deflate is unsurprising given the remarkable synchronicity of the house price increases across countries. For a full discussion on asset bubbles and reasons for their synchronicity, the reader is directed to Shiller (2005).

Australia's House Price Bubble

Whilst the housing bubble was a global event, it is important to note that through it Australian house prices have been the most expensive – defined as the ratio of price to income – in the developed world. This is immediately apparent on examination of this graph [http://www.rba.gov.au/Speeches/2008/_Images/270308_so_graph7.gif] published by the Reserve Bank of Australia (Richards 2008).

According to the RBA graph, the ratio of the median Australian house to income was roughly 5.5 at the end of 2007, having reached 6 in 2006. With the exception of the relatively short-lived housing price boom of 1988-89, where the ratio reached about 3.7-3.8, the ratio has been under 3.5 from 1985 until the Australian experience of the housing bubble commenced in 1996.

For a very long term view of Australian house price movements, as well as a discussion of the role of debt in the current bubble, readers are directed to this excellent article [http://www.debtdeflation.com/blogs/2008/03/03/steve-keens-debtwatch-no-20-march-2008-double-or-nothing/] by Associate Professor Steve Keen (2).

Even though much of the discussion of the house price boom and bust centres on the US – where it is openly and uniformly acknowledged as a bubble that is now deflating – their ratio "only" reached about 3.7 at its peak! In other words, equivalent to 1988-89 Australia's mini price boom, and much, much lower than our current level.

Whilst someone, or some country, must hold this position, there must be reasons specific to Australia which allowed its citizens and foreign investors to bid our prices so high. I have read arguments which suggest that we are a people that appreciate owning our own homes more than others. This, to me, seems a nonsense and grasping at straws to justify high prices.

But perhaps a common trait in us Australians, celebrated by many as a national identity trait of which to be proud, has something to do with it. That is a penchant for gambling – the common view that "Aussies would bet on two flies crawling up a wall".

The bubbles throughout the world were marked by very significant levels of speculation on future house price increases – which became an almost fanatical view that "house prices only ever go up" – what Shiller (2005) described as a naturally occurring Ponzi scheme. Essentially people throughout the developed world were gambling that the price of houses would increase. But everybody convinced themselves that it was a no lose game. And Australians, with our penchant for "punting", were quick to join the game!

But I do not believe for a second that Australians' penchant for gambling completely explains why our houses are the most expensive in the developed world.

Of equal, or greater importance, has been Government policy frameworks in Australia, and adjustments to those. (See the Report of the Senate Select Committee on Housing Affordability 2008 [http://www.aph.gov.au/Senate/committee/hsaf_ctte/report/report.pdf] for full coverage of this topic.)

I will just highlight here – as many others have before me – that the implementation of concessional capital gains tax (CGT) rates in 1999, followed by the First Home Owners Grant (FHOG) in 2000, which was doubled for a period, hugely stimulated demand for housing when other conditions were conducive, such as relatively low interest rates. This undoubtedly added momentum to the bubble, and spread it throughout the country from its epicentres in Sydney and Melbourne.

Of course, these are not the only policies which have a distorting influence on Australian house markets. Australia has long permitted negative gearing on residential investment properties, whereby an investor can offset losses from a rental property against other income, such as from salaries.

If we go back to the RBA graph, we note that Australia has had high house prices, relative to other countries, since at least 1985. In fact, there were only two or three years when Australia did not have the most expensive houses.

And I would argue that is mostly due to there being a long-term speculative premium in our housing market, there mainly because successive Australian federal governments have endorsed, or even promoted, house price speculation as a completely acceptable wealth creation tool in Australia.

I say promoted because yet another speculator/investor incentive was legislated by the then government just prior to the 2007 federal election – the option to leverage into residential property, as well as other assets, in self-managed superannuation funds. These funds have a maximum of 4 members, usually a wealthy individual, couple or family, and had an average balance at end of year 2007 of $800,000! Moreover, around 30% of funds had a balance of less than $200,000. So there are some very wealthy people that have been given further taxation incentives – through the very significant tax benefits for superannuation – to speculate/invest in residential property.

The very significant disadvantage that first home buyers are at in comparison to property investors, in a very similar government and tax policy environment, was recently highlighted in a paper from the Reserve Bank of New Zealand (Hargreaves 2008) [http://www.rbnz.govt.nz/research/discusspapers/dp08_06.pdf].

Thus, it is little wonder that, as the RBA put it, higher income earners tend to gain when house prices rise, but lower income earners tend to "suffer"! (Richards 2008) [http://www.rba.gov.au/Speeches/2008/sp_so_270308.html]

Brisbane House Prices (3)

I analysed data from 1989/90 onwards, but an excellent paper by Abelson and colleagues (2005) [http://www.econ.mq.edu.au/research/2005/HousePrices.pdf] looked at house prices throughout Australia from 1970. They noted 4 house price booms over that period: a) from 1972-74, and they stated "the combination of high inflation, full negative gearing and no capital gains tax produced high returns to investors"; b) 1979-81, and they stated "policy setting continued to be favourable for investors"; c) 1987-89, and they stated "the collapse of the stock market in September 1987 sparked a flow of funds into housing"; and d) 1997-2003, and they stated "Investor demand for housing was high. The boom appeared to get a second wind … from favourable policy settings for investors, including negative gearing combined with high marginal tax rates and a perceived lowering of the CGT."

