ECONOMICS & GLOBAL MARKETS RESEARCH
HOUSING SNAPSHOT

24 January 2011

CONTRIBUTORS

Ange Montalti
Senior Economist, Property and Financial System Research
+61 3 9273 6288
Ange.Montalti@anz.com

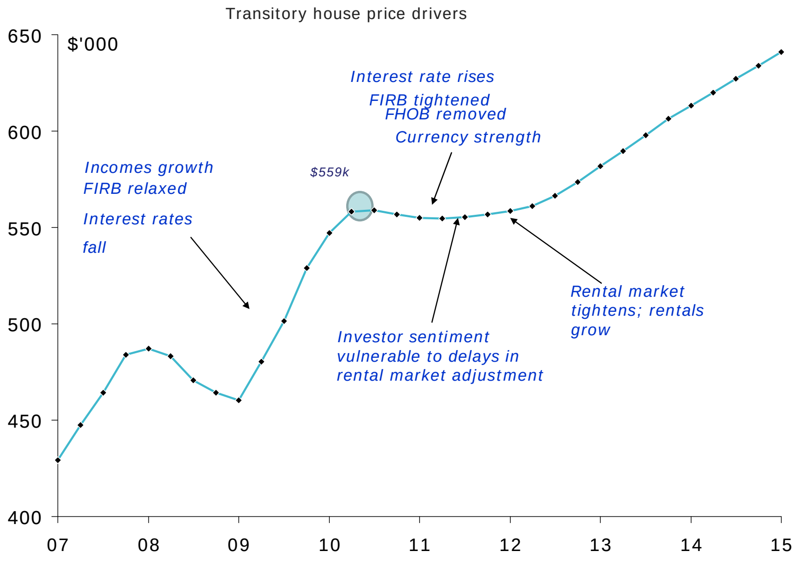
David Cannington
Economist, Property and Financial System Research
+61 3 9273 4274
David.Cannington@anz.com

Dylan Eades
Analyst, Economics
+61 3 9273 2708
Dylan.Eades@anz.com

Australia's medium-term economic outlook remains favourable given exposure to the fast-growing Asian region. The labour market will remain tight and while inflation is well contained for now, core inflation is expected to head higher over 2011. The RBA appears to be comfortably on hold for the next few months as consumer spending has remained sluggish and the impact of Queensland floods is more fully digested. The policy rate is expected to lift further in 2011 and indicators of housing activity and the policy backdrop suggest subdued building levels will persist. The absence of a coordinated political commitment to mobilise the supply-side of the housing market suggests continued exacerbation of an already record dwelling shortage.

House prices are taking an expected 'breather' after a solid run-up through 2009. A number of key influences (rising mortgage rates, lapse of first-home owners boost, tighter foreign investment rules and strong currency) have combined to soften conditions. Further price weakness is expected over 2011 as the prospect of additional rate rises weigh on both affordability and investor sentiment. While the market is vulnerable to weaker momentum becoming more entrenched, good support from healthy economic growth and a further tightening in rental markets should begin to shift perceptions over 2011/12. Accelerating rental growth will play the key role in signalling for renewed support to prices. Perceptions that national house prices are overdue for a major correction are misplaced with structural drivers 'explaining' the observed house price outcomes to date. For more detail, refer to "ANZ Housing Overvaluation".

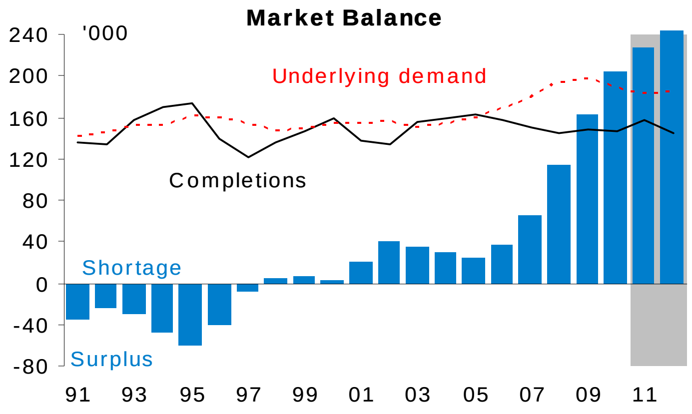
FIGURE 1. HOUSE PRICES TAKING A BREATHER

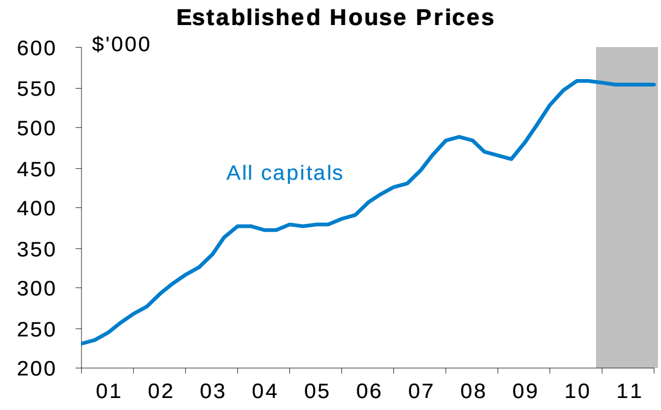


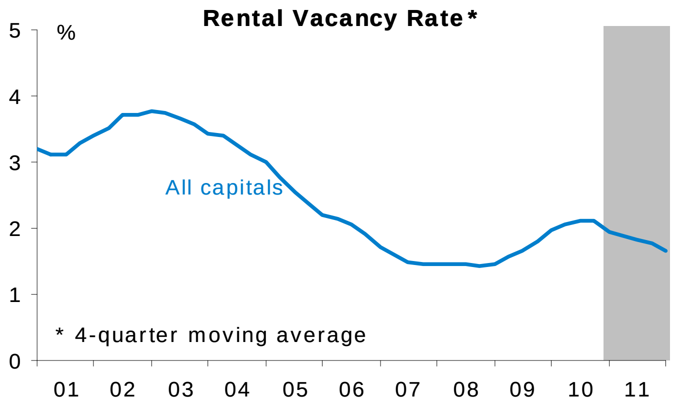
Sources: ABS, RBA, ANZ

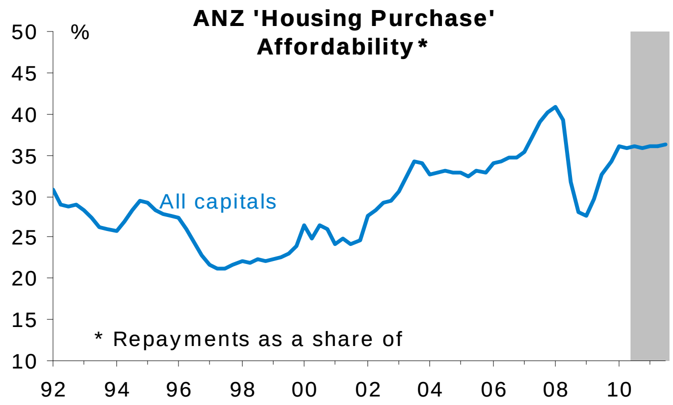
AUSTRALIA

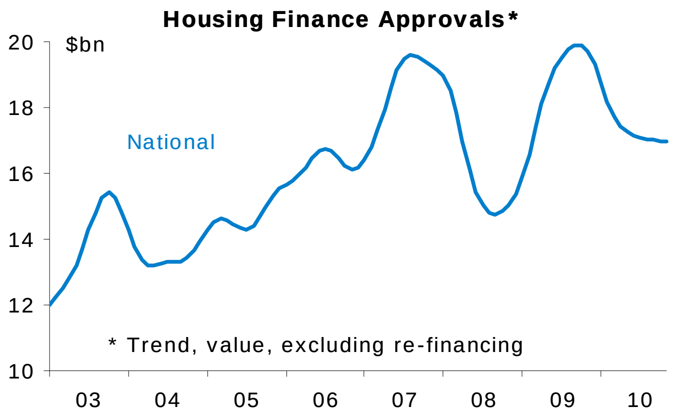
The national economy lost considerable momentum over the back half of 2010 but by year's end is expected to be on track once again to achieve trend rates of growth. The lagged effects of rising mortgage rates will maintain a reasonable headwind, inhibiting the much needed recovery in dwelling construction over 2011 and into 2012. Builders will remain cautious while margins are vulnerable to sluggish house prices. Dwelling starts are projected to decline from 149,000 in 2010/11 to 131,000 in 2011/12 before recovering gradually, a far cry from the 180,000+ dwellings required to merely stabilise the shortage at its already record high levels. This market imbalance is expected to reveal as an acceleration in rentals growth and renewed tightening in rental vacancies. The market tightening process had already commenced in 2007 but was interrupted by accommodating policies to combat the impact of the GFC on the domestic economy. By 2011, a re-emergence of market tightening should become apparent, which will once again establish the pre-conditions for a recovery in prices through 2012.

