Australian real estate market focus

November 2020

Thinktank..

The following represents a monthly snapshot of how we see the property markets across the country along with the near-term outlook. For a more detailed commentary, please visit our website thinktank.net.au for our Quarterly Market Update. This month we feature the ATO SMSF statistics in our News and Views segment.

The Westpac-MI Consumer Sentiment Index jumped again in September by 11.9% to 105.0 after surging 18% in August driven by recovery outside of Victoria. In the last two months the index has risen to its highest level since July 2018. The AiG Manufacturing Index also leapt by 9.6 points to 56.3 moving into expansion above 50. The Services Index was also up by a spectacular 15.2 points to 51.4 its first positive month since November 2019. The Construction Index was up again in September by 7.5 points to 52.7 moving into expansion with rises in all States except Victoria and bringing all AiG indices into expansion.

At its November meeting, the RBA Board cut the Cash Rate by 15 basis points to a new record low of 0.10% as widely expected after clear signalling from the RBA Governor. While some were originally forecasting this would happen in October the Federal Budget delivered on the same day took precedence and the Treasurer certainly delivered a lot of extremely important fiscal stimulus. This was completely understandable after the second quarter GDP figures showed a 7.0% decline and with unemployment at 6.8% and forecast to rise. The action on Monetary Policy is expected to further help housing markets which noted below are now doing better than many had forecast. The US Fed has said the same about interest rates but 10 year US Treasuries were last traded at yields of 0.83% (up a bit due to the election) and AUS 10 year Gov't bonds at 0.82% (down a bit) marks the first time many can recall a lower Australian yield. Markets continue to expect interest rates to remain at these levels for some years to come and this has reversed expectations of a rising AUD which had broken through USD 0.73 but then back down to USD 0.70 and has since gone back up.

CoreLogic housing prices for October were a great start to the week preceding the RBA Board meeting and the running of the Melbourne Cup. National Housing values were up by 0.4% after five months of consistent declines. In Sydney prices were up 0.1% while in Melbourne the drop was just 0.2%. The rest of the capital cities were all up with Adelaide leading the way at 1.2%. There is quite a difference between Houses and Units and part of this is reflected in the three month rolling rents reported which were +0.8% for Houses and -2.3% for Units for the combined capitals. We had anticipated some of these developments and as a result no changes were required to our ratings and trends as noted below.

Last month we took the opportunity of preparing our Quarterly Market Update to make some changes in our ratings and trends from previous months. As a result as noted for Residential above, no changes needed this month. Retail which had already been struggling had hit even more difficult times and we wait now for its recovery. Industrial has proven to be quite resilient and appears to be everyone's favourite. Office continues to await the longer term response of businesses to work from home attitudes but we are more positive than some. As noted in the paragraph above on Residential we are seeing the start of a recovery. Our section on Residential in our Quarterly Market Update contained plenty of detail on our thinking for this key sector as well as others together with a first look at some new design features which we hope you liked.

	SYDNEY		MELBOURNE		ADELAIDE		BRISBANE (SEQ)		PERTH	
Resi- Homes	Good	Stable	Fair	Softening	Good	Stable	Good	Stable	Fair	Stable
Resi- Units	Fair	Softening	Fair	Softening	Fair	Stable	Good	Stable	Fair	Stable
Office	Good	Stable	Fair	Stable	Strong	Stable	Fair	Stable	Fair	Stable
Retail	Weak	Deteriorating	Weak	Deteriorating	Fair	Deteriorating	Weak	Deteriorating	Weak	Deteriorating
Industrial	Good	Stable	Good	Stable	Strong	Stable	Fair	Stable	Weak	Stable

Sources: ABS, ACCI, AiG, ABS, AFR, ANZ Research, ATO, CBA, CBRE, Colliers International, CoreLogic, Cushman & Wakefield, HTW, IMF, MSCI, JLL, Knight Frank, OECD, PCA, Preston Rowe Patterson, RBA, RLB, Savills Research, Westpac Economics, World Bank

News and views

- This month we look at the latest statistics on SMSFs provided by the Australian Tax Office (ATO) as at 30 June 2020. Typically the ATO has released quarterly statistics on this sector a couple of months after the quarter end however it is important to note that while 30 June is the year-end for SMSFs, these are only estimates and separately the ATO reports 30 June numbers on an annual basis once they have received a substantial number of Annual Returns which doesn't happen for some time. It is also worth noting that there is seldom significant shifts from period to period but rather it is the longer term trends that are important to try and identify.