For Brisbane, they found that, real house prices (i.e. adjusted for inflation) fell between 1974 and 1980, and1982 and 1987.

My analysis of ABS data, adjusted for inflation using the calculator on the RBA website, shows that Brisbane house prices failed to keep up with inflation for over 9 years from 1991/92 to 2000/01 (Figure 1).

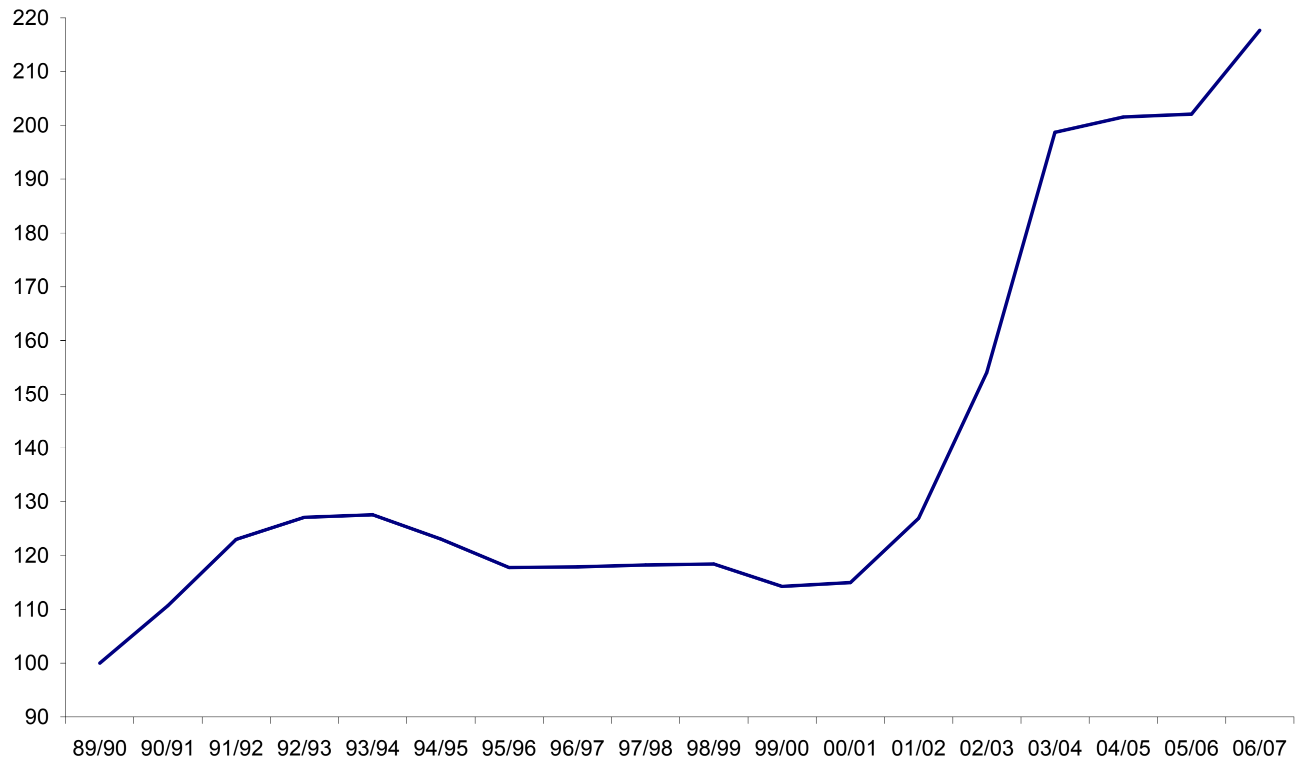

Figure 1. Brisbane house price index 1989/90 to 2006/07 adjusted for inflation. 89/90 = 100. (Original index data from ABS. Adjusted for inflation using the RBA calculator on its website.)

However, the housing bubble spread to Brisbane in 2001, and the Brisbane median house price essentially doubled (92% increase) in three years from June 2001 and June 2004. House price growth slowed for a few years, but picked up strongly again in 2007. Between March 2001 and March 2008, the Brisbane median house price increased by a staggering 168% - from $156,600 to $420,000!

At time of writing, there are clear signs that the Brisbane house price bubble has popped, along with the rest of the country. Various data sources point to a sharp contraction in the demand for credit, especially for housing. Newspaper articles have highlighted that sales in Brisbane are dropping whilst more houses are coming onto the market. Brisbane auction clearance rates have been below 30% for a number of weeks. At end of June 2008, there were over **20,000 more houses listed for sale** in Queensland compared to the same time last year; **an increase of 150%** (4). And in the three months to May 2008, 1575 fewer Queensland houses were sold in comparison to the same period of the previous year, **a decrease of 22%** (5).

