

The following represents a monthly snapshot of how we see the property markets across the country along with the near-term outlook. For more in depth commentary, please visit our website thinktank.net.au for our latest Quarterly Market Update. This month in News and Views we once again take a closer look at MSCI's review of Australia's property sector during the first half of 2021.

The Westpac-MI Consumer Sentiment Index rose by 2.0% in September to 106.2 and was described as truly remarkable at a time when Australia's two largest cities were in lockdown. This month's results for the AiG Manufacturing Index saw a small decrease of 0.4 points to 51.2 after a large 9.2 points decline last month but still maintaining a 12th month of expansion above 50. The PCI Construction index after a fall 10.3 points to 38.4 last month rose an astonishing 14.9 points to 53.3, returning to expansion although all of the gains were in engineering construction with commercial and residential experiencing further declines. The PSI Services index rose slightly by 0.1 points to 45.7 and not surprisingly remains in contraction for a second month.

At its October meeting the RBA Board once again left the Cash Rate at the record low of 0.10%. Governor Lowe's remarks contained a new comment about possible action to maintain lending standards and the following day APRA announced an increase in the "interest rate buffer" to be used by banks in calculating servicing capacity of home loan applicants. The Governor also reconfirmed the view that rates would not rise until 2024. He also noted we are now facing a negative growth September quarter from the latest lockdowns but the positive second quarter saves us from another recession as long as we experience the expected recovery in the fourth quarter as restrictions are lifted and consumer confidence returns. August Retail sales released by the ABS were down 1.7%, the third monthly fall in a row. All states fell except for WA and SA which rose 2.8% and 6.6% respectively with no lockdowns. 10 year US Treasury Yields were last traded up at 1.54%; AUS 10 year Gov't bonds matched that increase at 1.57%. The AUD has traded at around 0.73 since last month.

CoreLogic dwelling prices for September continued the upward run of the past few months but again at a somewhat reduced pace. National Housing values were up by a further 1.5% for the month and a total of 20.3% for the past year. In Sydney House prices were up 2.0% for the month and a remarkable 28.9% for the last 12 months. The results were a little less in Melbourne up 1.1% for the month and 18.0% for the past year. The rest of the capital cities except for Perth at 18.5% had over 20% growth for houses for the past twelve months. There continues to remain a difference between Houses and Units with Units on a national basis up 12.0% for the year. As noted above the prospect of lending controls was mentioned by the RBA at their monthly Board meeting and the following day APRA announced controls on interest rate buffers used by Banks in assessing serviceability of borrowers with an increase from plus 2.5% to 3.0% in calculating Interest Coverage Ratios.

We continue to be encouraged by the extension of the rise in Residential even though some are obviously rather more concerned than ourselves but our Ratings and Trends are unchanged. Retail continues to struggle and we are still waiting for signs of a turnaround which may have to await the end of lockdowns. The August fall in national retail sales was as expected with the current NSW and Victoria lockdowns being very damaging; down 3.5% and 3.0% respectively. Industrial continues to be very strong and remains the market favourite and strengthening. Office has responded to some favourable public comments and we take a closer look at all sectors in the MSCI half-year update in our News and Views as well as our Quarterly Update.

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

Once again we are taking a look at the MSCI Australian All Property performance reports for the periods ending 30 June 2021. What is very encouraging is that all sectors are showing improvement and the various charts and graphs produced by MSCI for their webinar really identify what is driving this improvement and within which sectors and in which capital cities.

