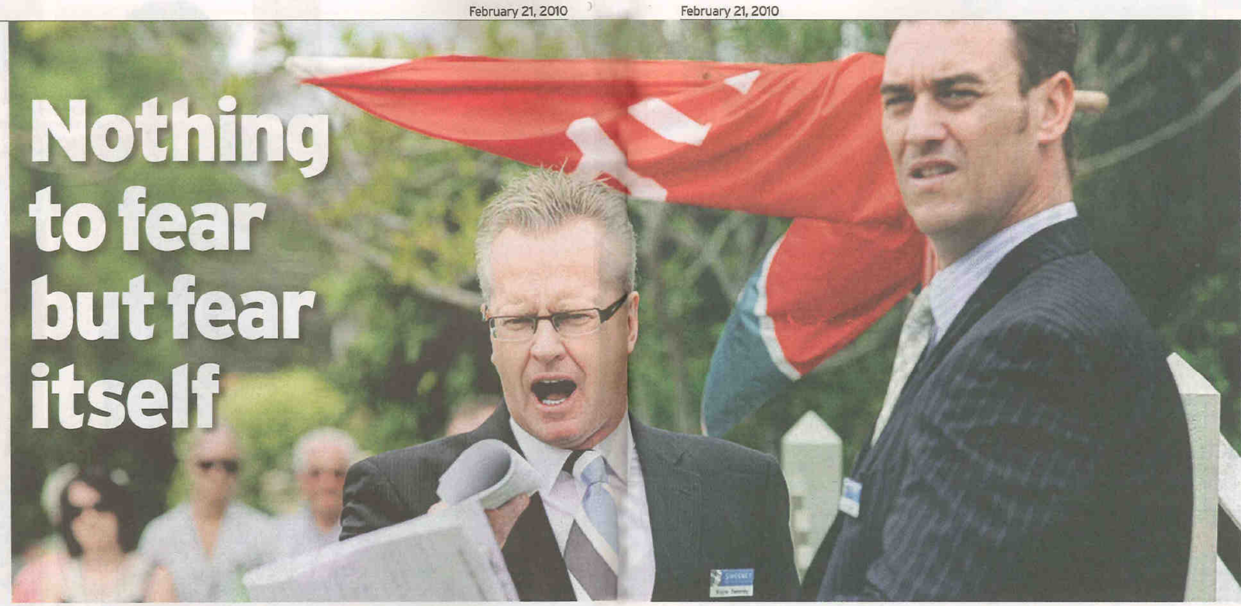
OVERVIEW

Nothing to fear but fear itself

Solid demand, rising prices and some potentially risky conditions characterise the market at present, writes **Chris Vedelago.**



IF THERE is one lesson to be learnt from 2009, it's that reading the property market is much more of an art than a science. In hindsight, it's hard to overplay the stark difference between how 2009 turned out versus what was feared when the year opened. The 2008 global financial crisis, which has so ruthlessly crippled developed economies throughout the world, was threatening to wreak the same kind of havoc in Australia. Everywhere there was a sense of impending doom.

Fortunately, however, we were spared the worst effects. Sure, there was pain: the share market tumbled but the financial system didn't fail; unemployment rose but didn't blow out; property prices fell but the market didn't collapse.

Instead, seemingly against all odds and defying the worst predictions, not too far into 2009 — and following deep cuts to interest rates and billions of dollars in stimulus spending — things started to look up.

Nowhere was this clearer than in Melbourne's residential property sector. Veteran market watchers were shocked to see a tentative recovery in early 2009, which transformed into a near record-setting run by the end of the year.

Analysts don't agree on how much property prices rose, but none dispute that it became one of the strongest years in the past decade.

House values reportedly rose by 14.25 per cent or 14.9 per cent at the metropolitan level in calendar year 2009, according to Residex and RP Data-Rismark. Australian Property Monitors (owned by Fairfax) said growth was as high as 18.5 per cent.

For units/apartments, the three groups said growth ranged from 11.5 to 18 per cent.

However, the Real Estate Institute of Victoria, which compiled the data used in the Domain Property Review, said growth was more subdued when viewed over the year to January 31, 2010, the most current figures available (before publication).

The REIV reports median prices rose 4.3 per cent for houses and 9.2 per cent for units/apartments at the metropolitan level: "2009 was a year of extreme movement in the market [but] sometimes statistics alone can't tell the whole story," REIV chief executive Enzo Raimondo said. "These median figures cover that entire period and as a result do not reflect the amount of growth achieved in the final quarter of 2009."