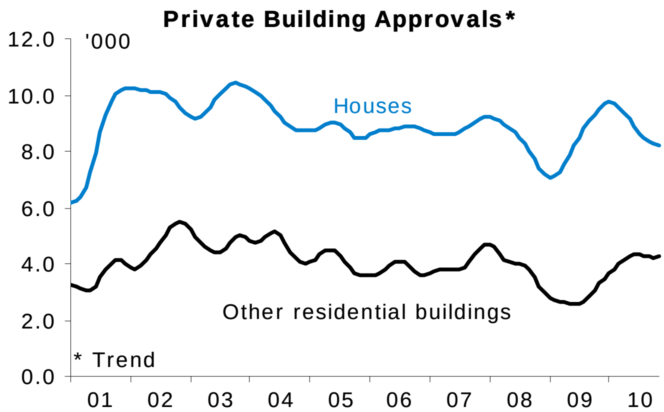










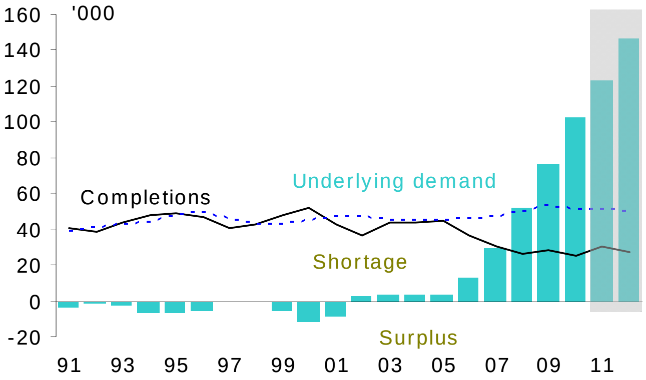


Sources: Australian Bureau of Statistics, RBA, REIA, Residex, ANZ

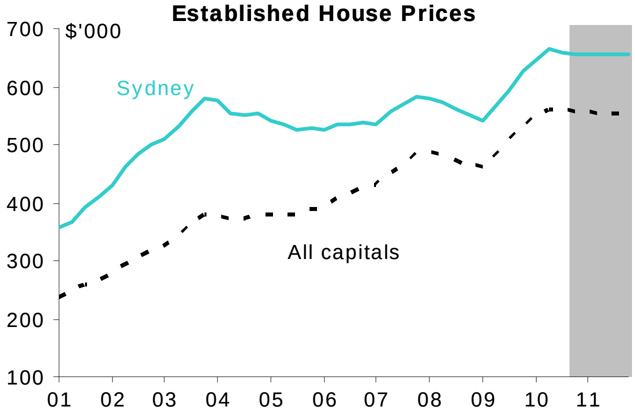
NEW SOUTH WALES

The economic environment in NSW has remained relatively healthy with the economy expanding by 1.7% over 2009/10, supporting house price growth of 5.7% over the year to November, although interest rate rises have tempered price growth more recently. Finance approvals have fallen by 13.5% since July 2009 whilst clearance rates, which were hovering in the vicinity of 70-80% at the beginning of the year, have regularly fallen below 60% over the second half of the year. Fundamental conditions in the Sydney housing market remain tight, with dwelling completions running at a meagre 26,000 (around half the levels of a decade earlier), well below underlying requirements. Indeed, the chronic NSW housing shortage will continue to accumulate to remarkable levels. We expect competition in the rental markets to intensify, with vacancy rates forecast to head below 1% in the second half of the year. Rental growth will be close to double digits by the end of 2011, challenging rental affordability, but signalling support to the market over the medium term. In the near term, we expect the cyclical upswing in interest rates to put a cap on house prices and anticipate modest growth of 2% in 2011.

