

Economic research note

5th February 2009

Housing market to experience divergent price movements over 2009

- According to the Australian Bureau of Statistics (ABS), established house prices fell 3.3% over the year to December 2008.
- Prices will remain weak in 1H09, should stabilise in 2H09 and recover over 2010. However, this outcome will vary considerably across market segments differentiated by pricing tiers.
- While unemployment will rise over 2009 and weigh on prices, this should be offset by the current aggressive easing in monetary policy.

The Australian Bureau of Statistics Home Price Index is the one official measure of residential house prices in Australia.

The data

Prices of established homes in Australia fell 3.3% in 2008; the largest annual fall since the series began in 1987. In real terms, house prices fell 6.7% during the year. Falling annual house prices were observed in all capital cities but Adelaide and Darwin. The most substantial falls occurred in Perth (-6.7%), Sydney (-4.1%) and Canberra (-4.1%). This is highlighted in Figure 1. Positively, it seems the largest falls were in the September quarter as the pace of price falls slowed in the December quarter. This occurred across the national index and in all capital cities but Hobart.

In addition to pricing data, transactional information in November shows that activity is fragmented across the market. As shown in Figure 2, trends in monthly sales data highlights rising sales amongst first home-buyers, though non-first home-buyer demand remains weak. In November 2008, sales of homes to first home-buyers of 11,665 were 32% higher than sales in August 2008. However, on a moving annual basis, sales to first home-buyers fell 11% and sales to non-first home-buyers fell 17% to November 2008. Figure 2 also highlights the period of strong first home-buyer sales that occurred in 2001 and preceded the broader residential price boom of 2003 and 2004.

Figure 1

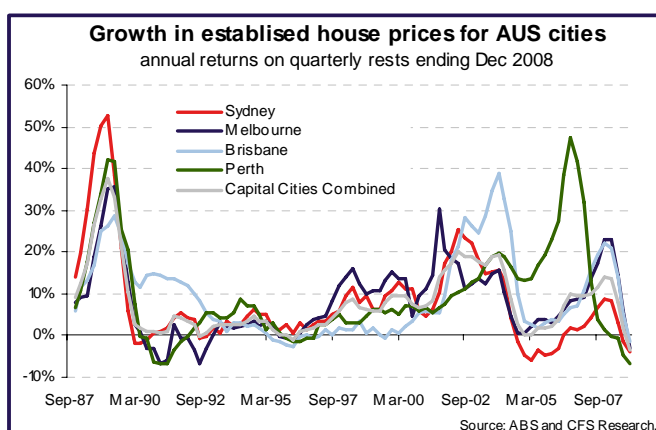
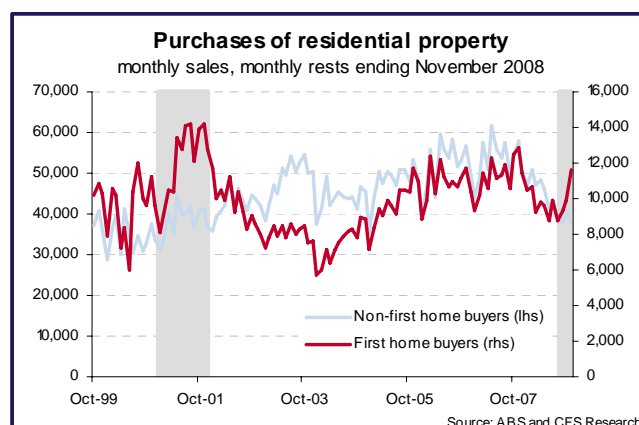


Figure 2

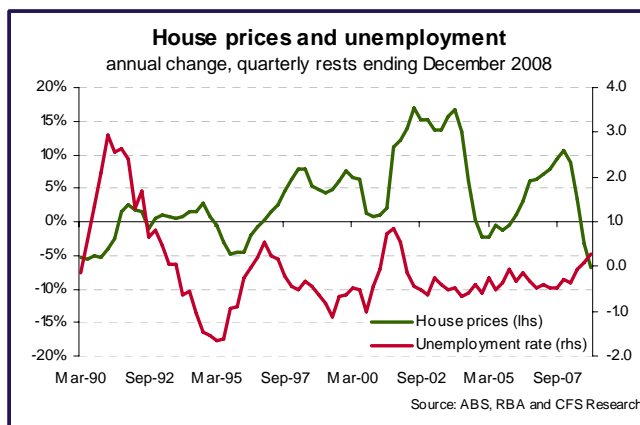


Analysis

The fall in house prices over 2008 was largely due to aggressive monetary tightening and the impact of higher commodity (oil and food) prices on household balance sheets in 1H08. However, in 4Q08 the impact of lower interest rates and the first home-buyers grant appears to have slowed falling house prices.

The state of the labour market is a key risk to the outlook for the broad residential housing market in 2009. The importance of the labour market is highlighted in Figure 3 which shows unemployment and house prices. Figure 3 shows periods of inverse co-movement but also periods where house prices are also influenced by monetary policy. For instance, between October 2000 and October 2001 unemployment in Australia rose from 6.0% to 7.1%, but house prices rose 11.2% in the year to September 2001 and 12.0% for December 2001, a time of falling interest rates. While we expect the unemployment rate to rise towards 6% over 2009 and weigh on prices, this should be offset by the current aggressive easing in monetary policy.

Figure 3



The outlook for prices at the top end of the market is gloomy due to substantial falls in upper quartile household wealth as a result of the equity market crash and rising unemployment in financial services. House prices in up-market areas such as Sydney's eastern suburbs and lower North Shore are experiencing substantial price falls.

In 2009 Australia is unlikely to see a broad-based fall in house prices. Prices will remain weak in 1H09, should stabilise in 2H09 and recover over 2010. However, this outcome will vary considerably across market segments differentiated by pricing tiers.

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Contact details

Anthony De Francesco	Head of Research	+612 9303 3598
James White	Investment Economist	+612 9303 2645
Mary Culjak	Research Assistant	+612 9303 3518

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