Statistics also can't convey the radical transformation in the market as it was experienced at the coalface. Highly competitive auctions returned to areas of the city that had gone quiet or had been almost wholly given over to low-key private sale campaigns. This change was obvious in the middle suburbs, where auctions became a favoured sales method only during the 2007 boom, and at the top-end, where cost- and failure-conscious vendors had turned to off-market deals during the downturn.

Fear of failing to sell at auction, which was the most conspicuous sign of the collapse of confidence in the 2008 downturn, was soon replaced by complaints that there weren't enough properties to go around. The REIV reports that auction clearances averaged about 81 per cent in 2009, compared to 82 in 2007 and 63 per cent in woeful 2008. It became a common refrain that Melbourne's auction market had never been hotter, with even low-quality properties attracting multiple bidders and selling for well above vendors' (increasingly unrealistic) expectations.

By the end of the year, as the Domain Property Review will show in its market segment reports, the recovery had spread to virtually all corners of the Melbourne residential market. So strong did demand and price growth become that some in the industry began openly talking of a "new boom" that could rival the heady days of 2007.

So how did it happen? Too many buyers for too few properties. It's as simple as that.

There's no escaping that the near-record sales levels and exceptionally rapid and strong price growth in 2009 was the result of a huge, artificially driven influx of new buyers into a market that was experiencing a serious housing shortage. For several years already, Melbourne's supply versus demand equation had been out of balance, because of a combination of rapid population growth (now about 1700 people a week), an extremely tight and pricey rental market and a chronic inability to build enough houses or apartments to deal with either.

Then the 2008 global financial crisis led to some extraordinary interventions in the economy — the Reserve Bank slashed interest rates to a 49-year low, and first-home buyers received huge government incentives, which pushed legions of shoppers into the property market without fundamentally improving supply.

(Despite significantly higher first-home grants for building new houses, Melburnians continue to prefer to buy established homes.)

Peter Lock, St George Bank's managing director for Victoria, said tight financial regulations and early interventions played a vital role in limiting the damage the crisis had on the economy and property market. "That did underpin confidence and, importantly, when it comes to home loans, confidence is reflected through job security and employment," Mr Lock said. "[With the low interest rate and first-home buyer grant] people worked out that it was a pretty attractive proposition to come into the market."

For the first time in decades, the gap between the cost of meeting a mortgage repayment and paying rent closed significantly. Price falls also opened up individual buying opportunities that didn't exist before the crisis.

"With the benefit of hindsight, it was probably the perfect opportunity — if you had a secure job — to get into the market, at least in the early part of the year," said Robert Papaleo, research director for Charter Keck Cramer. "It pulled a lot of people into the market well ahead of when they otherwise could have bought, sometimes years ahead."

The effect was like a snowball rolling downhill. First-home buyers, flush with government cash and facing what looked like a long period of low-interest repayments, flooded into the lower end. Melbourne's outer suburbs, which had been characterised by stagnant or moderate price growth, became the best-performing market in early 2009, according to RP Data.

Then, owner-occupiers took advantage of rising prices and low interest rates to upgrade or downsize. Investors, who fled at the first signs of the crisis, began circulating again. "The pace of growth in these outer markets slowed by the middle of the year, with more expensive markets gathering pace as the economy and buyer confidence improved," RP Data research director Tim Lawless said.

What had begun as emergency measures eventually fuelled soaring prices across much of the city. Adding to the momentum were changes to foreign investment regulations that made it easier for overseas buyers to get into the domestic market, increasing competition and putting supply under further pressure.

"With all of those factors at work, there was only one way for the market to go, and that was up," said Peter Thomas, chief executive of Stockdale Leggo.

Meanwhile, the housing drought won't end soon — Victoria was 8800 new dwellings short of meeting demand from rising population by late 2009, according to the Housing Industry Association — and the lack of supply is expected to continue to drive the market in 2010.

Agents and buyer advocates are already reporting that swelling open-for-inspection numbers have made this January one of the busiest on record.

But far less clear is how well the Melbourne market will perform this year, although the consensus seems to be that we shouldn't expect a repeat of late 2009.

Most of the analysts and economists consulted by the Domain Property Review forecasted only moderate, single-digit price growth for 2010, possibly because of many of the special circumstances that made 2009 such a bumper year are disappearing.

