

# **Anatomy of the Australian Housing Bubble: All Eight Australian Capitals Vs Worst Eight US Cities**

Dr Brett F Edgerton

[www.geocities.com/homes4aussies](http://www.geocities.com/homes4aussies)

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## **Introduction**

In response to my first paper comparing the Australian housing bubble – using primarily data for Brisbane – to the United States<sup>1</sup>, many people have emailed and asked me how other Australian cities compare.

In this very brief report I present a comparison of house price growth for all eight Australian capital cities versus the eight US cities which experienced the greatest bubbles (had the highest price peak) in relation to the peak in the Australian and US housing markets.

In my original report, I suggested that the March 2008 quarter would mark the peak of the Australian market, and data reported since shows that Australian house prices declined in the June quarter. This adds further weight to my view as I, and others, expect these declines to continue for some time.

## **Data**

Australian house price data are from the Australian Bureau of Statistics and can be obtained at [www.abs.gov.au](http://www.abs.gov.au) – I used the median house price data for each city and indexed each series with June 1992 = 100. (Data for March and June quarters 2008 are based on provisional quarter on quarter movements.)

US city house price data are from S&P/Case-Shiller and can be obtained at [www.standardandpoors.com](http://www.standardandpoors.com) – indices for individual cities were recalculated with September 1990 = 100.

The data were plotted in 4 graphs after all cities for each country were ranked in terms of house price appreciation over the study period – with the top two Australian cities plotted against the top two US cities, and so on.

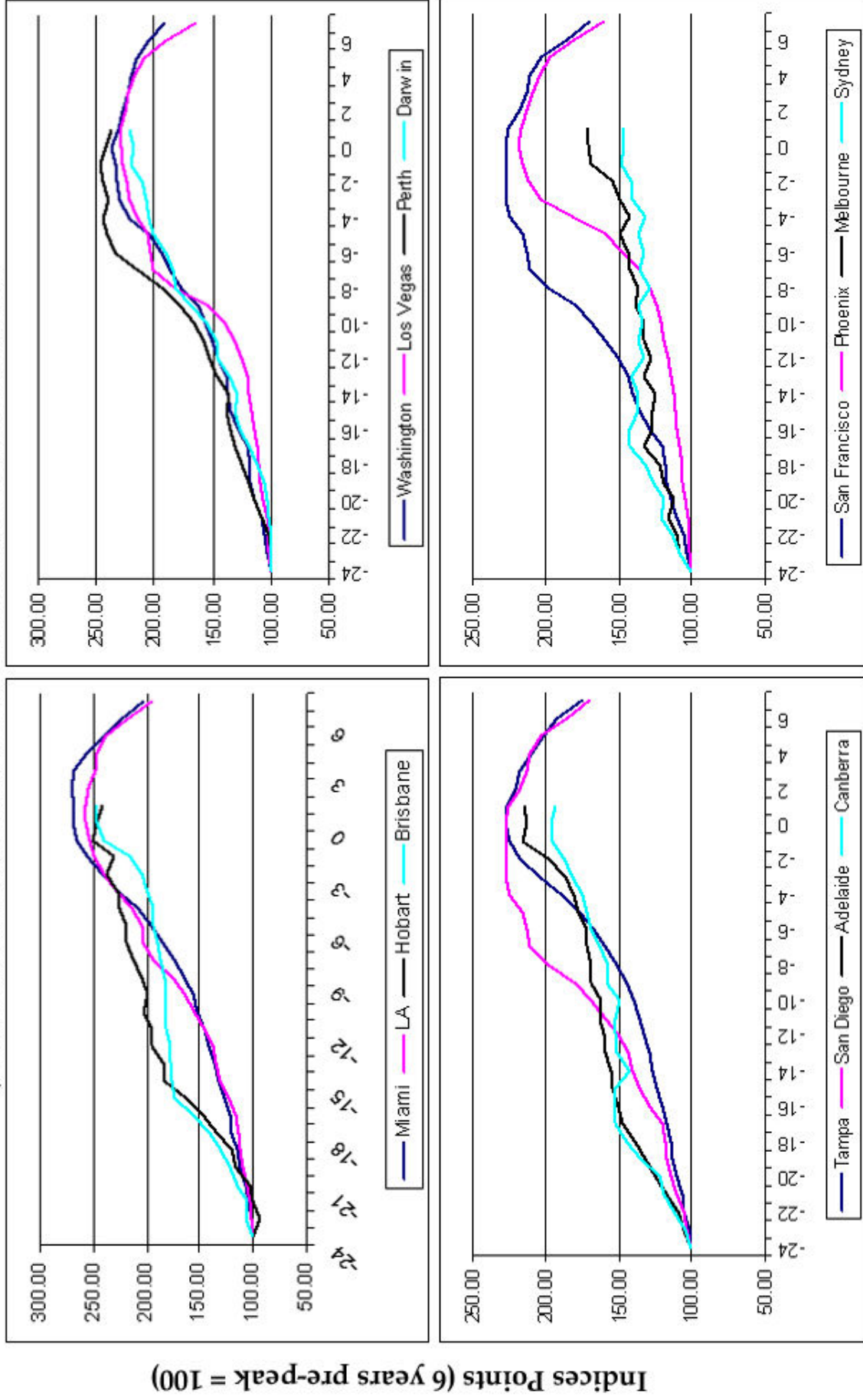
Data for the comparison of the Australian and US housing markets, as “a whole”, were from the same sources. The Australian data are the Weighted Average of Eight Capital Cities, “post-2005 method”, with data pre-2002 from the “pre-2005 method” spliced on following adjustment. The US data are from the “US National Values” series. March 1990 = 100.