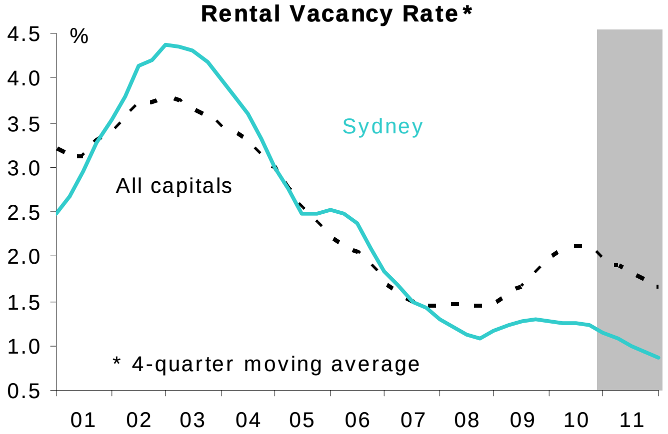
Market Balance - NSW



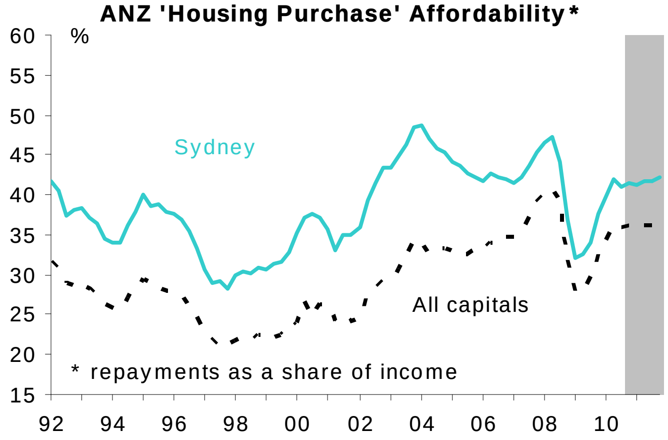
Established House Prices



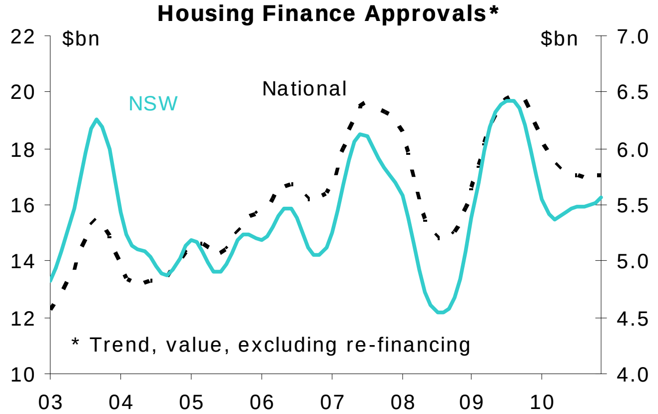
Rental Vacancy Rate*



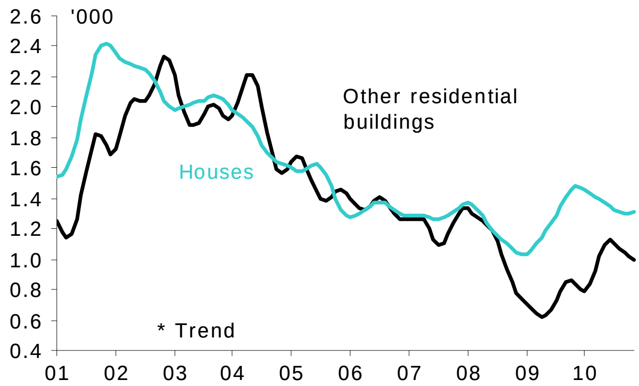
ANZ 'Housing Purchase' Affordability*



Housing Finance Approvals*



Private Building Approvals*

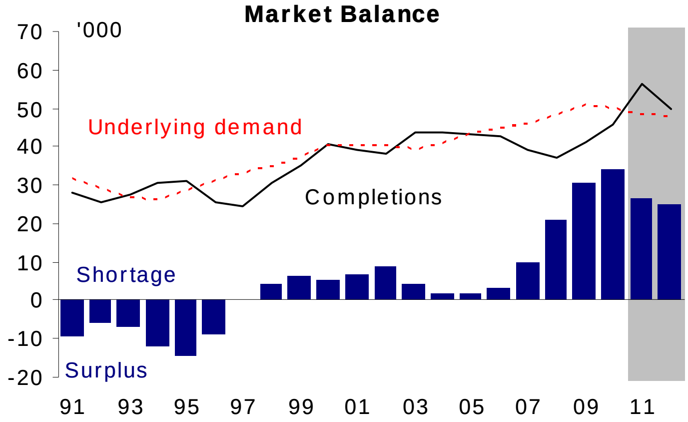


Sources: ANZ, Australian Bureau of Statistics, RBA, REIA, Residex

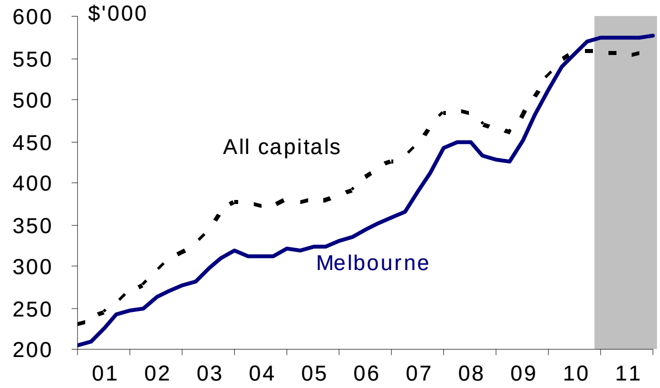
VICTORIA

While housing market conditions have moderated across Australia through 2010, the Melbourne real estate market has fared far better than other capital cities. Healthy employment growth and sustained strength in underlying market fundamentals have provided the foundations for Melbourne's outperformance. With dwelling completions running at 45,900 in 2009-10 and an underlying requirement for 49,800 dwellings, Victoria's housing market remains tight. This has been reflected by strong growth in Melbourne house prices compared to the national average (9.7% higher in the year to November 2010 compared to 4.9% across all capital cities). Despite house building approvals slowing through 2010 they remain at healthy levels. Combined with continued strong increases in approvals of medium density housing (flats, units, townhouses) this should relieve some of the underlying tightness in Victoria's housing market into 2011. The outlook for Melbourne's market does not point to any relief for potential homebuyers, with house prices expected to remain elevated through 2011. Rental vacancy rates should ease marginally higher but remain at historically low levels in 2011 maintaining upward pressure on Melbourne rents.

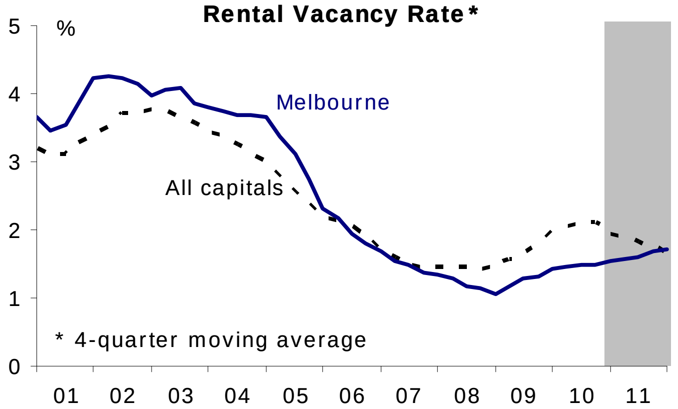
Market Balance



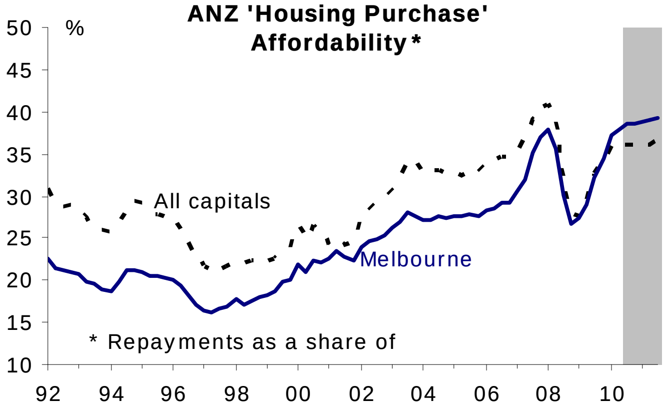
Established House Prices



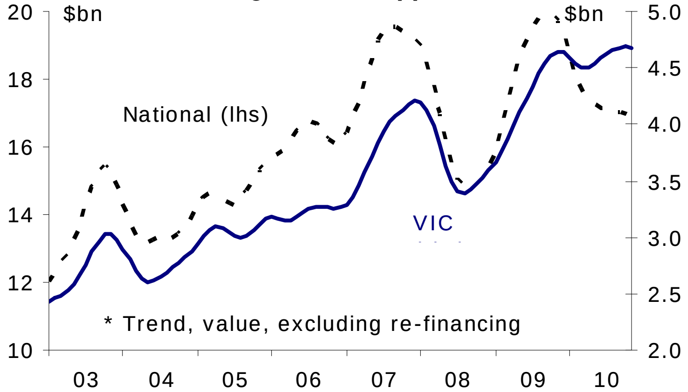
Rental Vacancy Rate*



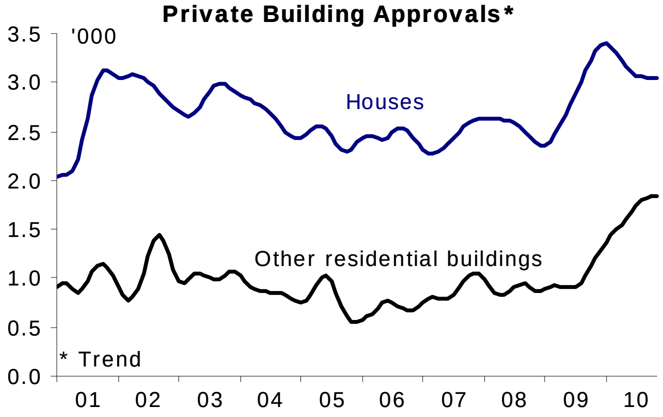
ANZ 'Housing Purchase' Affordability*



Housing Finance Approvals*



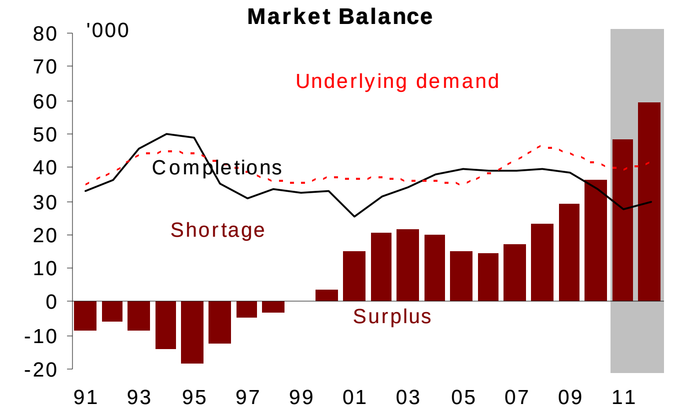
Private Building Approvals*

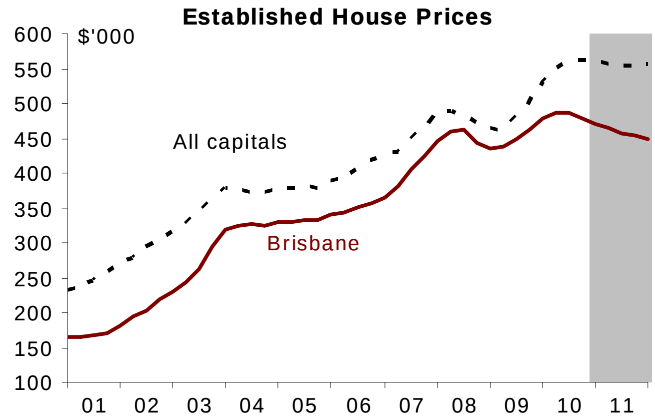


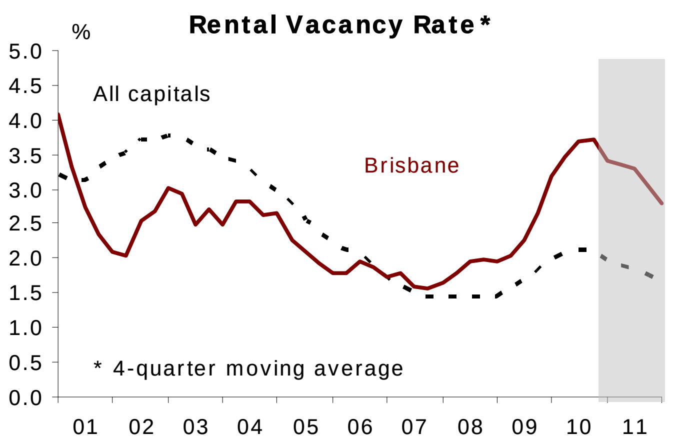
Sources: ANZ, Australian Bureau of Statistics, RBA, REIA, Residex