Clearly, people are trying to sell many more houses, but significantly fewer are willing to buy. This is having the effect of lowering asking prices on listed houses in mid 2008. It will also flow through to selling prices, negotiated discounts, and time required to sell.

It is important to note, however, that these changes may not become clear in the widely published data until late 2008 or early 2009 for a number of reasons. Firstly, the organisations that typically publish these data benefit from turnover, and therefore strong markets, of established and new housing, and publishing data is meant to be a positive influence on that, as well as free promotion. And secondly, most of these data are based on moving averages over 6 to 12 months, which have the affect of smoothing out the data so that the early stages of booms and busts are not immediately evident. Most likely, the first data to confirm the burstingg of the bubble will be the quarterly ABS data house price data.

Note, organisations that benefit from strong realestate markets include those in the realestate industry, property wealth advising and consultation industries, building and construction industries, and finance including mortgage broking and banking industries. Moreover, it is important to note that even state governments have become particularly dependent on increased taxes from increased property prices – property tax revenue increased 72% in 5 years! (6).

A counter argument to the first point above might be that organisations have provided data to be used in the quoted newspaper articles. But I strongly suspect that, at this early stage of the bear market, those organisations are attempting to “kick-start” some momentum back into the market by spreading a “buy on the dip” mentality. If they were successful, it would almost certainly be referred to as a “suckers rally” in the medium term.

Given the sheer number of houses listed for sale – presumably due to stressed sales and long-time owners’ concerns that they are not likely to have as profitable an opportunity to exit that market for some time – I would argue that it is highly probable that we have already entered a bear market in residential property. The Brisbane residential property bubble has indeed popped.

I will not spend a lot of time discussing why – as the “bubble psychology” fades the reality will be clear to most, and there is sure to be much said of it over the coming months. I would like to think that house prices just got so ridiculously high that it became blindingly obvious to most potential buyers. But I do not think that is the main reason – the fear of never being able to afford to buy a house was palpable. Forget the old fable of cabbies telling you where to buy, three day old embryos were yelling from the womb “buy me a home, it’ll never go down in value!” (I do mean this in a literal way – most parents assumed that house prices would always stay high and were deeply concerned about whether their children would ever be able afford to buy a home.)

The bursting of the bubble was probably due to three events, and their interaction with the market fundamentals of affordability and investment returns. In chronological order the events were the bursting of the US housing bubble, the credit crisis and interest rate rises in early 2008.

I think that Shiller (2005) is right that bubbles are essentially created by feedback loops, and in late 2007 Australians received a lot of negative feedback on housing markets from the bursting of the US housing bubble and the credit crisis. Australians were highly aware of the troubles in the housing market in Western Sydney, but that seemed not to matter. Then the RBA and bank interest rate rises in early 2008 seemed to have a major impact not just on affordability, but confidence. Perhaps it was more to do with interest rate uncertainty. (And very few people are even aware of the potential for a serious current account funding crisis!)

To sum it up, I would suggest that the bubble has popped because those events allowed buyers to analyse the market with a different frame of reference. Investors, especially more experienced ones, and speculators decided that prices had gone as high as they were likely to for an extended period. Most first home buyers were excluded from the market due to record low affordability and tighter credit availability from the credit crisis, and many of those that could afford to buy knew it was imprudent to do so.

(I would like to think that my blogging, along with others, played a very small part in people coming to their senses also – I have no doubt whatsoever that industry groups spend significant funds on attempting to influence public opinion though those channels – it would be interesting for Shiller et al. to research this issue.)

Forecast for Brisbane house prices (3)

The factors that led to the popping of the Brisbane house price bubble are similar to the popping of the US bubble. House price rises and interest rate rises led to very low levels of affordability. Stressed sales began to occur, by owner-occupiers and the large number of speculators that had come into the market, with fewer buyers able or willing to take up the slack. Thus a negative feedback loop commenced and the bubble began deflating. In some US cities it has popped.

Many will argue that the US situation is different because it is now clear that a lot of people were given loans that they would never be able to repay. I would argue that things were not that dissimilar in Australia. I know from personal experience that, so called full-doc (our equivalent to prime) lenders, were prepared to lend, without witnessing any history of savings, mortgages that required repayments equivalent to 60% of net income (when interest rates were at 7% and lower). Australia was no different to anywhere else – quantity of credit sold by lenders was the key driver, not quality! That caused a very significant reduction in lending standards, which as of writing is being reversed (because lenders know that they now need to have very good quality mortgages if they are to have any hope of on selling the credit through those complex instruments – residential mortgage backed securities.)

To come up with a forecast of what might happen to house prices in Brisbane over the next few years, I plotted an index of the median Brisbane house price versus the Case Shiller 20 US city index and indices for Miami and Los Angeles, two of the more spectacular boom cities (Figure 2). I realigned the US indices so that the peak of the 20 city index was in line with the presumptive peak in the Brisbane index at March 2008.