## **Results**

House price appreciation for Australian capital cities was remarkably similar to that for the eight US – the exceptional graph being the final one, of Sydney and Melbourne versus the 7<sup>th</sup> and 8<sup>th</sup> US cities (Figure 1). The ranking of Australian cities’ house price appreciation over the period June 2002 to March 2008 (descending) was Hobart, Brisbane, Perth, Darwin, Adelaide, Canberra, Melbourne, Sydney (Table 1).

Figure 1.

### Comparison of House Price Indices of the Top 8 US Bubble Cities and all 8 Australian Capital Cities (Data Sources: Case Shiller and Australian Bureau of Statistics)



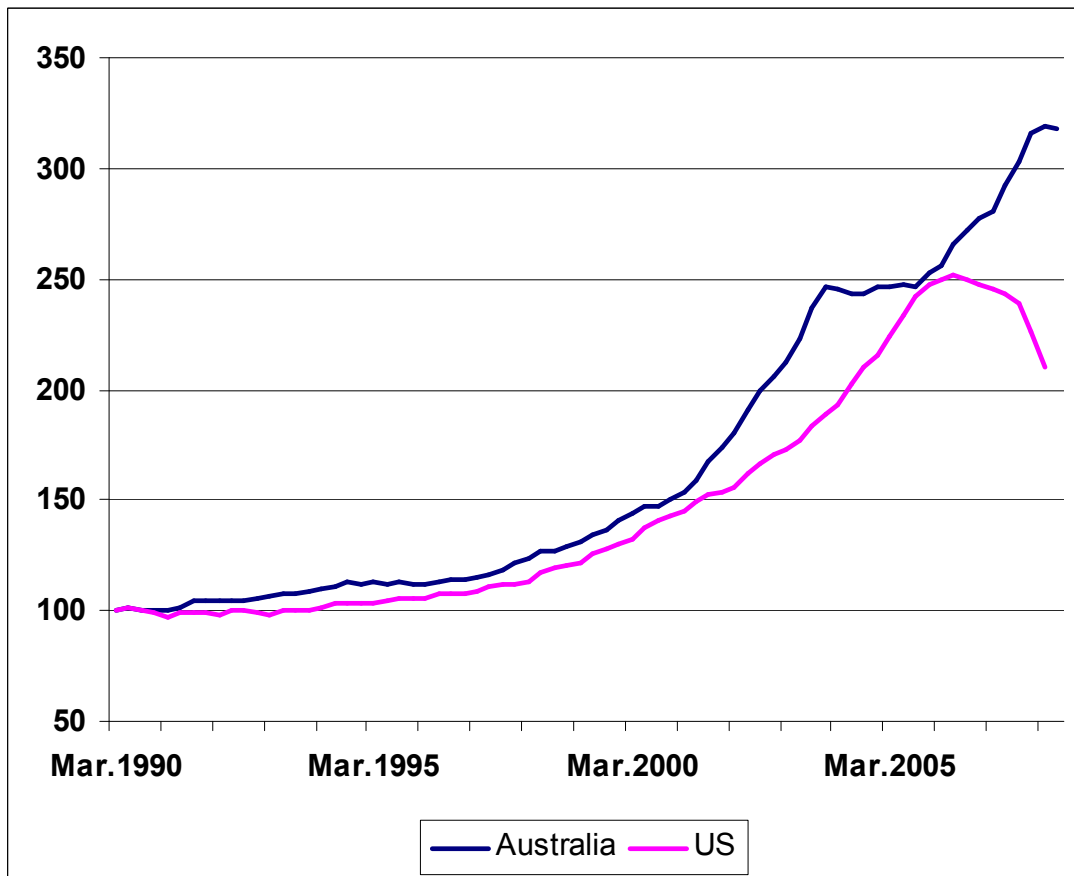
Quarters Relative to Peak (Australia - March 2008, US - June 2006)

