**Australian Gold Fund Economic Commentary**

# Sydney Apartment Prices – Topping Patterns Observed, Cliff Ahead?

## 12th June 2019

## Key Points

- The Sydney apartment/unit market is seeing a topping pattern, with prices having peaked across major suburbs between 2015-2018, and are now invariably heading downwards as a result of sharply decreasing sales volume.
- In suburbs previously considered to have strong demand and hence be expected to be robust, the average aggregate prices have fallen 2-18% from their peak. When stratifying the data by bedrooms, the price declines are more pronounced.
- Sales volume across key suburbs has sharply declined and the time taken for a sale to be made is noticeably higher in 2019, with many vendors waiting an average of 100+ days for a sale to be completed.
- Despite the Morrison government's incentives and the RBA rate cut, prices are expected to fall over the longer term due to the overwhelming force of a weakening economy, lower consumer confidence and mortgage fatigue.

## Houses and Apartments – A Tale of Two Cities, With a Twist

The topic regarding Sydney property prices is a tale of two cities, with houses and apartments/units being separately discussed. Many people believe that house prices will be more resilient than apartment/unit prices because of the former being supported by a perceived land shortage, lower density and that the apartment boom will be the author of a deeper decline. While people's beliefs are backed by data or logic or both, the reality does not agree with them. The truth is that prices of houses in key hot suburbs have fallen sharper and earlier than apartments/units. Last month, we released a report showing how house prices in various suburbs have fallen significantly from their peak, after adjusting for the number of bedrooms. This report presents our analysis on apartments and units using the same method. The findings may not be comforting to those who recently made their apartment purchase, especially if they are largely financed by debt. This is because the apartment prices suggest that **a topping pattern is evident in many suburbs**. And as 2019 continues, the sales volume may continue to remain weak despite the re-election of the Morrison government that has promised to offer first time buyers various incentives to make their purchase and the Reserve Bank of Australia reducing the interest rate to an all-time historical low of 1.25% on 5th June.

## What is a Topping Pattern?

Those who trade in equities and employ technical analysis (charting) will be familiar with the term "topping pattern". This is characterised by a stock where the price is breaking new record highs but the volume of transactions is declining significantly. The explanation in real terms is that those who want to sell are finding fewer buyers at the price that they want. Thus, the level of transactions is much lower. Those who want to buy are reluctant to pay higher prices while those wanting to sell at their desired price are similarly reluctant to reduce prices to meet the buyers' bids. This can hold out for some time depending on the sellers' ability to financially fund their asset holdings and their willingness to part with their holdings at a reduced price. However, if leverage or debt-funded investing comes into play, this dynamic becomes all that more complicated since leverage has an interest cost attached to it and also there is a thinner margin for error.

So, in the case of the housing market, the well-known fact is home-owners and investors alike have been leveraged heavily for many years. Despite lower interest rates offered by lenders, more households are finding it hard to make ends meet while trying to make mortgage repayments. With around $480 billion of $1.7 trillion in interest-only loans as reported earlier this year and average mortgage size of around $400 000 while average individual income is around $85 000 p.a., this may mean the margin of safety is indeed quite thin for many Sydneysiders.

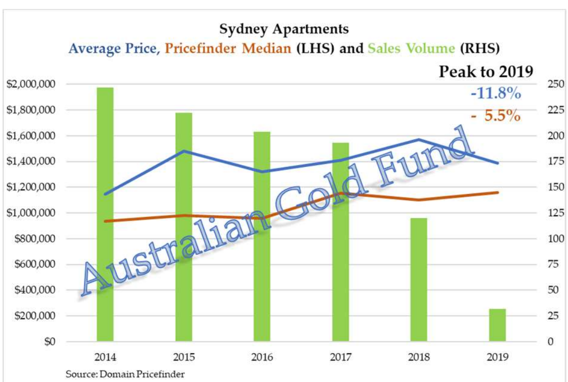
## The Topping Pattern of Apartment Prices

This report focuses on apartment sales in Bondi, Chatswood, Epping, Hurstville, Liverpool, Meadowbank and the Sydney CBD from 2014-2019. Prices have been stratified by number of bedrooms. The results selected for inclusion are for the more commonly transacted categories in each suburb, which ranges from one to three bedrooms. Worth noting in interpreting these results is that real estate agents have requested non-disclosure of more recent sales (in the past month) thus the data may not reflect the most recent post-election trend. However, the month prior to the election saw more subdued selling activity and lower prices.