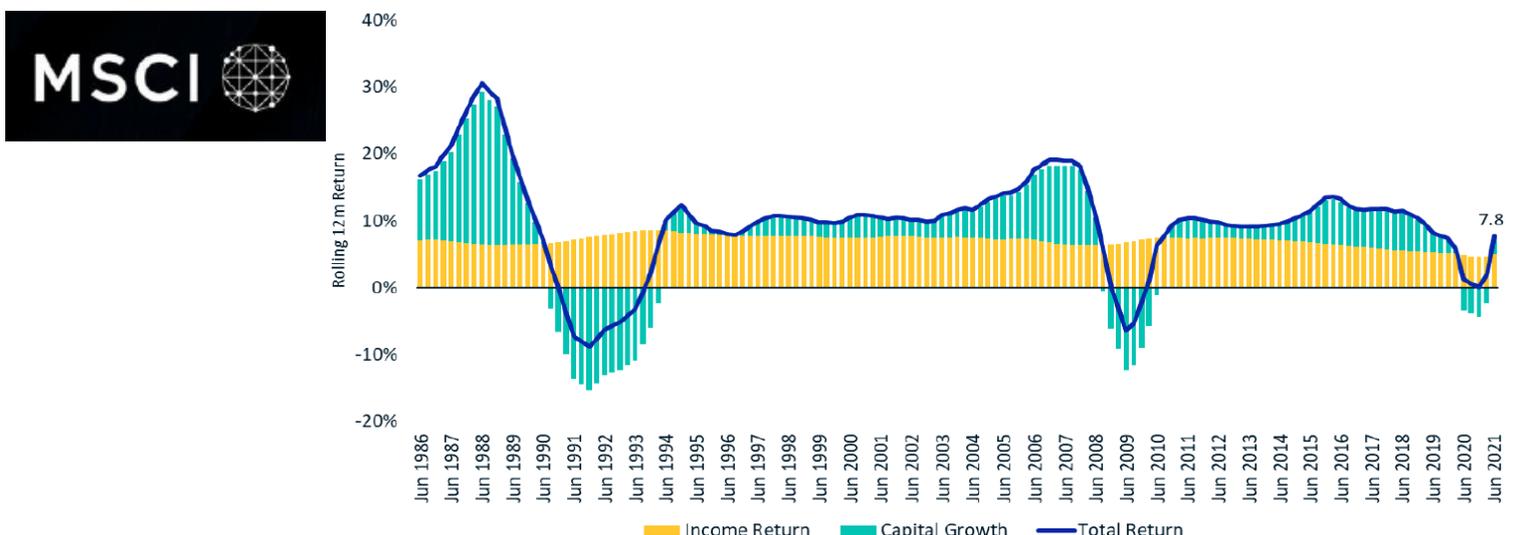
The graph below was the usual opening slide for MSCI property updates and provides a great long-term view of the performance of all of the sectors followed by MSCI in Australia. What continues to strike me is the consistency of “income returns” over the years and while interest rates fluctuate these tend to be more reflected in “capital returns” driven by movement in yields and capitalisation rates. For relatively short periods returns will drop sharply but then recover quite rapidly as we have seen over the past year as yields have fallen to record lows in many areas driving total returns up to 7.8%. We can see how widely these returns vary from sector to sector and across the various capital cities reflecting both physical demand from tenants and investor appetite.

Graph 1 opposite highlights the very wide divergence between the sectors with the greatest difference to be seen between Industrial and Retail with Retail moving through negative returns from March 2020 and recovering to positive returns in the June 2021 quarter as capitalisation rates in the sector started to compress in line with other sectors and catching up with lower long term rates. It is quite amazing to see the contrast with Industrial as capital values were strongly driven by an early compression as long term rates started to fall but then continued to move lower as sentiment firmed for what had for many years been considered a high yield product. Really quite an incredible shift between the two sectors. Similar comparisons can be made with Hotels and Healthcare while Office has started a slow recovery as investors await confirmation of what has been a high degree of confidence in a post-pandemic recovery despite mostly empty offices in Melbourne and Sydney.