Table 1. Peaks in the house price indices (for Australian cities March 2002 = 100; for US cities June 2000 = 100). Time = quarter that the city index peaked relative to national index peak.

City	Index at Peak (Time)	City	Index at Peak (Time)
Hobart	251.42 (-1)	Miami	271.40 (0)
Brisbane	248.35 (+1)	Los Angeles	257.56 (0)
Perth	245.79 (-1)	Washington	236.14 (0)
Darwin	221.08 (+1)	Los Vegas	229.12 (+1)
Adelaide	215.06 (-1)	Tampa	227.77 (0)
Canberra	195.87 (0)	San Diego	227.65 (0)
Melbourne	170.65 (0)	San Francisco	227.65 (0)
Sydney	147.95 (-1)	Phoenix	218.90 (0)

I plotted national indices as a reference point for these analyses (Figure 2). In both countries, house price growth was relatively flat from 1990 to 1998. Obvious in the Australian index, and in several cities' indices, is the fact that the Australian bubble occurred in two phases – the first leg up until December 2003, and the second leg up running from early 2006 to early 2008. The US bubble occurred in one phase. The Australian index at March quarter 2008 was 26.5% higher than the US index peak at June quarter 2006.

Figure 2. Graph of house price appreciation in Australia and the US. (Australia – ABS 8 Capital City Weighted Average; US – S&P\Case-Shiller US National Values; March 1990 = 100).



## Conclusions

America serves as a useful comparison for two very significant reasons – 1) they are further along in the housing cycle than most other countries which participated in the synchronized bubble, having been the epicentre of the credit markets (the fuel for the housing bubbles); and 2) it is now universally accepted that they experienced a very significant housing bubble.

That graphs plotting house price appreciation for six of eight of Australia's capital cities very closely resembles the magnitude of the US cities which experienced the greatest bubbles is absolute proof that Australia has experienced a very large housing bubble.

At a national level, it is clear that Australian house prices appreciated more than US house prices. It should also be noted that the S&P\Case-Shiller National Value Index is considered by many analysts to overstate the US bubble because it is rather narrow (after all, there are 52 state capitals and many other large cities.) On the other hand, the Australian data are the weighted averages of ALL Australian capital cities. Thus this graphical representation would tend to understate the difference.

The breadth of the housing bubble in Australia, and its magnitude and duration, suggest that it was significantly larger than the housing bubble experienced in the US.

Some may be surprised that these data suggest that the bubbles in Sydney and Melbourne house prices were not as great as those in the other capital cities. This may be true to a point. But this is also likely to be due to the anatomy of the Australian house price bubble, and the fact that individual markets in Australia were not as synchronized as in the US.

I would suggest that Australia's housing bubble had its genesis in Sydney in the run-up to the 2000 Olympics. Melbourne also got involved as a tag-a-long – not wanting to be outdone by its arch rival, no doubt. As the population of these two cities constitutes about 40% of the Australian population, this produced the uptick in the 8 city weighted average. Certainly, investing would have been a part of this uptick – housing investing had remained part of the national psyche, with the ongoing negative gearing provisions, even through the long flat period in the market. But it is also reasonable to assume that much of the early stage of the uptick was from owner-occupiers in Sydney and Melbourne.