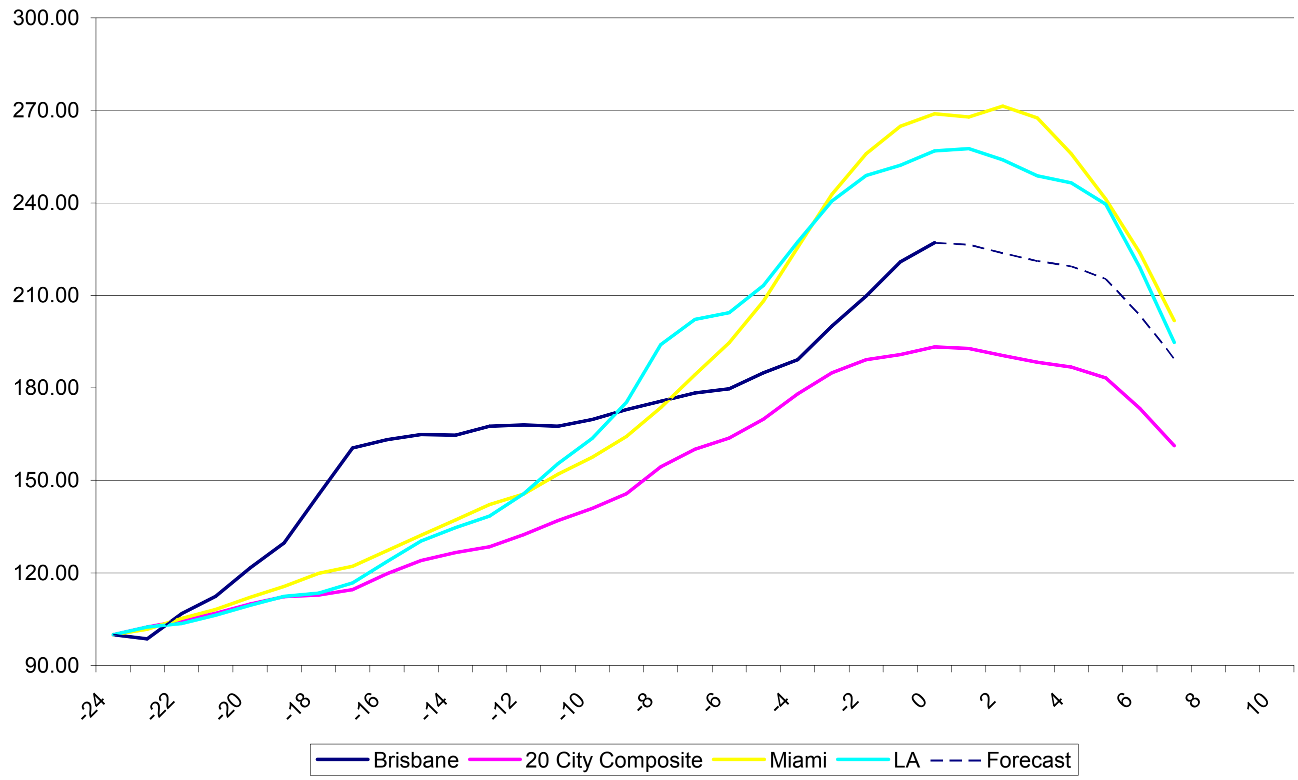

Figure 2. Comparison of house price indices for Brisbane, 20 US cities, Miami and Los Angeles. Data sources – ABS and Case Shiller. Six years pre-peak = 100.

The early stage of the Brisbane bubble was more rapid. The 20 US City index took over 4 years, and the Miami and LA indices took 3.5 years, to achieve the gains that the Brisbane bubble made in the first 18 months! Ultimately the Miami and LA bubbles proved to be bigger than the Brisbane one, but the presumptive peak of the Brisbane bubble is well above the peak of the 20 city index.

The LA and Miami house price bubbles were two of the biggest in the US, and their price indices have since collapsed by 26% and 28%, respectively. That the Brisbane house price index peaked between the peaks of these two cities, and the 20 city index, shows just what a huge bubble Brisbane house prices have been.

Because the causes of the bubbles were virtually identical, the magnitudes of the bubbles were similar, and the reasons for the bubbles popping were similar, I would argue that it is valid to forecast the likely movement of the Brisbane house price index based on movements of these Case Shiller Indices of US house prices.

It would be valid to develop a forecast between LA/Miami and the 20 US city index seeing as the Brisbane house index peaked between them. However, I used a more conservative approach of applying the movement of the 20 US city index to forecast the likely movement of Brisbane house prices.

This forecast results in the median price of Brisbane houses having decreased by 17% by December 2009 – from $420,000 in March 2008 to $350,443.

I wanted to take my modeling further. From house price movements since 1970, reported above and in Abelson et al. (2005), we know that: a) this has been the largest house price boom, a bubble, Brisbane has experience in at least 4 decades, perhaps ever; b) it is typical for real house prices to decline for extended periods after price booms, and c) government policy settings, particularly applicable to investors, are major factors in house price movements. The new Federal government has given some clear indications in this respect (Table 1).

Table 1. Federal government policies, current and planned, related to housing and likely impacts.