First, take a look at the aggregate property average and median prices from the peak to 2019:






While aggregate apartment prices for these suburbs do not look dire, falling between 2%-18%, the price level declines are understated in these statistics because they combine all apartments sold, rather than being stratified. What is noticeable in each case is that the prices peaked between 2015 to 2018 across these suburbs and the declining trend is evident. The sales volume in 2019 for each suburb, even after adjusting for the fact that the data is up to late May, is nowhere near the levels seen prior to 2017 when the Sydney property market is recognised to have peaked. With the price peak evident and the sales volume precariously declining, the aggregate data is clearly pointing to a topping pattern.

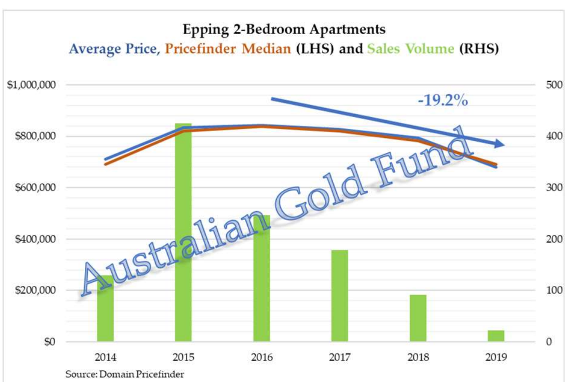
Having seen the topping pattern manifest itself in the aggregate price data, have a look at how the average and median price levels are for the stratified price data, considering the key categories of apartments in each suburb:

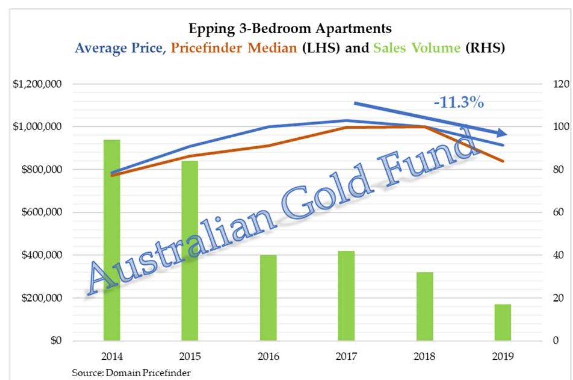

Bondi 1-Bedroom Apartments
Average Price, Pricefinder Median (LHS) and Sales Volume (RHS)
-19.5%
$1,000,000
$800,000
$600,000
$400,000
$200,000
$0
100
80
60
40
20
0
2014
2015
2016
2017
2018
2019
Australian Gold Fund
Source: Domain Pricefinder


Bondi 2-Bedroom Apartments
Average Price, Pricefinder Median (LHS) and Sales Volume (RHS)
-4.8%
$1,500,000
$1,250,000
$1,000,000
$750,000
$500,000
$250,000
$0
180
150
120
90
60
30
0
2014
2015
2016
2017
2018
2019
Australian Gold Fund
Source: Domain Pricefinder

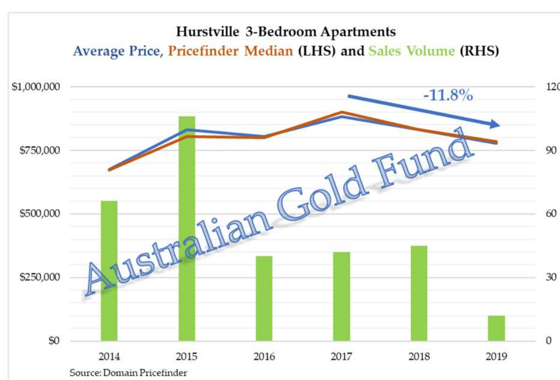

Chatswood 1-Bedroom Apartments
Average Price, Pricefinder Median (LHS) and Sales Volume (RHS)
-12.2%
$1,000,000
$900,000
$800,000
$700,000
$600,000
$500,000
$400,000
$300,000
$200,000
$100,000
$0
250
225
200
175
150
125
100
75
50
25
0
2014
2015
2016
2017
2018
2019
Australian Gold Fund
Source: Domain Pricefinder