House price growth in the rest of the country remained flat at least until 2001. In 2000 the Federal Government introduced the capital gains tax concession and this was the catalyst to the housing price appreciation spreading throughout the Australian eastern seaboard. The first home owners grant, which was doubled for a period, was also introduced around the same time and no doubt played a part. I would argue that this point marks the start of Australia's housing bubble.

The house price appreciation in Sydney and Melbourne provided an opportunity for residents of these cities to extract equity and invest in the closer capital cities of Hobart, Brisbane, Adelaide and Canberra. No doubt many investors had noted that these markets had remained comparatively flat since the early 1990s. And, of course, local investors and owner-occupiers also entered the fray once the uptick started.

By March 2002, the start of the graphs in Figure 1, the explosion in house price growth was in full swing in these other centres. Because much of the equity extracted in Sydney and Melbourne was invested in other cities, house price growth there was more subdued. From personal experience, it was common place in 2003 to witness "southerners" attend house inspections in Brisbane, driving from house to house in a rental car or even a taxi.

The internet also played a critical role. Even in my small home town of Innisfail, in north Queensland, there was much talk of “southerners” buying houses sight unseen off the internet. Houses were being sold within a few hours of listing on real estate internet sites. This in a town where through the late 1990s it was common for houses to be listed for sale for several years!

In late 2003 the market slowed significantly. I believe that this was primarily achieved by the “jawboning” from the Reserve Bank of Australia and rate policy action. The RBA was outspoken in its concern for a house price correction, and raised rates in November and December 2003. House price appreciation slowed considerably.

But during this plateau period, Australia began to fully feel the very positive effects of the explosive growth in China, and its consequent demand for raw materials which Australia was able to supply. This prompted the spread of the housing bubble to our most remote capitals – Perth and Darwin – which are proximal to the mines and form the base for many mine employees. Of course, this phenomenon was not restricted to capital cities – house prices in Queensland regional cities such as Mackay and Rockhampton also began to skyrocket.

Although it was local factors that initiated price growth in these markets, there is no doubt that many investors who had enjoyed capital gains from investments in the eastern seaboard again withdrew equity and invested in these much smaller markets. This period also coincided with the rapid expansion in credit availability as mortgage providers increasingly sourced funds from the US securitisation markets. At this time, there were reports in the press of operators chartering aircraft to take investors from the eastern seaboard to Perth to purchase residential properties.

Consequently, house price appreciation in Perth and Darwin very quickly caught up to – and in the case of Perth, overtook – the smaller eastern capitals. Perth price growth stopped fairly abruptly in early 2007 – this coincided with common media reports that the Perth median house price was quickly encroaching on Sydney’s, the premier Australian city. In fact, at 1Q2007 the differential was only \$17,000 (3.7%)!

“Affordability issues” were the commonly quoted reason for the slowdown in Perth house price appreciation. However, I rather suspect that speculators could no longer ignore the sheer absurdity that Perth would very soon have the most expensive housing in Australia – in nominal terms, not just relative to wages – if house price growth continued at the same rate.

The final stage of the inflation of the bubble was when Perth residents began to fly to the eastern seaboard to invest in property. Again, at house inspections in Brisbane in early 2007 I personally spoke to several groups of people from Perth who had flown in for the weekend to buy investment property. Moreover, at the same time there were press articles discussing real estate marketers chartering aircraft to fly investors from Perth to Adelaide and Melbourne on weekends with the express intention of purchasing investment properties.

I would suggest that the ramping up of investor activity in these markets in 2006 and 2007, together with local investors, and easy credit from foreign markets, was the major reason for the acceleration in house price growth in the Brisbane, Adelaide, Hobart and, a little later, Melbourne. The negative news reports of mortgage stress and significant house price declines in western Sydney served as a deterrent to investor activity in greater Sydney.

The main point that I draw from this anatomy of the Australian bubble is that it suggests that a higher proportion of the house buying activity in the smaller capitals was by speculators and investors. Consequently, I suspect that house price falls through the popping of the bubble will be greater in these cities than in Sydney and Melbourne.