Increasing Investor Demand	Increasing Owner-occupier Demand	Increasing Supply by/for Investors	Increasing Supply by/for Owner-occupiers
•Negative Gearing •CGT Concessions •Gearing within SMS ALL UNDER REVIEW	•No CGT •First home owners grant •First home savers accounts	•Affordable rent initiative – subsidise construction of 50,000 houses in 5 years (100,000 in 10 years if necessary)	•(perhaps initiatives to stimulate first home buyers' demand for new dwellings will come from the tax review) UNDER REVIEW

As continually stated by Abelson and colleagues (2005), as well as many, many others, Federal government policy settings affecting investor demand for housing – particularly those relating to taxation – have a very significant affect on housing markets over the medium to long term. With the taxation review, "Australia's Future Taxation System", there is considerable uncertainty surrounding these settings, and policy frameworks will not be clear for several years.

I modeled future Brisbane house price movements based on two scenarios: a) my central forecast that the Federal government will end negative gearing and the CGT concessions following the taxation review because of mounting evidence and public concern that they promote speculation in house prices, and b) taxation concessions to investors remain as is, and other setting stay as per table 1.

The following assumptions are implicit in each forecast scenario:

a) Central forecast: negative gearing and CGT concessions are ceased in early 2011; the first home savers accounts (FHSA) are successful in attracting a high proportion of first home buyers, thus decreasing their demand until late 2012 when there is a surge in demand as the first participants gain access to their funds; Federal and state governments plans to increase supply of housing succeed.

b) Alternative forecast: investors continue to receive significant taxation concessions which continue to be funneled into established houses, rather than new dwellings, especially in the lead up to the first participants of the FHSA gaining access to funds; the FHSA initially attracts many first home buyers, thus decreasing their demand until late 2012 when there is a surge in demand as the first participants gain access to their funds; Federal and state governments plans to increase supply of housing succeed.

The results of that modeling are presented below in Figure 3.

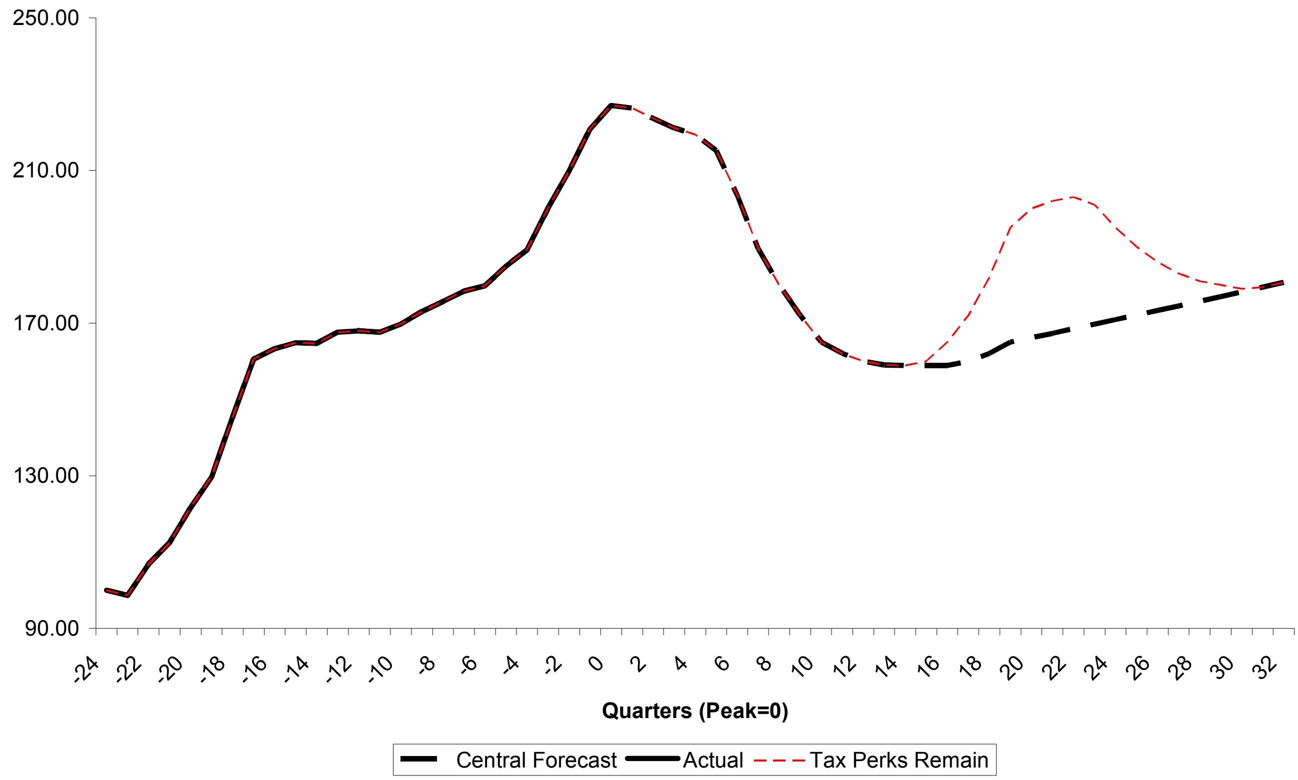

Figure 3. Forecast of future Brisbane house prices. Stage 1 of the forecast, up until 18 months (6 quarters) post peak, is modeled on the 20 US city house price movements. Stage 2 modeling, from 18 months to 8 years, involves two scenarios of whether investors continue to receive favourable taxation treatment.