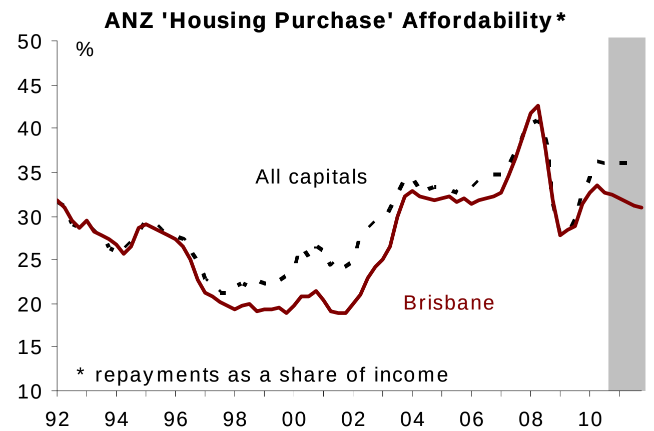
QUEENSLAND

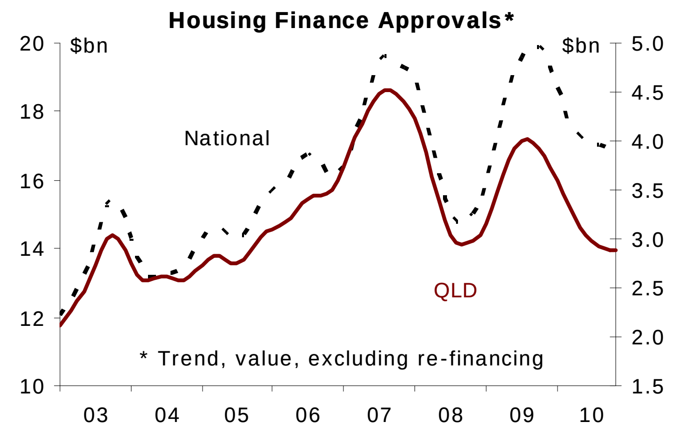
The severe floods in Queensland have damaged an estimated 40,000 homes and up to 28,000 homes will need to be rebuilt. To put this in perspective, during 2009/10 only 33,700 homes were built, meaning that reconstruction alone is the equivalent to a year of homebuilding. Before the onset of the floods, building approvals had fallen by 60% - to 2000 levels – and completions were on a sustained downwards trend. This suggests that although the reconstruction effort will boost construction activity, there is substantial spare capacity in the Queensland building sector. Due to softer economic conditions, house prices fell 0.8% over the year to November 2010. In the near term, the floods are likely to exacerbate this trend, exerting further downward pressure on prices. However, these impacts will dissipate over the medium term. The reduction in the housing stock, in conjunction with the large number of displaced homeowners will see a tightening in the rental market. After climbing to 3.7% in September last year, we expect rental vacancy rates to fall to under 3% by the end of this year, supporting moderate rental growth.

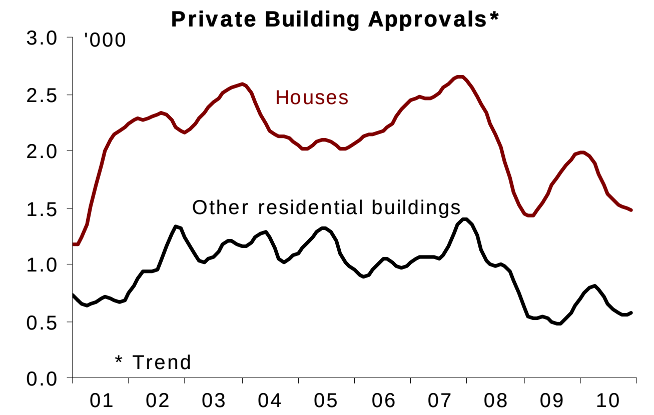








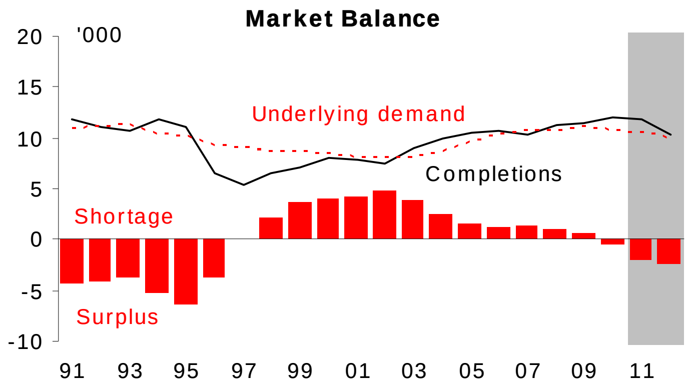


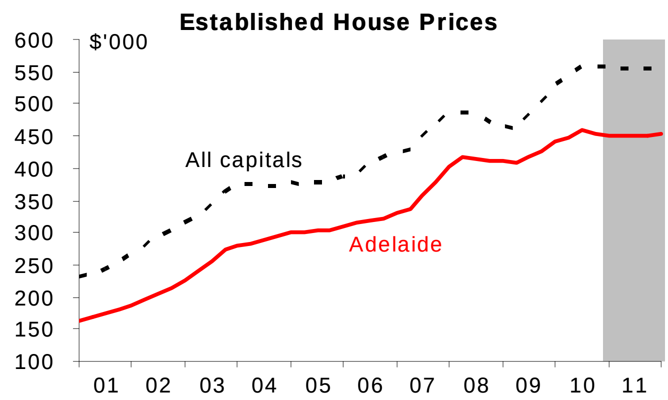


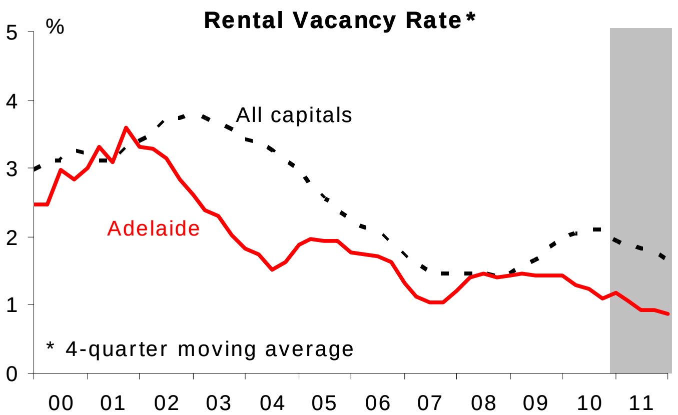
Sources: ANZ, Australian Bureau of Statistics, RBA, REIA, Residex