Chatswood 2-Bedroom Apartments
Average Price, Pricefinder Median (LHS) and Sales Volume (RHS)
-6.8%
$1,500,000
$1,250,000
$1,000,000
$750,000
$500,000
$250,000
$0
300
250
200
150
100
50
0
2014
2015
2016
2017
2018
2019
Australian Gold Fund
Source: Domain Pricefinder

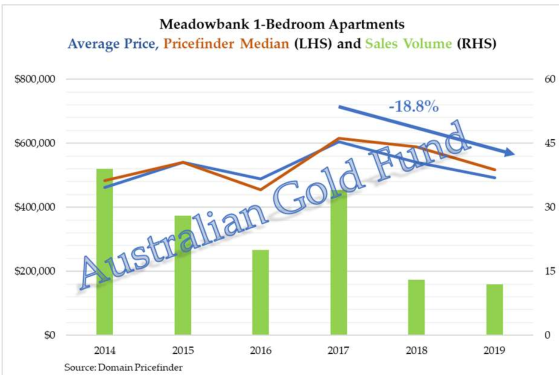

Epping 2-Bedroom Apartments
Average Price, Pricefinder Median (LHS) and Sales Volume (RHS)
-19.2%
$1,000,000
$800,000
$600,000
$400,000
$200,000
$0
500
400
300
200
100
0
2014
2015
2016
2017
2018
2019
Australian Gold Fund
Source: Domain Pricefinder


Epping 3-Bedroom Apartments
Average Price, Pricefinder Median (LHS) and Sales Volume (RHS)
-11.3%
$1,200,000
$1,000,000
$800,000
$600,000
$400,000
$200,000
$0
120
100
80
60
40
20
0
2014
2015
2016
2017
2018
2019
Australian Gold Fund
Source: Domain Pricefinder

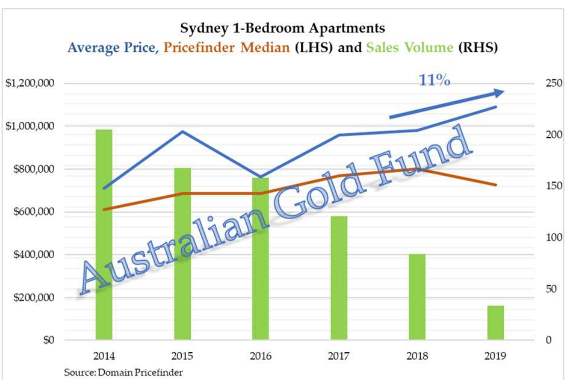

Hurstville 2-Bedroom Apartments
Average Price, Pricefinder Median (LHS) and Sales Volume (RHS)
-11.2%
$1,000,000
$800,000
$600,000
$400,000
$200,000
$0
250
200
150
100
50
0
2014
2015
2016
2017
2018
2019
Australian Gold Fund
Source: Domain Pricefinder

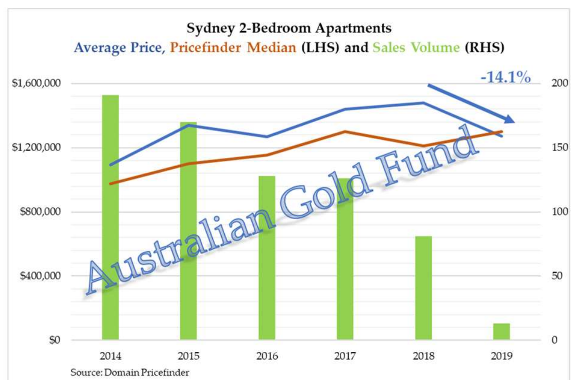

Hurstville 3-Bedroom Apartments
Average Price, Pricefinder Median (LHS) and Sales Volume (RHS)
-11.8%
$1,000,000
$750,000
$500,000
$250,000
$0
120
90
60
30
0
2014
2015
2016
2017
2018
2019
Australian Gold Fund
Source: Domain Pricefinder