- While the individual number of SMSFs and their members has grown strongly, it is the total assets that are most impressive. These are all shown in Graph 1 opposite with total assets now nearly $733 billion representing the largest portion of total superannuation savings, just in front of both Industry Funds and Retail Funds. Growth has levelled out over the past few years but the investment total remains a very significant figure. The graphic below was produced by the ATO to celebrate 20 years of SMSF regulation and shows $748 billion as at June 2019; this has now dipped slightly as market values were hit by COVID-19 earlier this year which is also clearly shown in the graph with the declining blue line falling from a peak of $767.3 billion in December 2019.

- Asset allocation within SMSFs continues to be a hotly debated issue with heavy concentration of assets in a particular asset class being a major concern of the Regulator. An SMSF's Investment Strategy is meant to be the tool that allows Trustees to assess specific asset allocation levels and the rationale that supports them. These are meant to be reviewed regularly and this has been interpreted as at least annually. The argument is often made that as long as the Investment Strategy accepted by the Trustee(s) justifies their position there is no specific limitation on what that is. A frequently seen range of 0 – 100% for a particular asset class would be an example of an approach that is not acceptable and should be identified as such by the SMSF Auditor involved.

- Graph 2 opposite shows the distribution across the major asset classes with Listed Shares & Trusts being the largest followed by Cash & Deposits being 32% and 21% respectively of Total Assets. This is over half of all SMSF assets being invested in very liquid but now low yielding investments. Again it can be seen how little change takes place over time other than for market volatility in listed investments which have fallen this year.

- A key area of interest for us is of course Limited Recourse Borrowing Arrangements (LRBAs) which make up a relatively small segment of Total Assets at just under 7%. The assets that secure these loans are Residential Property at 5.3% and Non-residential Property at 10.0%. The level of concentration in individual SMSFs is higher than those numbers suggest but overall the impact of LRBAs and Real Property investment is not as great as many commentators and the Regulators have suggested although they are up slightly.

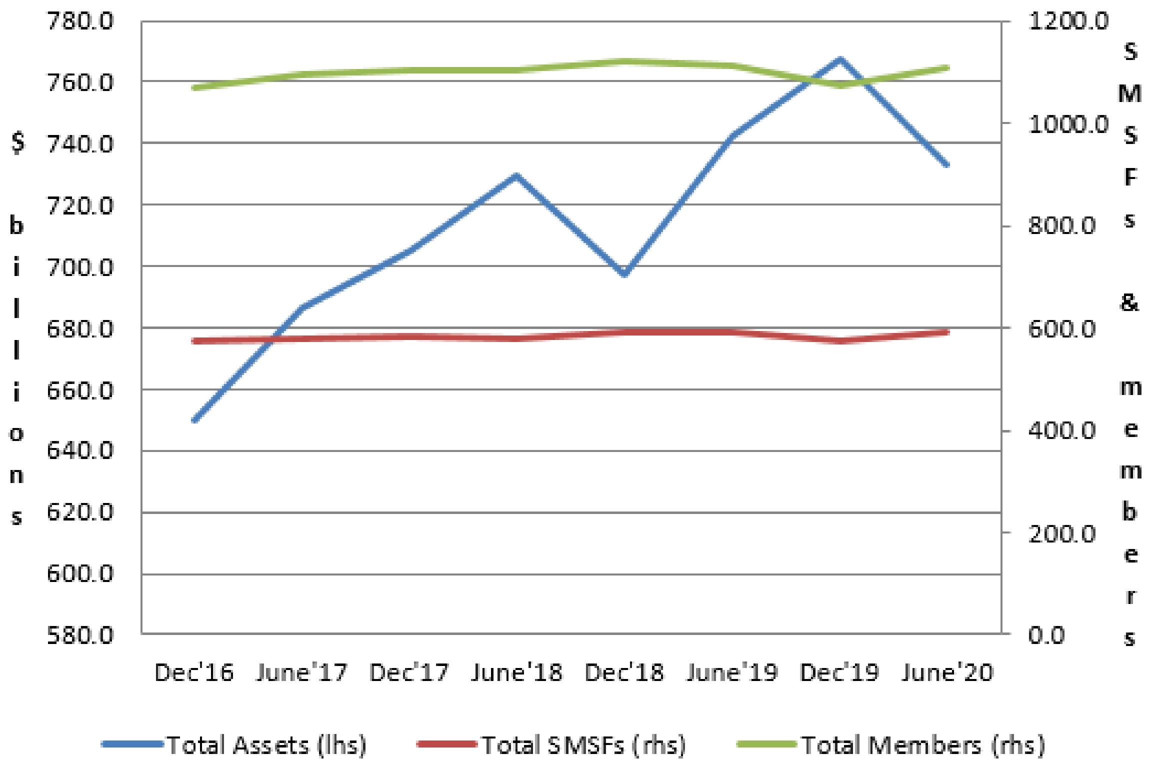
- It is interesting to note our experience during the COVID-19 crisis that our SMSF–LRBA portfolio which is similarly diverse compared to the rest of our portfolio has performed relatively better, consistent with our experience in prior periods. It seems the high % of owner-occupiers in commercial ("business real property") real estate works as a positive in stabilising performance during economic difficulty. This may be because a high percentage of third party tenants took advantage of rental relief available through emergency legislation. We are however already seeing regular loan repayments being resumed by most LRBAs and Victorian based SMSFs are expected to follow now that many lock-down restrictions have been lifted in that State.