The RBA has lifted the interest rate three times and, despite holding off in February, more rises have been promised as the economy returns to "normal" pre-crisis conditions.

Although lending rates are coming from an unusually low place, the big question is how well homeowners will be able to absorb multiple increases over a relatively short period, even if they are returning the interest rate to a "normal" level.

The First Home Buyers Grant has also been wound back to its pre-crisis level (apart from the still-sizeable amount on offer by the Victorian government for new house construction).

"Demand is pretty solid but I still think there's a risk in terms of just how far interest rates go up and how much first home buyer demand drops off ... which is important to continue that funnelling effect through to higher prices," said BIS Shrapnel analyst Angie Zigomanis. "[But] population growth is strong and there's not enough new houses being built to keep them out of the market for too long."

RP Data suggests that as Melbourne led the property market into a new growth cycle, it's likely to be one of the first areas to "wind down" to a "much more subdued rate of growth".

Then there is the potential fallout that could be caused by last year's soaring prices and pent-up demand. "Affordability will become a major issue in 2010 as growth in wages fails to keep pace with the surge in property prices that has occurred during the last 12 months," said Greville Pabst, chief executive of valuer WBP Property Group.

Martin North, managing director of Fujitsu Consulting, who developed the "mortgage stress-o-metre", said that as many as 40 per cent of the 250,000 first-home buyers who entered the market at the national level since late 2008 could experience "mortgage difficulty" by the end of 2010. "If you're one of those people who stretched to take advantage of low interest rates and government incentives, potentially you're going to have a very sorry time over the next 12 to 18 months," he said. "If you aren't in the market and trying to save to get in, [interest rates and high prices] are going to make it tougher.

"But if you're in already, you've got good levels of income and everything is looking sweet [with the economy], then you're going to be able to gain some real capital appreciation."

Disclaimer
The REIV statistics quoted throughout this report, the Coastal and Country reports – and in the A-Z suburb listings – compare Melbourne's median house and unit and apartment prices for the year ended January 31, 2010, and differ from those quoted throughout the other reports in the Domain Property Review. These use REIV statistics that track price growth over the 12 months to December 31, 2009.

GETTING THE DATA

REIV quarterly or annual median price figures are calculated by finding the "middle" number after the prices of all houses or units sold in a given area are ordered from lowest to highest. The REIV estimates it captures about 70 per cent of all sales, with the sale prices reported voluntarily by member agents.

APM uses a "stratified" or "mix-adjusted" methodology that counters the biases found in straight median price measures that occur when different types of properties are sold at different times. Suburbs in each city are divided into groups based on their long-term price level, and a median price is calculated for each group based on the property sales that happen over a quarter or year. The metropolitan median is a weighted average of the median prices from all the groups.

RP Data-Rismark uses a "hedonic regression" methodology that calculates the median using recent sales data combined with information about the attributes of individual properties such as the number of bedrooms and bathrooms, land area and geographical context of the dwelling. By deconstructing a property into its constituent parts, the company says a much more reliable and accurate representation of capital movements in property values can be calculated.

Residex calculates its median using a "non-revisionary repeat sales index" that tracks the purchases and sales of every property. The methodology then takes "sale pairs" on every property with two or more sales and measures the growth between those sales, employing a form of statistical linear regression to calculate monthly, quarterly and annual growth rates.
CHRIS VEDELAGO

HOUSES

Most Expensive*

Suburb	Median
Toorak	$2,500,000
Brighton	$1,660,000
Canterbury	$1,660,000
Armadale	$1,602,500
Malvern	$1,500,000
Eaglemont	$1,453,500
Middle Park	$1,452,500
Balwyn	$1,397,500
Kew	$1,346,000
Hawthorn	$1,317,500

Most Affordable*

Suburb	Median
Norlane	$160,500
Corio	$200,000
Melton South	$221,000
Melton	$225,000
Frankston North	$237,500
Kurunjang	$241,000
Werribee	$261,000
Melton West	$266,000
St Albans Park	$267,000
Wyndham Vale	$275,000

Greatest 1-year Growth*

Suburb	Median	%
Armadale	$1,602,500	25.7%
Broadmeadows	$330,000	24.5%
Hughesdale	$775,000	24.0%
Clifton Hill	$817,500	23.9%
Dallas	$296,000	23.3%
Eaglemont	$1,453,500	22.5%
Black Rock	$1,270,000	22.1%
Mont Albert Nth	$801,000	20.9%
Footscray	$542,575	20.6%
Abbotsford	$716,000	19.3%