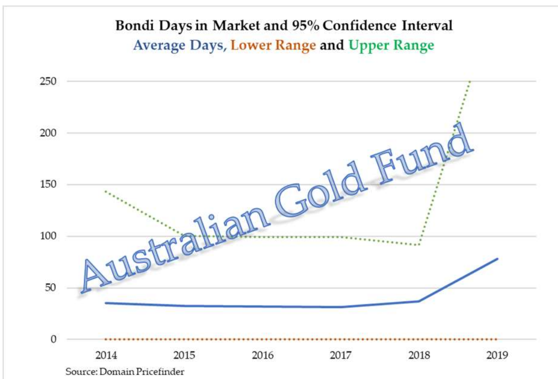


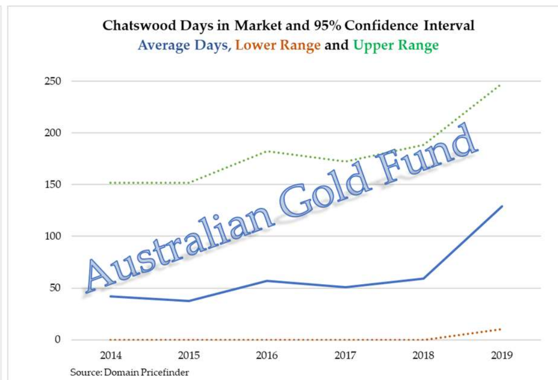



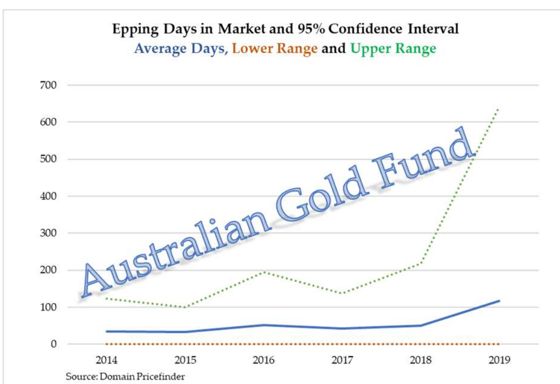

With the exception of Sydney 1-bedroom apartments that are seeing the average price rise 11% from last year, the average price levels have been declining 5-20%, with the average being around 12% from the peak levels. The media price trends are similar to the average price trends, although the median appears to be declining more than the average. This is due to the average price being distorted by sales of apartments in the higher price ranges. Despite significant developments of new apartments in these suburbs that was expected to keep prices elevated, the price levels are clearly on the decline. The less common categories in various suburbs, that are not included in the figures above, have seen more dramatic declines. Of note, 3-bedroom apartments in Chatswood have fallen 39.1% from 2017 to 2019, with the average sale price of $1.23m and 3-bedroom apartments in the Sydney CBD falling 54.8% from 2017 to $1.42m. These figures may look very alarming but it is worth noting these are based on a smaller number of sales and also the 3-bedroom apartments may be from the prestige apartment blocks that command a significant premium.

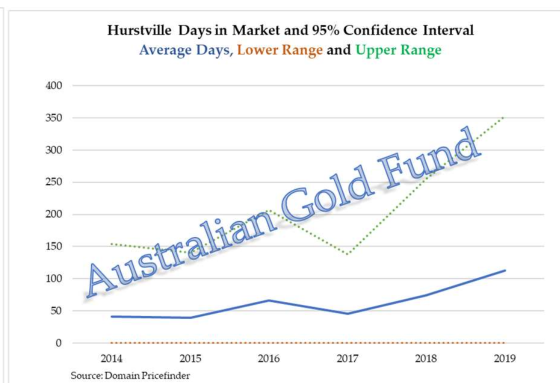
As is the case with the aggregate price data, it is abundantly clear that the market has become a buyer's market as the number of transactions have dropped at least 50% since 2017, and even 2017 sales volume is around 50% of that in 2014-2015. Despite the mood about the property market being elevated in 2017, in retrospect the market was actually sagging. By the time the media and property market experts changed their tone in mid-2018, the party has well and truly ended. Not only has the sales volume collapsed in many suburbs, even the most popular hotspots that are covered in this report, but those that are left on the market now are actually left on the shelf for an even longer time.