Australian Government
Australian Taxation Office

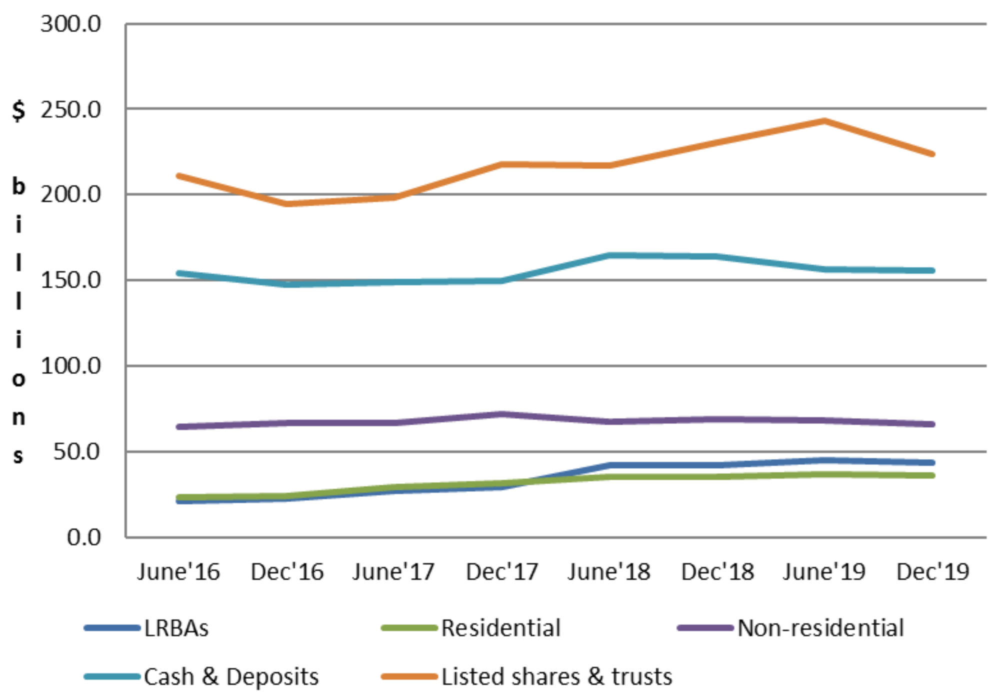
20 Years Regulating and protecting SMSFs

ato

Graph 1 – SMSF Total Assets and Numbers



Graph 2 – SMSF Investment Portfolio Data



Source: Australian Tax Office

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Thinktank Property Finance

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- Finance for the purchase, equity release and refinance of commercial and residential property;
- Set and forget loan terms up to 30 years with no ongoing fees or annual reviews;
- Self-Managed Superannuation Fund (SMSF) loans; and
- Loan serviceability options ranging from fully verified to self-certification of income.