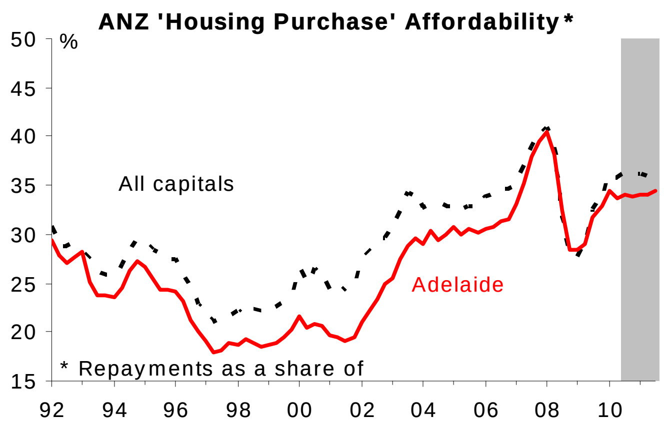
SOUTH AUSTRALIA

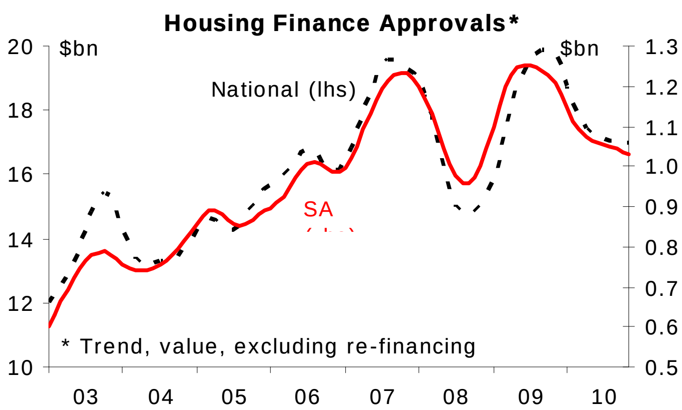
Adelaide's housing market weathered the volatility of 2010 relatively well with the lowest rental vacancy rate across Australian capital cities (1.1% at September 2010) and annual house price growth marginally lower than the national average (3.8% higher in the year to November 2010). While these conditions haven't yet transferred to strong growth in rents (up a moderate 4.6% for houses in the year to September 2010), it's only a matter of time before investors start chasing stronger rental yields. The South Australia housing market is effectively in balance with annual dwelling completions tracking at 11,900 and an underlying annual requirement of 10,700 dwellings. Expectations for further moderation in house price growth and housing affordability below the national capital city average could arouse home buying activity and push house prices higher. Nonetheless, balanced housing market fundamentals should maintain annual house price growth in Adelaide around 2% in 2011 with completions expected to slow through 2011 and population growth expected to remain a modest 1.2%.

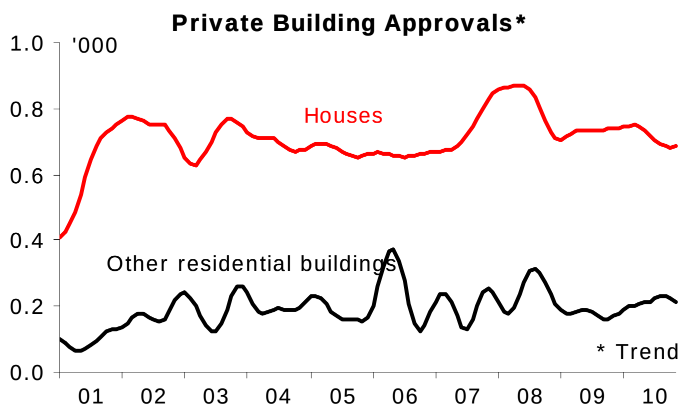








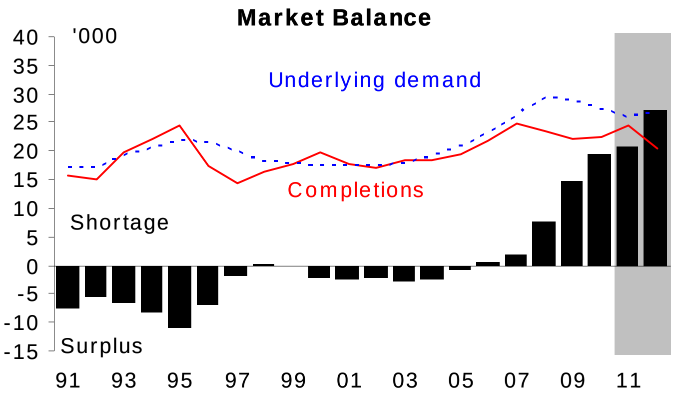


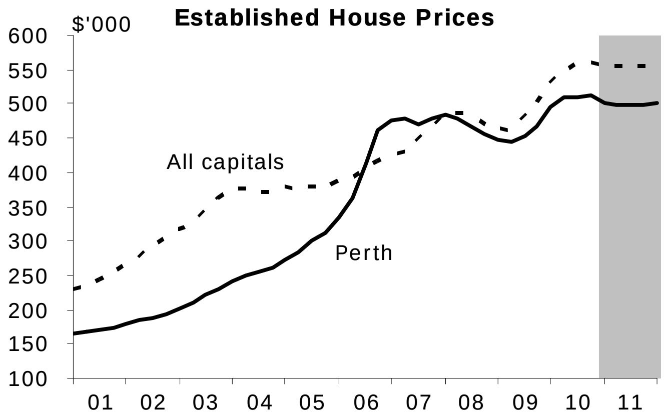


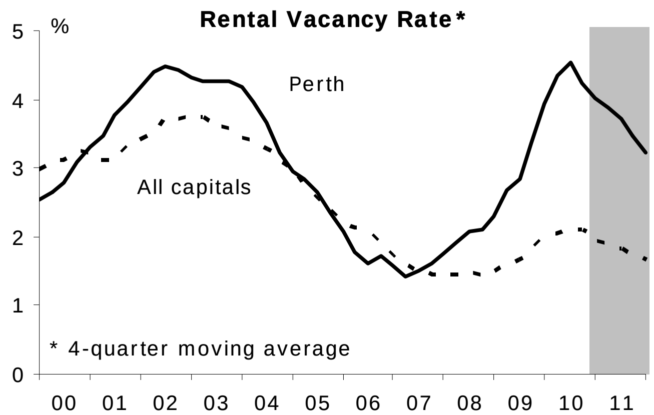
Sources: ANZ, Australian Bureau of Statistics, RBA, REIA, Residex

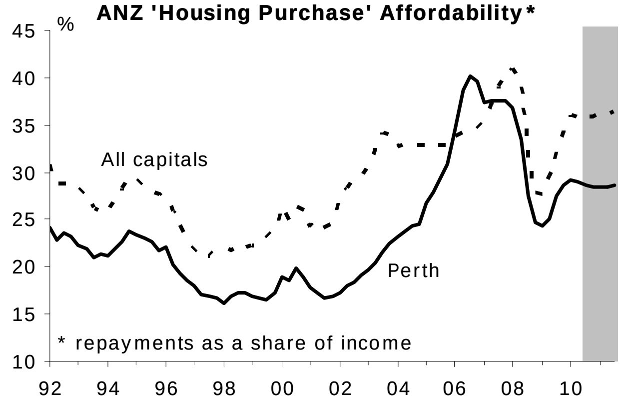
WESTERN AUSTRALIA

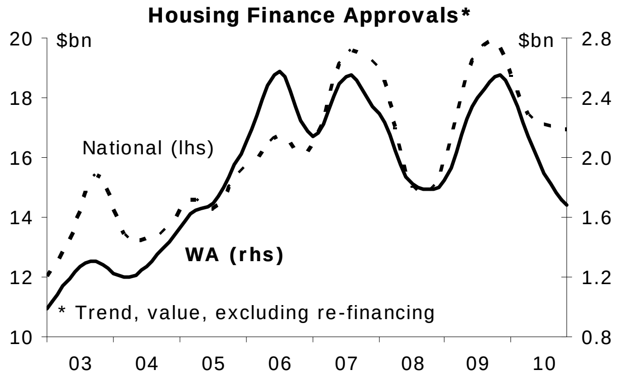
Western Australia's underlying housing market fundamentals are expected to tighten over 2011 with the economy already reaping the rewards of the current commodity boom. However, despite a solid outlook the Perth housing market is not expected to experience the same growth in house prices that it did in the pre-GFC commodity boom. Indicators show growth in the Perth housing market was overdone in the lead-up to the GFC; between 2004 and 2007 Perth house prices increased 76% and housing affordability became almost twice as difficult while rental vacancy rates increased from around 1.4% at the start of 2007 to around 4.5% in June quarter 2010. Since 2007, Perth house prices have increased a relatively moderate 6% (compared to a national capital city average of 15%) while Perth rental vacancy rates have blown out to 4.2% in September 2010 (2.0% across all capital cities). Consequently, in comparison to most other Australian capital cities Perth housing market conditions into 2011 are expected to remain favourable for both home buyers and renters, while price growth and housing stock additions are expected to weaken.

