



Property still the favourite

The nation loves brick and mortar, so much so it actually defines consumer spending, reports KARINA BARRYMORE

AUSTRALIANS love property. It is our favourite investment, the foundation of family wealth and has a huge emotional pull – unlike some of our international cousins who are not so fussed about owning their castles.

Now new research backs up our view that property really is the be all and end all in Australia.

In fact, property dictates our wider economic conditions, not the other way around.

A 34-year study of Australian property markets, *Unlocking the Riches of Oz*, has identified rises and falls in the economy follow those in the property market by between 12 and 24 months.

In other words, “the tail is wagging the dog”, the report’s author and Land Values Research Group director Bryan Kavanagh said.

“The revelation makes it possible to forecast economic booms and busts,” Mr Kavanagh said, by watching where the property market is heading.

So do our pockets of rapidly rising property prices signal we are in for an even greater economic boost as we go on a spending spree? Possibly.

property

National Australia Bank chief economist Alan Oster said property prices do impact on people’s perception of wealth and, therefore, their spending habits.

This has a wide economic impact, as people decide to either spend more or spend less.

According to Mr Oster, property prices more than anything else affect spending patterns, often with major economic consequences.

“Changes in house prices affect people’s perception of wealth,” Mr Oster said.

“Research we have done suggests that if house prices move by 10 per cent either way then consumption activity overall will change by around 1.2 per cent.

“And consumption is two-thirds of total gross domestic product.

“So if someone tells you your house is now worth \$100,000 more than you thought, on average the Australian consumer will spend \$10,000 more than if they hadn’t known the higher value.

“Roughly, that’s about three

times the size of impact a change in the equity markets would have on consumer spending.

“House prices have a much more powerful impact on the economy.”

Independent valuer and research company Charter Keck Cramer agrees that people react to property prices in a very strong way.

“People feel wealthier because their asset is worth more than previously. It can result in greater consumer spending because there is less incentive to save because they’ve got an appreciating asset,” Charter senior economist Andrew Ballantyne said.

However, extending this theory to imply that an economic bust could soon follow these price rises, was not necessarily the case.

Any slowdown will limit subsequent belt tightening to those households which generally have higher average incomes and can probably better weather any perception for the need to cut spending.

Current price growth was also based on strong demand from owner-occupiers, not hype from overactive investors, Mr Ballantyne said.

the big picture

VERN GOWDIE



Fool’s gold

Here’s a mantra; don’t be greedy, don’t be gullible

THE recent demise of ACR together with the collapses of Westpoint and Fincorp has provided investors with a jolt of reality.

In an environment of economic prosperity and share markets’ returning 20 per cent plus per annum, it has been easy to forget that return comes with risk.

The promise of 9 to 10 per cent per annum returns from the aforementioned companies did not carry a wealth warning sign. Investors thought these returns could be achieved without risk.

Unfortunately these high profile collapses demonstrate how cruel financial markets can be. There are a number of stories about investors losing their life savings. Investors

the average yield from the listed property trust sector is 5.44 per cent and the average yield from the ASX 200 is 3.6 per cent.

For the purpose of this exercise there are three investors each with \$100,000.

Investor A invests their \$100,000 into a 10-year government bond and receives income of \$6260.

Investor B invests into listed property sector and receives \$5440, while Investor C invests into the ASX 200 and receives \$3600.

Investor A receives \$820 more than Investor B and \$2660 more than Investor C.

Investor A’s capital and interest

“At some point, financial gravity will kick in and markets will come back down to earth with a thud.”

were ignorant or chose to ignore the golden rule of risk/return; either way their capital is now a fraction of what it was.

Regular readers will know that I have been cautious on the direction of the share market for exactly the same reason. Investors chose to ignore or are ignorant to the fact share markets do not rise at a rate of 20 per cent plus per annum.

At some point financial gravity will kick in and markets will come back to earth with a thud. Unfortunately the higher markets go, the more exuberant the investor becomes and the more foolish the investment activity.

When this current market cycle unwinds we will hear the horror stories of investors who over-borrowed to invest in what they thought was a sure thing.

The warning signs are out there in the current yields that the various asset classes are paying. At present a 90-day bank bill is 6.36 per cent, a 10-year government bond is 6.26 per cent,

are guaranteed by the Australian government, the other two investors are subject to market forces. Why would investors B and C invest in property and shares? Obviously they feel the growth on their \$100,000 will offset the loss of annual income and compensate them for the lesser capital security.

To date they have been correct. The growth in both the property and share indexes has been nothing short of stellar. But in recent months we have witnessed an increase in the 10-year government bond rate. This increase has been gradual but as they say “one straw can break the camel’s back”.

If the 10-year bond rate continues to increase, albeit slowly, there will be a point where professional investors will exit the share and property markets for the higher return and security offered by a government bond.

Then risk and return will again take centre stage in the financial markets but, unfortunately, it will be a painful lesson to learn.