Welcome to CoreLogic’s update on the housing market for May 2018. Nationally dwelling values continued their downwards trend last month; the seventh consecutive month on month decline since the national index series peaked in September last year.

While the national market has slid into reverse, many of the trends we have been following over the past five years have reversed. For example, regional housing markets are now outperforming the capital cities. Also, the unit sector has taken over from houses as the best performed, at least in Sydney and Melbourne, where affordability constraints are the highest. Another change has been that the lower priced end of the market is now showing better conditions than higher priced properties, which is likely the result of more first home buyers as well as affordability barriers preventing more activity across the higher price points.

These trends aren’t always uniform across each of the capital cities and regional markets.

Generally we are seeing growth conditions showing a mild pick up across the regional markets while capital city markets ease. CoreLogic indices show the combined regional markets recorded a 2.4% rise in dwelling values over the past twelve months while capital city values were down 0.3%. On a rolling quarterly basis, the performance gap is getting wider, driven by strong conditions across the major centres within close proximity to Sydney and Melbourne, as well as more demand flowing into regional coastal and lifestyle markets. Additionally, regions linked with the mining sector are showing signs of bottoming out, creating less drag on the headline growth rates across the mining states.

Looking at the performance based on housing types, units are now broadly outperforming houses, either by showing higher capital gains or more resilience to falling prices. While this is the case at a national level, it’s really Sydney and Melbourne, where the pricing gap between houses and units, as well as a surge in price sensitive first home buyers are supporting growth in unit values over house values. Every other capital city has seen house values outperform the unit market over the past twelve months.

While the most expensive properties are showing the weakest conditions across most cities, in Perth and Canberra it’s actually the most affordable end of the market that has underperformed relative to other broad value based segments.

The falls in home values are very much concentrated within the two largest cities, Sydney and Melbourne, where dwelling values had previously been rising the quickest. Since peaking in July last year, Sydney home values are down a cumulative 4.3% and Melbourne values have fallen by 1.1%. These are also the cities where investment activity has been most concentrated, highlighting that tighter credit conditions for investors has played a large role in slowing the market.

While Sydney and Melbourne are experiencing the most substantial and consistent falls, most other capital cities have also seen the rate of capital gains easing over the year to date or they have shown subtle falls. Over the first four months of 2018, dwelling values have nudged lower across Brisbane, Adelaide and Perth, while Darwin and Canberra have recorded a subtle gain. The only market showing a consistently high rate of growth is Hobart, where values are 4.6% higher over the first four months of the year.

As housing market conditions generally ease, other key indicators have also softened, including the number of settled sales, auction clearance rates and credit flows. Additionally, advertised stock levels have shown a substantial rise in Sydney and, to a lesser extent, Melbourne.

Nationally, settled sales are down 5.7% year on year. Although there will be some upwards revision as off the plan unit sales move through to settlement, it’s clear that there are fewer buyers active in the market. Sydney has seen the largest year on year fall in settled sales activity, with volumes down 12.3% relative to the previous 12 month period.

Clearance rates, have generally been holding around the mid 60% range through most of 2018. More recently, clearance rates have been trending lower, with the final week of April seeing Sydney’s clearance rate dip to 56% and Melbourne clearance rates are also on a clear downwards trajectory. The lower clearance rates highlight that selling conditions have weakened over the past month.

Unsurprisingly, housing credit, which is a key indicator of market activity, has remained weak. The Reserve Bank figures show annual growth in housing credit has reduced to 6.1% per annum, the slowest rate of growth since March 2014. Weaker credit growth is the result of less investment activity, with annual growth in investment lending tracking at just 2.5% compared with owner occupier credit which is up 8.1% over the past twelve months.

The slowdown in investment has been ongoing since the first round of macroprudential changes in December 2014. Although APRA has recently announced they will lift the ten percent limit on investment credit growth for eligible banks on July first, we aren’t expecting there to be a rebound in investment lending due to overall tighter credit policies, with more focus on debt serviceability, restrictions on interest only lending and a general requirement for keeping low deposit lending to a minimum.

Now let’s take a look across the capital city housing markets in more detail.

Australia’s largest housing market, Sydney, has continued its slow melt, with dwelling values slipping 0.4% lower over the month to be down 4.3% since the market peaked in July last year. House values have worn the brunt of the downturn, falling 5.8% since peaking, while unit values have seen some support, down a less substantial 1.4% since peaking, as buyer demand remains stronger across the more affordable price ranges. As the market slows, the typical selling time for private treaty sales has pushed higher, reaching 36 days at the end of March compared with 31 days twelve months prior. The longer selling time is also visible in advertised stock levels which are now tracking 26% higher than a year ago.

In Melbourne, the market’s resilience to a downturn seems to be wearing off, with month on month declines gathering some momentum. Dwelling values were down 0.4% in April, taking values 1.1% lower since peaking in November last year. Similar to Sydney, the local unit market, where price points are more affordable, has shown some relative strength, in fact unit values across Melbourne remain at record highs after rising 0.2% over the first four months of the year. As the market softens, listings numbers are tracking higher, up 5.1% relative to last year. Despite the rise in inventory, private treaty selling time remains very low at just 29 days and discount rates are also low, tracking at 4.7%, suggesting vendors are still holding some leverage in the selling process.