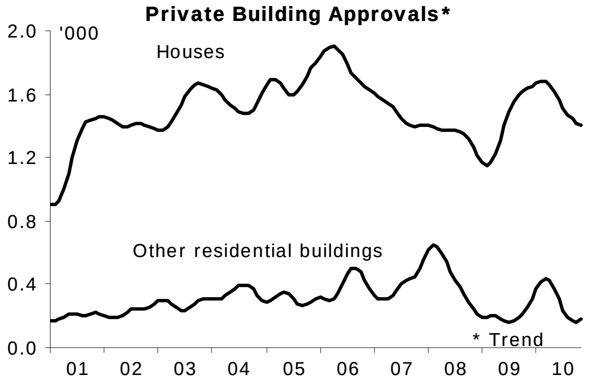








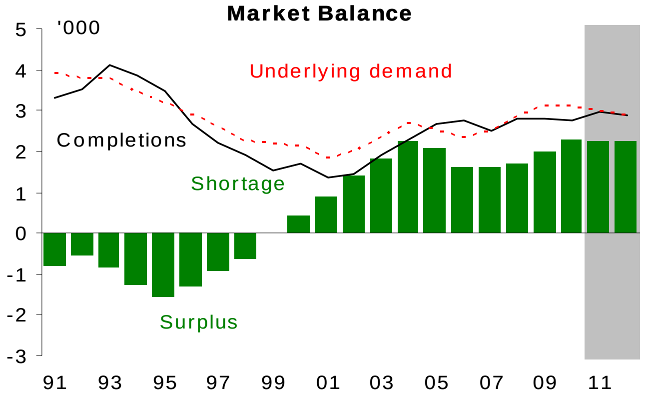


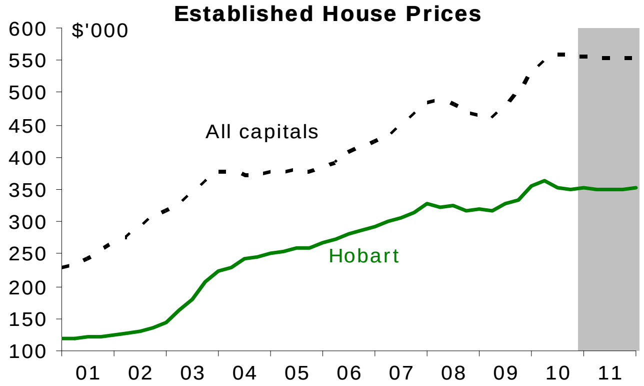


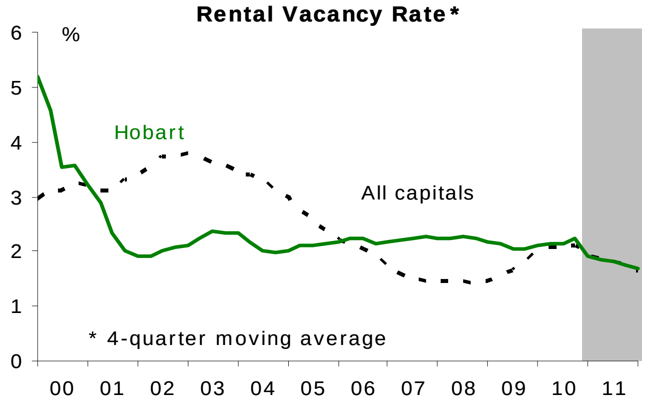
Sources: ANZ, Australian Bureau of Statistics, RBA, REIA, Residex

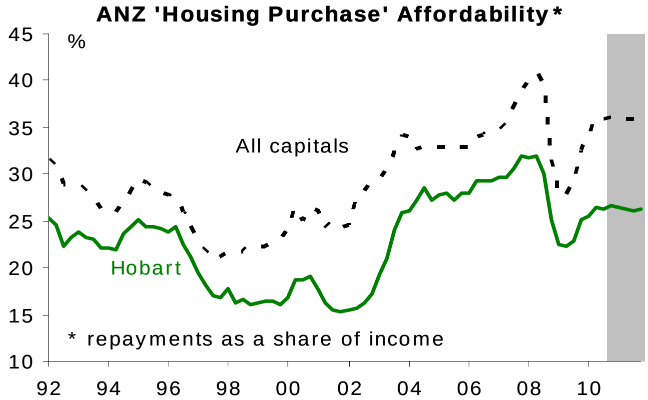
TASMANIA

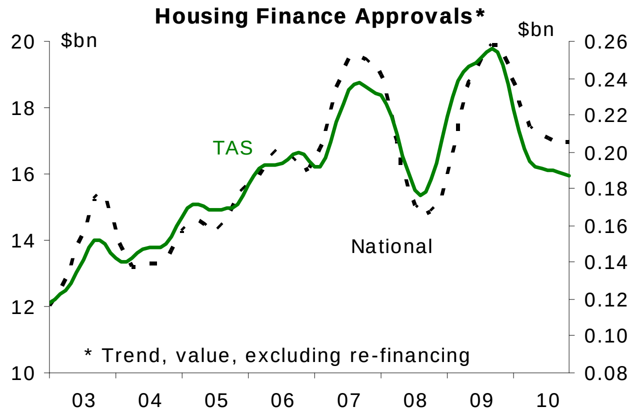
The Tasmanian economy remains in the doldrums and was the worst performing state over 2009/10 with its economy growing by just 0.4%. The less than stellar economic conditions have begun to take their toll. Finance approvals have plummeted by 26%, with both investors and owner occupiers withdrawing from the market. Softer economic conditions and reduced housing market activity have seen house price growth reversed, with prices falling by 1.3% over the year to October. With the cheapest median house prices in Australia, Hobart remains one of the most affordable housing markets with a purchase affordability of 26.2% (compared to the Australian average of 36%) which should prevent any significant price declines. We expect house prices to largely move sideways through 2011. Despite declining by 27% building approvals still remain at relatively healthy levels and we expect this to translate into 2900 completions in 2011. Given Tasmania's anaemic population growth, we anticipate dwelling completions will be sufficient to meet underlying demand, capping price and rental growth. The rental market has remained remarkably stable, with the vacancy rate continuing to hover just above 2%. We expect that this will be maintained moving forward, with rental yields remaining in the 3.5% to 4.5% range.