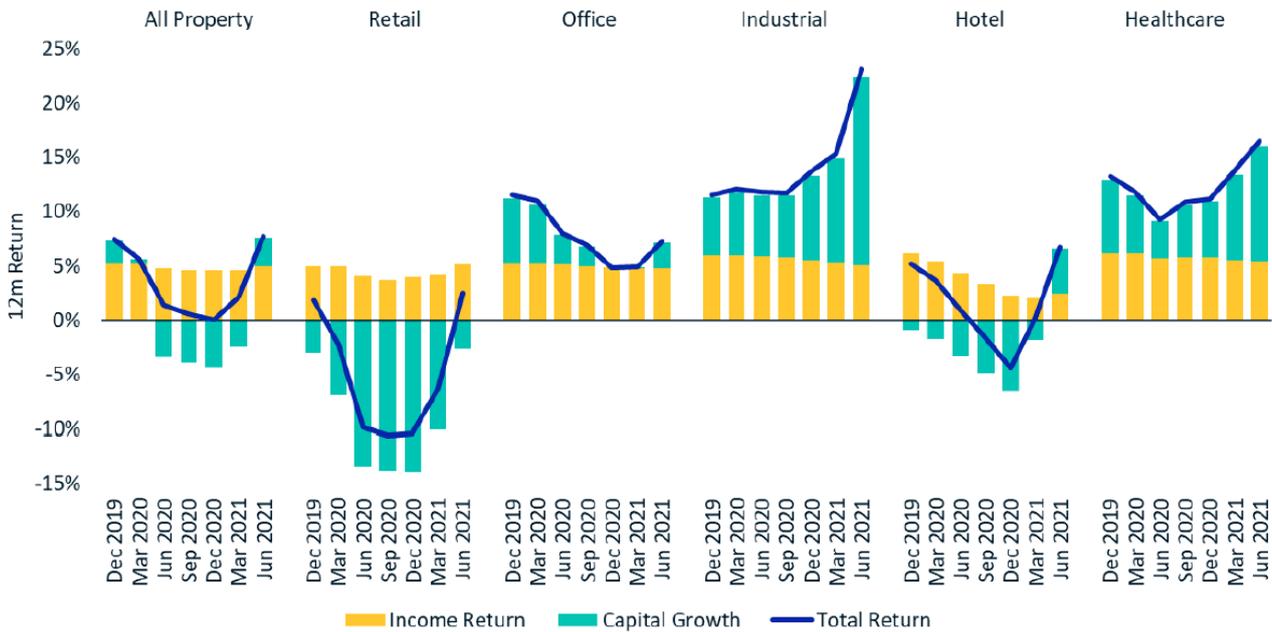
Graph 2 shows how widely performance has varied from capital to capital with some like Adelaide moving from -5.4% total return to +9.5%. This recovery of 14.9% compares to Sydney’s of 4.4% despite a relatively strong performance throughout the pandemic. Melbourne has struggled to recover as quickly as other capitals no doubt due to the length of their lockdowns but others such as Perth have simply had to deal with sluggish activity and historically high vacancy rates that have little to do with COVID-19. Brisbane is recovering at about the same pace being up 7.4% from last year compared to Perth’s gain of 7.2% but from a lower base.

The indications from this MSCI report are that things were improving in the property sector and while the period during the months immediately after has seen both Melbourne and Sydney in lockdowns, there is reason to believe the recovery will once again pick-up once the lockdowns are lifted which will start very shortly. A significant factor is that Australian interest rates will not be rising anytime soon which is a major positive.

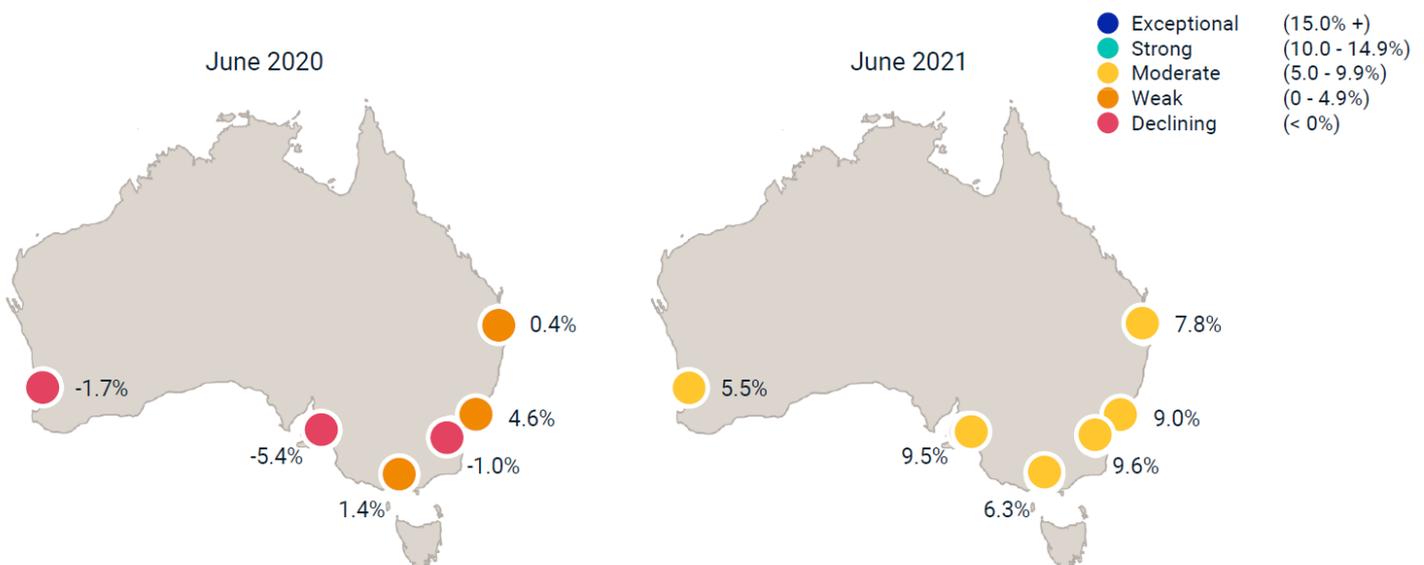
Australian All Property Annual Total Return June 1986 to June 2021