In the central forecast, house prices continue to decline to trough at September 2011 at 30% below the March 2008 peak. This represents a median price of $294,000. The median price forms a solid base there over several quarters, and with the increase in demand from first home buyers, prices begin to rise in the late 2012/early 2013. Price rises are roughly inline with inflation from 2013 out to the end of the modeling period at March 2016 when the median price is $334, 224.

In the second scenario, house prices continue to decline and once again trough at September 2011 at 30% below the March 2008 peak. However, with the property investor taxation concessions still in place and promoting speculation in housing, investors begin to position themselves to take advantage of the surge in demand from the FHSA participants gaining access to their funds. This surge in demand initially from investors results in house prices quickly moving off their trough in late 2011/early 2012 and accelerating upward through mid 2012. By late 2012, when the first FHSA holders hit the market, house prices are already $66,750 above their trough prices. Some FHSA holders decide to buy, others decide not to, but the feedback loop has been reignited to a slight degree by the price gains, so more speculators come into the market further driving up prices. However, the ability of spruikers to build moment in the market is hampered by the coexistence of negative feedback loops from the most recent price declines. In other words, spruikers will not be able to perpetuate the myth that “house prices never fall”. Through mid 2013 it becomes apparent that first home buyers are still not entering the market due to poor affordability, so the mini price boom is short lived and it peaks at September 2013 at a median price of $375,548. Affordability continues to be a major issue for first home buyers; some make use of FHSAs, many do not. The mini price boom deflates out to March 2016 to finish at the same median price of $334,224.

Given the size of the house price bubble, the degree of indebtedness by Australians (as elegantly covered in Keen 2007), and the degree of credit market disruption caused by the American subprime crisis, **I would consider that the risks to these forecasts are to the downside**, i.e. house price falls are more likely than not to be greater than presented in these forecasts.

But what about the fundamentals – Undersupply and Immigration?

Firstly, lets look at how these forecasts fit with longer term price movements of Brisbane house prices.