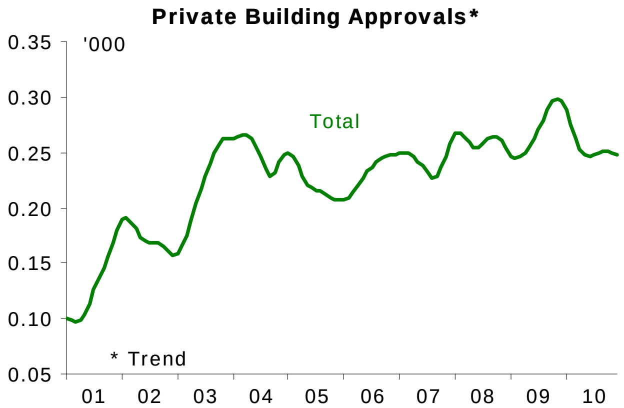










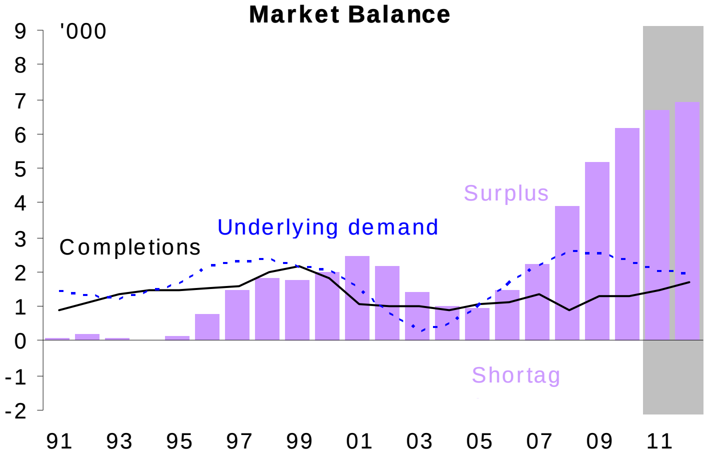


Sources: ANZ, Australian Bureau of Statistics, RBA, REIA, Residex

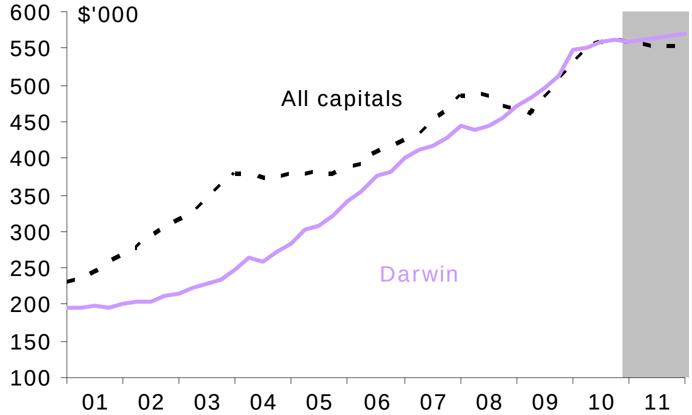
NORTHERN TERRITORY

Economic conditions in the Northern Territory have moderated over the past year with growth slowing to 1.3% over 2009/10, compared to a nation-beating 5.1% over 2008/09. Slowing economic conditions, coupled a cyclical upswing in interest rates have seen housing market conditions soften, with finance approvals declining by 34% over the past year. After recording average annual price growth of 18.8% between 2005 and 2009, house prices in Darwin have slowed, climbing by 8.4% over the year to November. With a number of key resource projects having wound up, the state has experienced a sustained decline in net interstate migration for the first time since 2006. This has weakened the rental market, with growth in rents slowing to 6.9% in September from a peak of 13.5% in March 2009. Building approvals have declined by 42% over the past six months and despite reduced population growth, Darwin's housing market imbalance will continue worsen. While we expect softer prices in the near term the tight conditions should continue to place upwards pressure on rents and prices over the medium term.

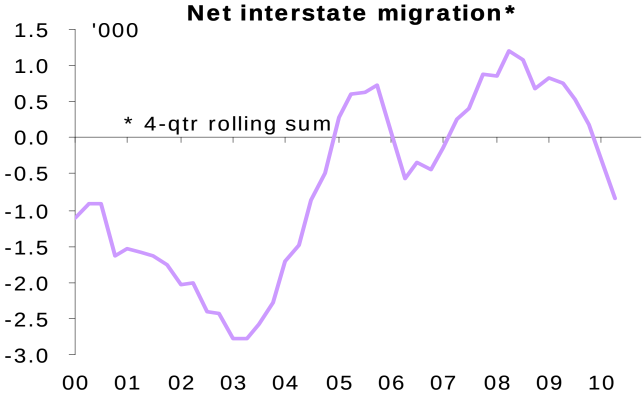
Market Balance



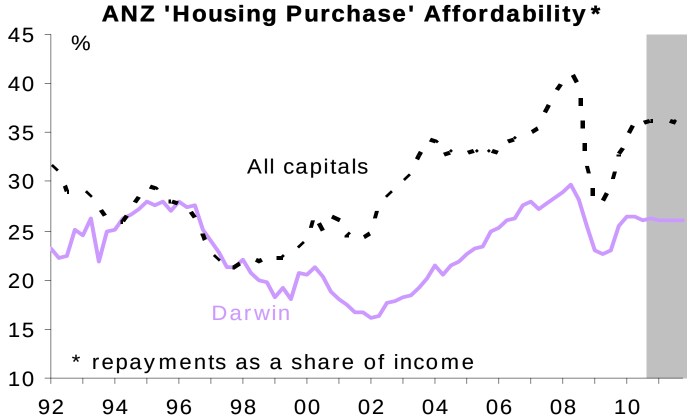
Established House Prices



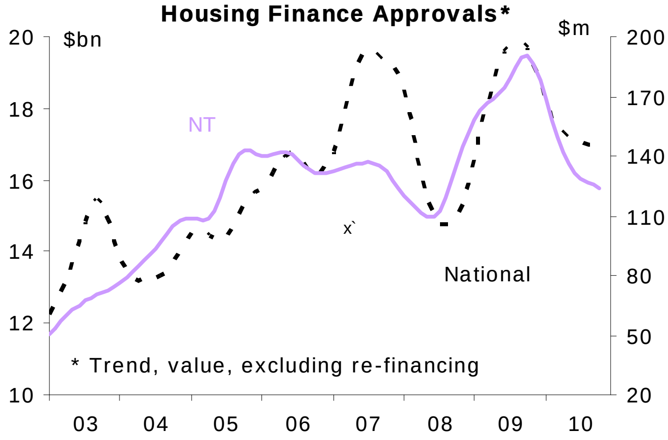
Net interstate migration*



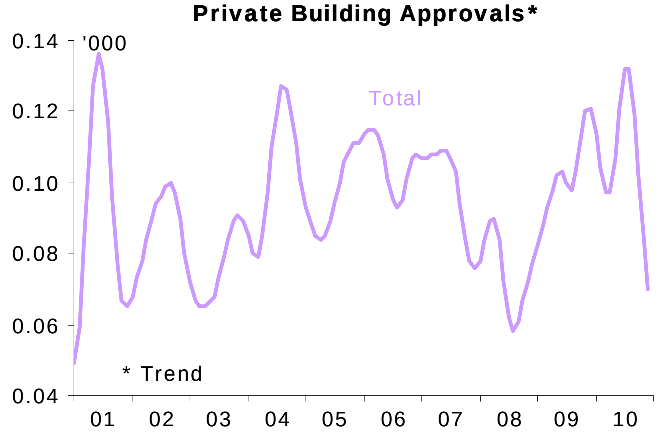
ANZ 'Housing Purchase' Affordability*



Housing Finance Approvals*



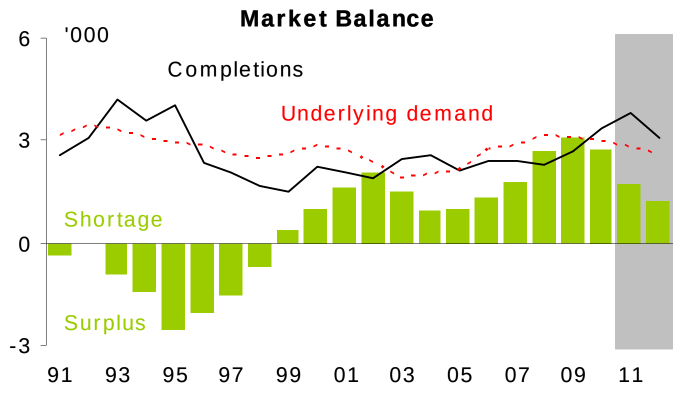
Private Building Approvals*

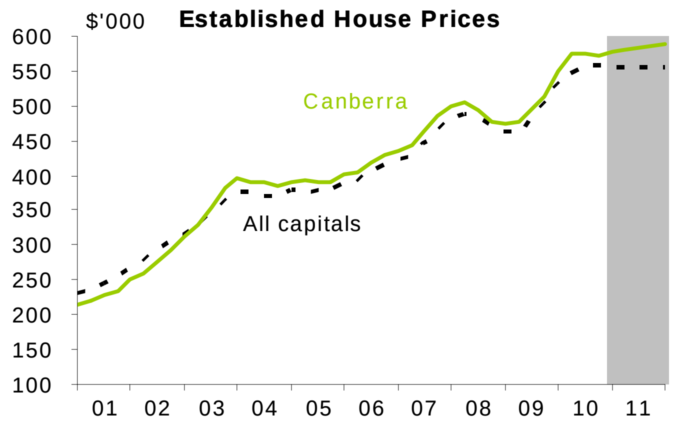


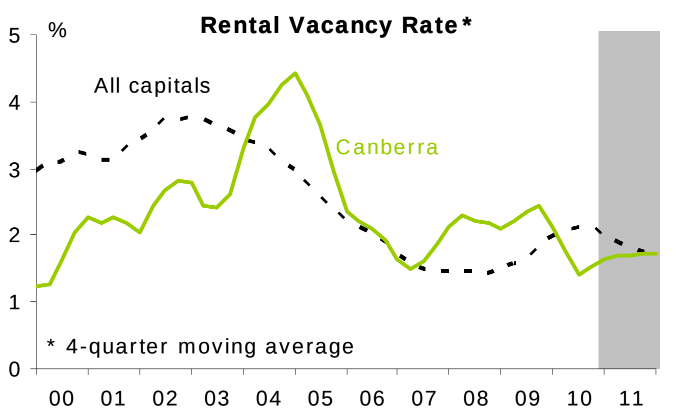
Sources: ANZ, Australian Bureau of Statistics, RBA, REIA, Residex