The Brisbane housing market has remained relatively flat over the first four months of the year. Dwelling values are down 0.1% so far this year, in essence a flat result. The Brisbane unit market is been under a lot of focus due to high supply levels across key inner city suburbs, and overall, Brisbane unit values remain almost 12% lower than where they were ten years ago. Despite the long term weakness, Brisbane unit values have edged higher over the first four months of the year, rising 0.1%. While it’s probably too early to signal the local unit market has turned a corner, it’s important to note that unit construction activity peaked almost two years ago and new supply additions are now tapering as population growth picks up.

The Adelaide housing market saw values edge 0.1% higher in April, however the market is down 0.4% over the first four months of the year. Despite the relatively steady conditions, settled sales have tracked 3.2% higher year on year across Adelaide and activity is now outpacing the decade average. As buyer numbers rise, advertised inventory levels have reduced across the city, falling by 5.8% relative to the same time last year. The lower stock levels suggest vendors may see some improvement in selling conditions, although the average time on market for private treaty sales remains elevated at 56 days.

Perth dwelling values held firm in April, with both house and unit values remaining steady over the month. While the result remains soft, the Perth housing market is showing a variety of signals that it has moved through the bottom of its downturn. Average selling time has reduced over the year, from 65 days down to 55 days, advertised stock levels are falling, down 4.3% compared with the same time last year, and year on year transaction volumes are rising off a low base, up 3.3% over the past twelve months. While it looks like conditions are levelling out, we are still seeing relatively weak demographic trends with regards to the interstate migration outflow. With housing now very affordable and jobs growth improving we would expect the rate of interstate migration to improve over the coming year which will provide a further boost to housing demand.

The Hobart market continues to power ahead with dwelling values surging another 1.2% higher in April to be 4.6% higher over the year to date and 12.7% higher over the past twelve months. The house market is showing stronger growth conditions than units, with house values up 13.6% over the past twelve months while unit values are up 8.2%. Rental conditions are also very buoyant, which is keeping Hobart’s rental yield high, despite the high rate of capital gain. Gross rental yields for houses are tracking at 5.0% which is the second highest of any capital city after Darwin.

The Darwin housing market has edged back into positive growth territory, with dwelling values rising 0.7% over the past three months to be 0.5% higher over the year to date. Considering the small size of the Darwin market, housing indicators show higher volatility than other capital cities, so we probably need to see a few more months of positive change before we can be more confident the top end capital has moved through its prolonged correction. Darwin dwelling values remain 21% below their 2014 peak.

Canberra is one of only three capital cities to record a rise in dwelling values over the first four months of the year, with the market rising by half a percent over the year to date. Despite recording some subtle growth, a year ago values were 2.7% higher over the same time frame. Despite the subtle rise, the number of settled sales is down almost 9% year on year and homes are taking longer to sell at 46 days compared with 40 days a year ago. In balance, listing numbers remain low and migration rates are strong which is likely to help keep a floor under home prices.

Overall, the weaker conditions across the capital cities are likely to be mostly attributable to tighter credit conditions, particularly for investors who have been faced with mortgage rate premiums, restrictions on interest only lending and more recently, stricter servicing requirements. To highlight the slowdown in investment, annual growth in investor mortgages has fallen to just 2.5%, well below the recent peak of almost 11% growth per annum in early 2015, which was just after the first round of macro prudential tightening.

Of course other factors are at play as well in dampening housing market conditions. Despite lower prices, housing affordability remains a pressing issue, especially in Sydney and, to a lesser extent, Melbourne. Our latest dwelling price to income ratios put Sydney dwelling prices 9.3 times higher than gross household incomes, and Melbourne prices are 8.0 times higher than household incomes. Other capital cities are showing much lower ratios highlighting that housing prices haven’t outpaced income growth as much. In fact, on this measure, housing affordability has improved substantially across Darwin and Perth as dwelling prices have trended lower and incomes have posted a modest rise.

The outlook for the housing market will be largely dependent on how credit policies play out with regards to bank appetite for lending. Although APRA has announced it will lift the first macro prudential policy; a 10% speed limit on investment credit growth, we aren’t expecting this to have a material impact on credit availability.

Lenders are likely to be focusing more on overall debt serviceability, validating borrower expenses and incomes, minimizing high debt to income loans and low deposit loans, all of which will keep a lid on credit growth, especially for investors who still face mortgage rate premiums and less opportunity to secure a loan on interest only terms.

Add to this the uncertainty of a federal election which will be held sometime over the next twelve months. No doubt there will be further debate around taxation policy as it relates to housing. Changes to negative gearing and capital gains tax policies could pose a further headwind for the housing market, should they be introduced.

It sure is interesting times. If you would like to stay up to date with the latest trends in the housing market, you will find plenty of research content at www.corelogic.com.au.

Short version

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Another emerging trend is that the most expensive properties are leading the downturn, while properties at the more affordable end of the market have generally been more resilient to falls. While the most expensive properties are showing the weakest conditions across most cities, in Perth and Canberra it’s actually the most affordable end of the market that has underperformed relative to other broad value based segments.

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Of course it isn’t just credit policy working to slow down housing conditions. Despite lower prices, housing affordability remains a pressing issue, especially in Sydney and, to a lesser extent, Melbourne. Our latest dwelling price to income ratios put Sydney dwelling prices 9.3 times higher than gross household incomes, and Melbourne prices are 8.0 times higher than household incomes. Other capital cities are showing much lower ratios highlighting that housing prices haven’t outpaced income growth as much. In fact, on this measure, housing affordability has improved substantially across Darwin and Perth as dwelling prices have trended lower and incomes have posted a modest rise.

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