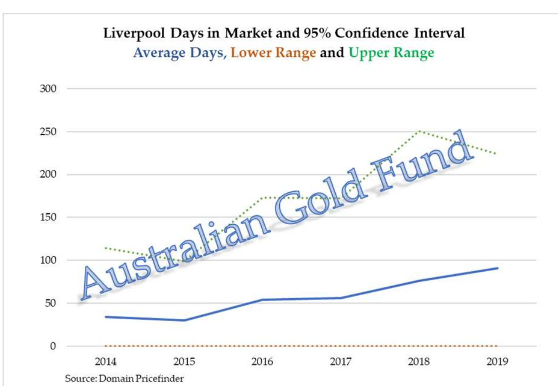
The next indicator of interest on the topping pattern of apartment prices is the average time an apartment is on the market before it is sold. The figures below show how long vendors of apartments wait to make their sale in the different suburbs:

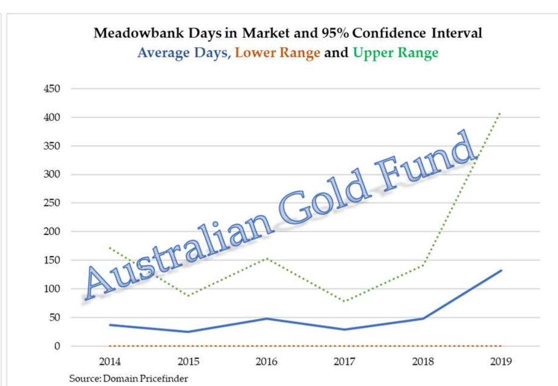


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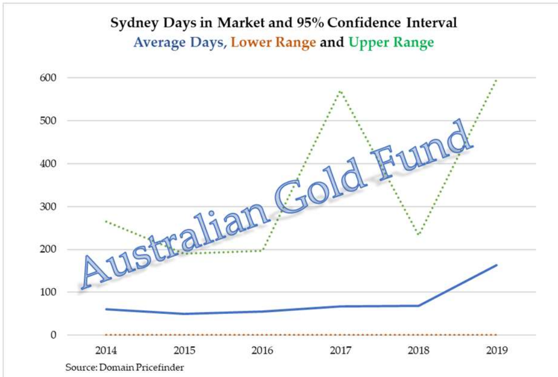



The average number of days apartments remain on the market before they are sold has doubled within the last year and the rise has been sharp. While most vendors in 2014-2018 saw the market slow down as time passed, they would have been caught out in the second half of 2018 as the buying interest diminished sharply. Anecdotal evidence of people waiting for months to sell their apartments and open house inspections or auctions with no bids trickled in but the empirical data seems to show this to be more dire than the media has made it out to be. More surprisingly, people had thought that the Sydney CBD or Chatswood would be perennially in demand because of their locality and hence buyers will always be wanting to buy a property there regardless of the price may have to think twice after looking at the data. Sydney and Chatswood apartment sales have slowed down and many sellers are waiting for at least 6 months to make a sale, if they even get an offer. Where offers are made, the price levels also suggest they have taken significant discounts on what they initially asked for. Going through individual property sales, the campaign history showed that the asking price was usually slashed over the period in order to attract buyers.

### What About the Coalition's Housing Incentives and the RBA Rate Cut?

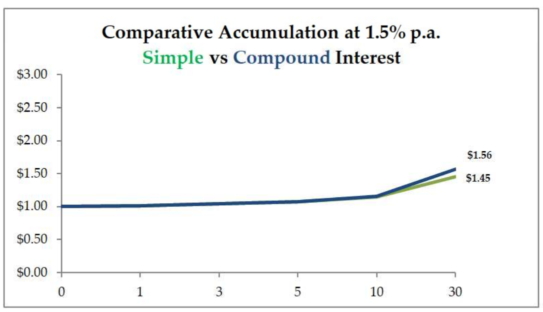
With the re-election of the Morrison government, there has been talk that confidence will return to the property market given that the Prime Minister promised to incentivise first homebuyers with a lowering of their first deposit to 5% compared to the 20% deposit needed by banks to qualify for guarantee against defaulting against their mortgage. This has also been coupled with the Reserve Bank of Australia reducing interest rates by 0.25% to an all-time low of 1.25% early June. To what extent will this help stem the falling prices and bring back market demand?