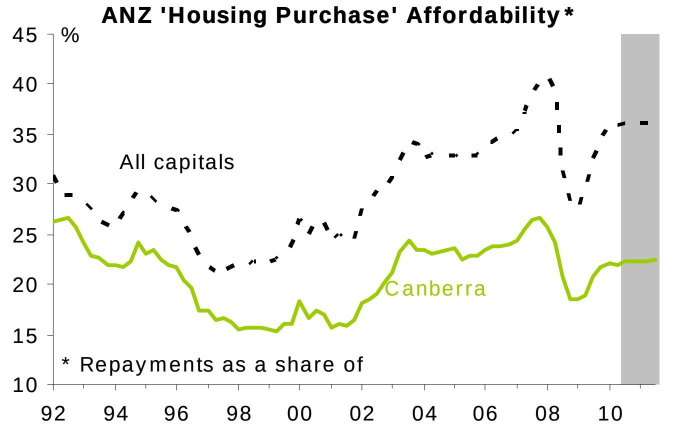
AUSTRALIAN CAPITAL TERRITORY

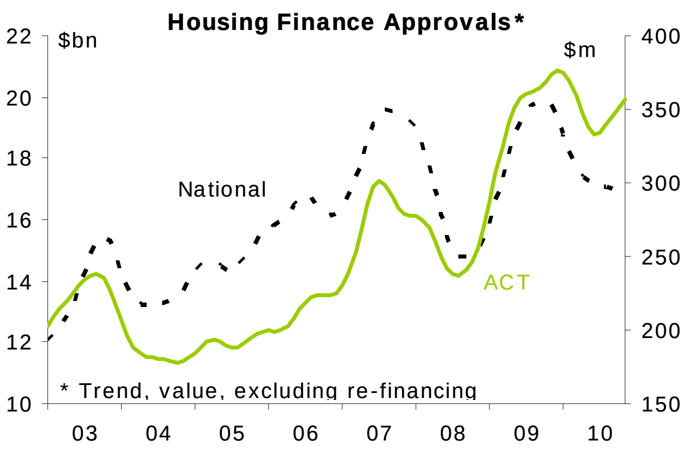
Canberra's property market has been a solid performer over 2010. Canberra house prices increased 8.1% in the year to November 2010. The shortage of housing stock in ACT (around 2,600 dwellings) softened in 2010. While completions hit a historical high with 3,300 dwellings added to Canberra's housing stock in 2010, the underlying annual requirement was 3,000 dwellings. With expectations of solid economic and employment growth in ACT, Canberra housing market indicators should continue to perform well supporting moderate house price growth (2% in 2011). Rental vacancies will ease marginally higher over 2011, maintaining the existing tightness in the rental market and upward pressure on rent growth. In line with this, housing purchase affordability (currently 22% in Canberra compared to 36% across all Australian capital cities) is expected to remain well below the national capital city average through 2011.

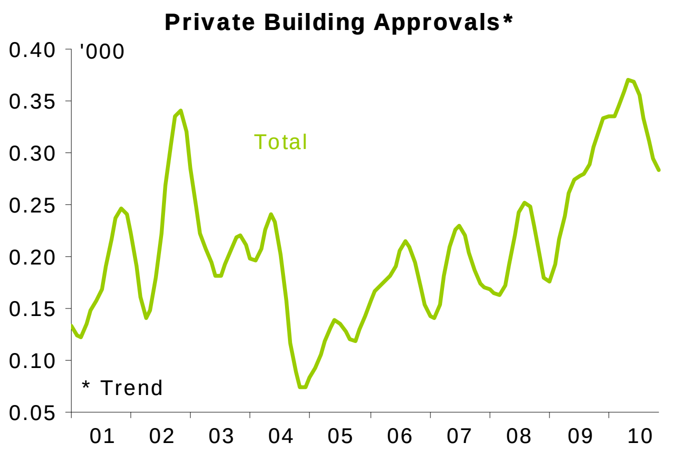












Sources: ANZ, Australian Bureau of Statistics, RBA, REIA, Residex

IMPORTANT NOTICE

Australia and New Zealand Group Limited is represented in:

AUSTRALIA

Australia and New Zealand Banking Group Limited

ABN 11 005 357 522

ANZ Centre Melbourne, Level 9, 833 Collins Street, Docklands Victoria 3008, Australia

Telephone +61 3 9273 5555 Fax +61 3 9273 5711

UNITED STATES OF AMERICA

ANZ Securities, Inc. is a member of FINRA (www.finra.org) and registered with the SEC.

277 Park Avenue, 31st Floor, New York, NY 10172,

United States of America

Tel: +1 212 801 9160 Fax: +1 212 801 9163

UNITED KINGDOM BY:

Australia and New Zealand Banking Group Limited

ABN 11 005 357 522

40 Bank Street, Canary Wharf, London, E14 5EJ, United Kingdom

Telephone +44 20 3229 2121 Fax +44 20 7378 2378

NEW ZEALAND BY:

ANZ National Bank Limited

Level 7, 1-9 Victoria Street, Wellington, New Zealand

Telephone +64 4 802 2000

This document ("document") is distributed to you in Australia and the United Kingdom by Australia and New Zealand Banking Group Limited ABN 11 005 357 522 ("ANZ") and in New Zealand by ANZ National Bank Limited ("ANZ NZ"). ANZ holds an Australian Financial Services licence no. 234527 and is authorised in the UK and regulated by the Financial Services Authority ("FSA").

This document is being distributed in the United States by ANZ Securities, Inc. ("ANZ S") (an affiliated company of ANZ), which accepts responsibility for its content. Further information on any securities referred to herein may be obtained from ANZ S upon request. Any US person(s) receiving this document and wishing to effect transactions in any securities referred to herein should contact ANZ S, not its affiliates.

This document is being distributed in the United Kingdom by ANZ solely for the information of its eligible counterparties and professional clients (as defined by the FSA). It is not intended for and must not be distributed to any person who would come within the FSA definition of "retail clients". Nothing here excludes or restricts any duty or liability to a customer which ANZ may have under the UK Financial Services and Markets Act 2000 or under the regulatory system as defined in the Rules of the FSA.

This document is issued on the basis that it is only for the information of the particular person to whom it is provided. This document may not be reproduced, distributed or published by any recipient for any purpose. This document does not take into account your personal needs and financial circumstances. Under no circumstances is this document to be used or considered as an offer to sell, or a solicitation of an offer to buy.

In addition, from time to time ANZ, ANZ NZ, ANZ S, their affiliated companies, or their respective associates and employees may have an interest in any financial products (as defined by the Australian Corporations Act 2001), securities or other investments, directly or indirectly the subject of this document (and may receive commissions or other remuneration in relation to the sale of such financial products, securities or other investments), or may perform services for, or solicit business from, any company the subject of this document. If you have been referred to ANZ, ANZ NZ, ANZ S or their affiliated companies by any person, that person may receive a benefit in respect of any transactions effected on your behalf, details of which will be available upon request.

The information herein has been obtained from, and any opinions herein are based upon, sources believed reliable. The views expressed in this document accurately reflect the author's personal views, including those about any and all of the securities and issuers referred to herein. The author however makes no representation as to its accuracy or completeness and the information should not be relied upon as such. All opinions and estimates herein reflect the author's judgement on the date of this document and are subject to change without notice. No part of the author's compensation was, is or will directly or indirectly relate to specific recommendations or views expressed about any securities or issuers in this document. ANZ, ANZ NZ, ANZ S, their affiliated companies, their respective directors, officers, and employees disclaim any responsibility, and shall not be liable, for any loss, damage, claim, liability, proceedings, cost or expense ("Liability") arising directly or indirectly (and whether in tort (including negligence), contract, equity or otherwise) out of or in connection with the contents of and/or any omissions from this communication except where a Liability is made non-excludable by legislation.

Where the recipient of this publication conducts a business, the provisions of the Consumer Guarantees Act 1993 (NZ) shall not apply.