Graph 1: Australian Quarterly Sector Returns, MSCI – December 2019 to June 2021



Graph 2: Australian Capital City Total Returns, MSCI – June 2021



Source: MSCI

Business relationships and loan inquiries

Heather Noonan

Regional Sales Executive
VIC / TAS / SA
M: 0435 960 646
E: hnoonan@thinktank.net.au

Joel Harrison

Regional Partnership Manager
VIC / SA / TAS / WA
M: 0410 861 540
E: jharrison@thinktank.net.au

Tony Zaccari

Senior Relationship Manager
VIC / SA
M: 0403 758 514
E: tzaccari@thinktank.net.au

Dev De

Senior Relationship Manager
VIC/TAs
M: 0466 576 338
E: sde@thinktank.net.au

Amod Mahatme

Relationship Manager
VIC
M: 0466 632 212
E: amahatme@thinktank.net.au

Cath Ryan

Regional Sales Executive
NSW / ACT
M: 0433 862 944
E: cryan@thinktank.net.au

Rob Tassone

Regional Partnership Manager
NSW / ACT / QLD / NT
M: 0450 642 995
E: rtassone@thinktank.net.au

Ranei Alam

Senior Relationship Manager
NSW
M: 0434 609 240
E: ralam@thinktank.net.au

Paul Burns

Senior Relationship Manager
NSW
M: 0434 609 241
E: pburns@thinktank.net.au

Claire Byrne

Relationship Manager
NSW
M: 0414 235 478
E: cbyrne@thinktank.net.au

Sam Dobbins

Relationship Manager
NSW
M: 0414 010 365
E: sdobbins@thinktank.net.au

Robyn Hadlow

Relationship Manager
NSW / ACT
M: 0406 857 708
E: rhadlow@thinktank.net.au

Adam Hutcheson

Regional Sales Executive
QLD / WA / NT
M: 0434 609 239
E: ahutcheson@thinktank.net.au

Kat Gasparovic

Relationship Manager
QLD / NT
M: 0405 815 287
E: kgasparovic@thinktank.net.au

Bob Whetton

Relationship Manager
QLD / NT
M: 0413 241 316
E: bwhetton@thinktank.net.au

Robert Ilov

Relationship Manager
QLD / NT
M: 0424 685 008
E: rilov@thinktank.net.au

Alex Turnbull

Marketing Manager
M: 0400 599 535
E: aturnbull@thinktank.net.au

For additional information, please contact

Publications & Market Update

Per Amundsen

Company Secretary
T: (02) 8669 5515
M: 0417 064 252
E: pamundsen@thinktank.net.au

Partnerships & Distribution

Peter Vala

GM Partnerships & Distribution
T: (02) 8669 5512
M: 0468 989 555
E: pvala@thinktank.net.au

Investor Relations

Lauren Ryan

BDM – Investments
T: (02) 8669 5532
M: 0401 974 839
E: lryan@thinktank.net.au

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