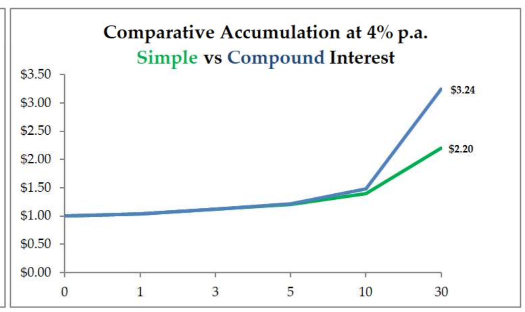
We are of the view that these measures are a drop in the bucket and may only have a temporary effect on the market due to a few reasons. The first is that the lowering of the first deposit to 5% for a guarantee on their loan does not actually resolve the housing affordability issue or reduce the burden on those with a mortgage. A $500 000 loan requires $25 000 deposit but this leaves the borrower with a loan of $475 000 they have to repay in the future, including any interest incurred over the term of the loan. A lower first deposit does not solve the problem of mortgage burden; it merely lowers the hurdle for an individual to become indebted.

The second reason is that with a reduction in the RBA Cash Rate leading to a partial or full decrease in the mortgage rates is a double-edged sword, working to take from one hand and take from another. Borrowers will face a lower interest burden on their existing mortgage but over the longer term, a lower interest rate will lead to the perception that the loan burden will reduce and thus lead to people borrowing even more. This, in turn, leads to the property price rising higher and thus requiring larger loans to be taken by future borrowers. However, this exacerbates the housing affordability problem.

The third reason is that on the savings side of the matter, lower interest rates result in slower progress in accumulating the first deposit or the need for greater risk-taking through investing in risky assets. Furthermore, savers receive around 1.5% p.a. on their bank deposits and borrow at around 4% p.a. on their mortgages. Mathematically speaking, the power of compound interest is only beneficial at a rate exceeding 3% p.a. As interest rates continue to fall, the net benefit to property buyers relying on debt sharply diminishes and becomes a greater burden on them.

| | Simple | | Compound | |
|---|---|---|---|---|
| **t (years)** | **1.5%** | **4%** | **1.5%** | **4%** |
| 0 | $1.00 | $1.00 | $1.00 | $1.00 |
| 1 | $1.02 | $1.04 | $1.02 | $1.04 |
| 3 | $1.05 | $1.12 | $1.05 | $1.12 |
| 5 | $1.08 | $1.20 | $1.08 | $1.22 |
| 10 | $1.15 | $1.40 | $1.16 | $1.48 |
| 30 | $1.45 | $2.20 | $1.56 | $3.24 |




## Future Outlook

In summary, the price trends in Sydney show that the rosy days are over. Apartments and units have peaked in the past two years and with sales volumes dropping significantly, expect that prices will correct more sharply as vendors face the reality of fallen demand and a need to cut prices if they wish to secure a sale. Many vendors in the past twelve months have paid the price (pun intended) for refusing an earlier bid in the hope of securing a higher bid, only to sell their properties months later for a substantial discount to what they were initially offered. Despite the Coalition government's measures to encourage buyers and the RBA cutting interest rates, the counter-trend of prolonged economic weakness and consumer confidence faltering will prove to overwhelm attempts to keep this market from further correction. The apartment and unit market peaked, and will likely follow the way of the houses in heading downwards. A bounce may come as a result of post-election relief and buyers seeking to capitalise on the government measures. However, it is expected that many will wake up to the fact that these measures are temporary and offer but a little relief to the longer term mortgage stress many will end up facing due to a combination of weaker income growth, slowing economy and the sheer size of the loan they have taken.

While optimism is a good thing, caution is far more important in the context of maintaining one's financial stability.

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