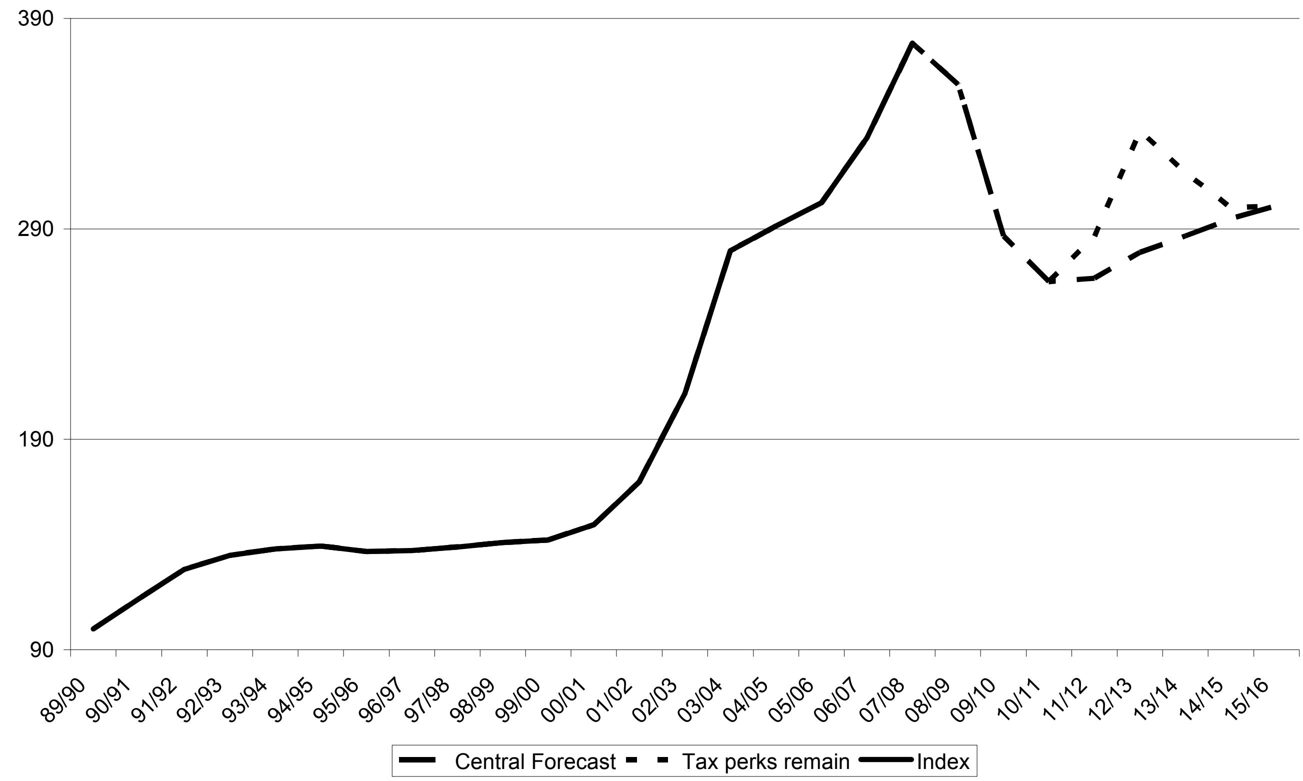

Figure 4. Brisbane median house price index: actual 1989/90-2007/08 (data source: ABS), forecast 2008/09 to 2015/16. 89/90 = 100.

Although the many proponents of property investing will suggest that these forecasts massively underestimate likely future Brisbane house price gains, and investors would rightly be shocked because clearly movements are not what they expected and were told to expect, in the context of long term price movements the forecasts are patently realistic. It is the skyrocketing prices from 2001/02 that appears unrealistic! I don't think anybody in the mid- to late-1990s would have forecast what was about to happen to house prices – then again, who was to know that Greenspan would enact his "put option" and supply liquidity to the world!!

Of course property spruikers and investors will argue against these forecasts based on fundamentals – as all proponents of any particular asset class do to justify their views. If markets were completely rational and always priced on fundamentals, that would be perfectly valid. But it is exceedingly clear that, especially over the last several decades as the globe has been awash with liquidity, markets rarely trade strictly on fundamentals. In fact, it is frequently argued that markets are very rarely priced accurately with respect to fundamentals – and these rare occasions simply mark a fraction of a moment in time as markets swing from overpriced to underpriced and vice-versa. What makes prices flip between the two is market participant psychology – the tendency of people to be optimistic or pessimistic, rolled together with emotions described at their extremes as greed and fear.

So the question needs to be asked: why should markets, from this point in time, move in line with factors which definitely do determine our future need for housing – household formation (dependant on various demographic factors such as population growth rate, both natural and from migration, etc) relative to existing housing? I do not argue that immigration to Queensland is not strong – but it has been for a long time. Ross Barker, director of the Queensland Department of Infrastructure and Planning stated "in terms of growth rates, Queensland has been the fastest of the states for most of the period between 1991 and 2007" (7). He added "overseas migration is now much more significant than interstate migration".

Clearly, house price movements throughout the 1990s did not reflect this fundamental because house prices declined in real terms. Moreover, that current migration levels are more dependent now on overseas migration, and from my understanding, specifically skilled migration under the 457 **temporary** visa scheme, suggests that this form of migration will be very quick to adjust to economic circumstances. Furthermore, as the migrants in question are highly mobile and skilled, in an economic downturn they may well leave to go to better performing economies. And finally, in regards to household formation by Australian citizens, the demographics underlying the increase in household formation may well change abruptly – there is already much discussion of children staying in the family home till later stages in life, but this is probably not all that new a phenomenon, and a deterioration in economic conditions could also lead to lower household formation through "bunching" up. (Certainly there are anecdotal reports of lots of students living together in one house, not unlike some friends I knew at uni in the late 80s!)

So we come back to this question again. When Brisbane house prices over the last 4 decades have shown to strongly follow a boom-bust pattern, and when many international organisations point to Australia as being in the grip of a house price boom, eg. the International Monetary Fund says that Australian houses are overvalued by 25% (See this article [http://www.abc.net.au/pm/content/2008/s2208561.htm] for coverage), is it really reasonable to expect that suddenly at the peak of the biggest house price bubble Brisbane has ever experienced future house price movements will be dictated by fundamentals? Of course the answer is No!

That is what makes it all the more disgraceful that such a well known and trusted Australian bank as the ANZ recently lent its name to an article in a national newspaper entitled "Home Prices to Explode" [http://www.news.com.au/business/money/story/0,25479,23961580-5013951,00.html]. As stated earlier, various industries have much financial interest in there being continued strength in Australia's housing markets. That one of Australia's biggest banks engaged in such an obvious attempt to influence market sentiment suggests two things: a) data at the banks' disposal must confirm that the housing bubble has popped, and in a dramatic fashion; and b) this bank is in a particularly precarious position and has significant concerns over the health of its loan book with the prospect of significant bad loans and writedowns, and thus its profitability is under threat. I would not be an investor in the ANZ going forward!(8)

Many property investors and speculators expecting capital gains from March 2008 prices will be extremely disappointed. Moreover, affordability issues will also impact their ability to raise rents – faced with the prospect of vacancies as rental increases ripple outward from the CBD, causing tenants to move progressively outward and those already in outer suburbs to become homeless – a ceiling to rental increases will be reached when owners decide, through financial realities of their own, they would rather have a stable tenant than attempt to continue to extract large rental increases.