Least 1-year Growth*

Suburb	Median	%
Sorrento	$700,000	-12.5%
Mentone	$635,000	-10.7%
Torquay	$516,000	-8.3%
Gisborne	$423,000	-5.5%
Rosanna	$561,000	-4.9%
Ascot Vale	$619,000	-4.8%
Toorak	$2,500,000	-4.6%
Parkdale	$625,000	-3.8%
Keilor	$510,000	-3.8%
Ormond	$790,000	-3.7%

Greatest 5-year Growth*

Suburb	Median	% (AGR)
Armadale	$1,602,500	16.0%
Balwyn	$1,397,500	15.9%
Malvern	$1,500,000	14.9%
Hughesdale	$775,000	14.7%
Footscray	$542,575	12.9%
Hawthorn	$1,317,500	12.8%
Maribyrnong	$722,000	12.8%
South Yarra	$1,190,000	12.5%
Middle Park	$1,452,500	12.3%
Mont Albert Nth	$801,000	12.1%

Least 5-year Growth*

Suburb	Median	% (AGR)
Mt Martha	$541,000	2.0%
Lysterfield	$537,000	2.9%
Geelong East	$312,500	3.0%
Grovedale	$300,000	3.5%
Werribee	$261,000	3.7%
Mt Eliza	$645,000	3.8%
Point Cook	$423,000	3.9%
South Morang	$367,000	4.0%
Melton	$225,000	4.0%
Taylors Hill	$395,500	4.2%

UNITS & APARTMENTS

Most Expensive*

Suburb	Median
Balwyn North	$820,000
Beaumaris	$779,250
Black Rock	$713,750
Brighton	$709,000
Brighton East	$707,500
Toorak	$672,000
Port Melbourne	$660,000
Balwyn	$626,000
Hampton	$590,000
Bentleigh East	$575,000

Most Affordable*

Suburb	Median
Cranbourne	$226,000
Werribee	$234,000
Carlton	$240,000
Frankston	$244,250
Sunbury	$252,500
Belmont	$254,250
Carrum Downs	$262,500
St Albans	$265,750
Langwarrin	$275,000
Sydenham	$275,100

Greatest 1-year Growth*

Suburb	Median	%
Murrumbeena	$482,750	33.2%
East Melb	$545,000	32.1%
Black Rock	$713,750	28.0%
Fairfield	$387,500	27.9%
Eltham	$445,900	26.0%
Box Hill North	$517,500	25.0%
South Yarra	$549,000	24.8%
Ivanhoe	$510,000	24.5%
Northcote	$418,250	23.7%
Beaumaris	$779,250	23.7%

Least 1-year Growth*

Suburb	Median	%
Carlton	$240,000	-25.0%
Williamstown	$410,500	-13.0%
Camberwell	$535,000	-7.0%
Brighton East	$707,500	-4.7%
Malvern East	$460,500	-4.1%
Hughesdale	$441,000	-1.3%
Flemington	$297,000	-1.0%
Collingwood	$456,000	0.2%
Yarraville	$387,750	1.4%
St Kilda West	$377,750	2.1%

Greatest 5-year Growth*

Suburb	Median	% (AGR)
Braybrook	$398,000	11.3%
Bentleigh East	$575,000	8.3%
Altona North	$413,500	8.1%
Chadstone	$513,000	8.1%
Springvale	$350,000	7.8%
Maidstone	$410,000	7.5%
Balwyn North	$820,000	7.2%
Heidelberg Hgts	$446,000	6.9%
Heathmont	$402,500	6.6%
Mt Waverley	$555,000	6.2%

Least 5-year Growth*

Suburb	Median	% (AGR)
Toorak	$672,000	-16.2%
Hawthorn	$440,500	-9.4%
Armadale	$478,000	-8.9%
Kew	$507,000	-8.2%
Hawthorn East	$472,500	-8.2%
Elwood	$467,500	-8.1%
Malvern	$493,125	-8.0%
Brighton	$709,000	-7.6%
Glen Iris	$470,000	-6.1%
Caulfield Nth	$500,000	-5.9%

* Only suburbs with a minimum of 50 sales reported in the relevant period(s) are included