I would suggest that my forecasts may be painted by some vested interests as pro-first home buyer. However, it is significant to note that even my central forecast is not especially good for first home buyers. In March 2001, the ratio of the Brisbane median house price to Brisbane average earnings was 3.95. At March 2008 it was 7.67! Under both forecasts, if Brisbane wages increase at the rate of 4% pa, at the end of the forecast period (March 2016) the ratio will be 4.43, 10% higher than in 2001! And remember, most international studies consider that housing is only affordable when the ratio is below 3!! Clearly, young Brisbane families will continue to have to make difficult decisions about family and their desires of home ownership.

Over the very long term, beyond the forecast period, I do believe that affordability will continue to improve for first home buyers as baby boomers sell down their assets through retirement. The continual supply of existing housing on the market should have a downward impact on Brisbane house prices over the next several decades.

Conclusion

This study and its forecasts show that poor Federal government policy has been, and will continue for a long period to be, damaging to the needs and aspirations of everyday Australians, and dare I say it, "working families". That very much includes the less sophisticated investors that joined the boom late, thereby transferring their current and future wealth to the earlier "smart money" investors.

And that is precisely why the current Australian federal government must finally take action and get rid of these ineffective taxation policies which promote, and provide an opportunity for spruikers to aggressively promote, Australian houses as speculative assets. They are our homes not casino chips!

Some Favourite Quotes

Adam Smith (from PJ O'Rourke, 2007, "On The Wealth of Nations")

"A dwelling house, as such, contributes nothing to the revenue of its inhabitant…….. It cannot yield any to the public, nor serve any function of a capital, and the revenue of the whole body of people can never be in the smallest degree increased by it"

Warren Buffet (Berkshire Hathaway's 1997 Chairman's Letter) [http://www.berkshirehathaway.com/letters/1997.html]

"A short quiz: If you plan to eat hamburgers throughout your life and are not a cattle producer, should you wish for higher or lower prices for beef? Likewise, if you are going to buy a car from time to time but are not an auto manufacturer, should you prefer higher or lower car prices? These questions, of course, answer themselves.

But now for the final exam: If you expect to be a net saver during the next five years, should you hope for a higher or lower stock market during that period? Many investors get this one wrong. Even though they are going to be net buyers of stocks for many years to come, they are elated when stock prices rise and depressed when they fall. In effect, they rejoice because prices have risen for the "hamburgers" they will soon be buying. This reaction makes no sense. Only those who will be sellers of equities in the near future should be happy at seeing stocks rise. Prospective purchasers should much prefer sinking prices."

(Note by Brett – the same goes for property – whether for an investment or for your home.)

Some Recent Property Specific Quotes

Warren Buffet on CNBC Squawk Box (talking about US housing market on CNBC Squawk Box on March 3, 2008)

"And if a house has doubled in price, and somebody lends 95 percent of the price that's doubled in a couple of years, there's a good chance they're going to lose money….. for a while people thought houses could do nothing but go up, so they paid no attention to any other factor..... the person who sold the house [during the bubble] got a bubble-type price….. every time anybody tells about somebody losing a lot of money by selling a house [after the bubble burst], there's somebody else that's buying it at a more attractive price than they would've paid a year or two ago."

Wilbur Ross on CNBC Squawk Box on March 7, 2008

"I think the credit crunch is not only getting worse in the US but it is spreading overseas. I was in England about two weeks ago, and my take of the housing market there is that it is in at least as bad a shambles as what we have in the United States. They had an activity there called "build to let" where little people, not real realestate professionals, but average citizens were building houses, highly leveraged, on speck, with the idea of renting them out. And I don't think that realestate is a very good game to play "Amateur Hour". And it's now coming back to haunt them. So I see the credit crunch spreading to England. Housing prices have been very badly hit in Ireland. Very badly hit in Spain. Even as far away as Australia. So I think "credit crunch" may be one of our big export products near term."

Notes

(1) The term bubble is used as per accepted convention in most national markets, particularly the US, along the lines described by Shiller (2005).

(2) Steve Keen's Debtwatch No. 20 March 2008: Double or nothing? http://www.debtdeflation.com/blogs/2008/03/03/steve-keens-debtwatch-no-20-march-2008-double-or-nothing/

(3) Figures quoted here are from, or have been calculated from, data from the Reserve Bank of Australia, the Australian Bureau of Statistics, and from Case-Shiller. The specific websites I used are – www.abs.gov.au – www.rba.gov.au/calculator/calc.go - http://www2.standardandpoors.com/spf/pdf/index/CSHomePrice_History_062418.xls

(4) http://www.news.com.au/couriermail/story/0,23739,23968923-5011140,00.html

(5) http://www.news.com.au/couriermail/story/0,23739,23954212-953,00.html

(6) Ludlow (2008)

(7) Mr Barker's comments were made at the Australian Population Association's 14th biennial conference and were reported in the Australian Financial Review on 3 July 2008, "WA steals march on Queensland", P10.

(8) As an aside, I always find it humorous how industry's suggested response following financial collapses – such as ACR, Fincorp, etc – always involves "investor education". Really! As if industry really wants us all to be wise to their tricks!!

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[Professer Shiller's website about the book, data and additional information is available at http://www.irrationalexuberance.com/index.htm]