Australian real estate market focus

December 2022

Thinktank..

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 take a look at the latest MSCI Capital Report and a recent Knight Frank Australian Industrial Review

The Westpac-MI Consumer Sentiment Index fell in November by 0.9% to 83.7 reversing last month's increase, returning to near historic lows well below the 100 (neutral) level of confidence, impacted by inflation and interest rate increases. The Westpac Leading Index for October saw the index fall to -1.19 from -1.09, to be at its weakest pace since the start of the pandemic. The result for the AiG Manufacturing Index for November was down by 4.9 points to 44.7 falling further into negative territory below 50. The AiG PCI construction index was up by 4.9 points to 48.2 but still in contraction. The PSI covering services and retail for November was down by 2.1 points to 45.6 and further into contraction below 50 and leaving all three of the AiG indices in that situation.

At its December meeting the RBA Board raised the Cash Rate 0.25% for a third month after four 0.50% increases in a row. This takes the rate from 2.85% to 3.10%. While further increases are expected in the New Year following the Board's January break, the slowing of the pace of increase over the past three months is viewed positively. Governor Lowe's remarks after the meeting again left economists expecting further increases but of a more moderate amount as signalled last month. The following day the 3rd quarter GDP was announced by the ABS up 0.6% for the quarter and 5.9% through the year. Retail sales for September were also positive being up 0.6% for the month and 17.9% yoy. The unemployment rate of 3.4% in September was little changed in months and continues to demonstrate the resilience of the Australian economy. The US Federal Reserve at its December meeting is expected to raise its base rate by 0.75% again and has signalled more increases to come and the Bank of Canada kept their November increase at 0.50% raising its rate to 4.25% with much the same comments as made by the RBA. At the start of the month 10 year US Treasury Yields traded at 3.44% and AUS 10 year Gov't bonds were at 3.31%. The AUD has now risen to USD 0.6742 at the start of December.

CoreLogic dwelling prices for November continued their decline but at a slightly slower pace. National Housing values posted a 1.0% fall for the month compared to 1.2% in October. The fall was 3.5% for the quarter nationally down from 4.1% last month. The fall of 4.4% in Sydney and 2.7% in Melbourne were also both down slightly. In Sydney, House prices were down 1.5% for the month with units down 0.9% and the results were similar in Melbourne with houses down for the month 1.0% while units were down by just 0.2%. Adelaide and Perth are showing signs of recovery this month with dwellings down just 0.3% and flat respectively but Brisbane Houses fell 2.2% for the month. Regionals were down less than Capitals by -0.9% to -1.1% for the month but very slightly down more -3.6% to -3.5% for the quarter but both figures are an improvement over last month.

We have continued to reflect the further but slower decline of Residential in almost all areas and have maintained our ratings and trends across most capitals. Sydney and Melbourne houses and units remain Weak and Declining and Brisbane has joined them. Retail continues to be showing some recovery as sales continue to improve as noted above. Office continues its slow recovery from the pandemic lockdowns but is just Fair. Industrial remains very strong and we are maintaining our Ratings and Trends which are either Strong or Good with an Improving Trend in each of the capitals. This is reflected in the MSCI Capital Report as well as the Knight Frank Q3 Industrial Review and we look at both in our News and Views segment.

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

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

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News & Views

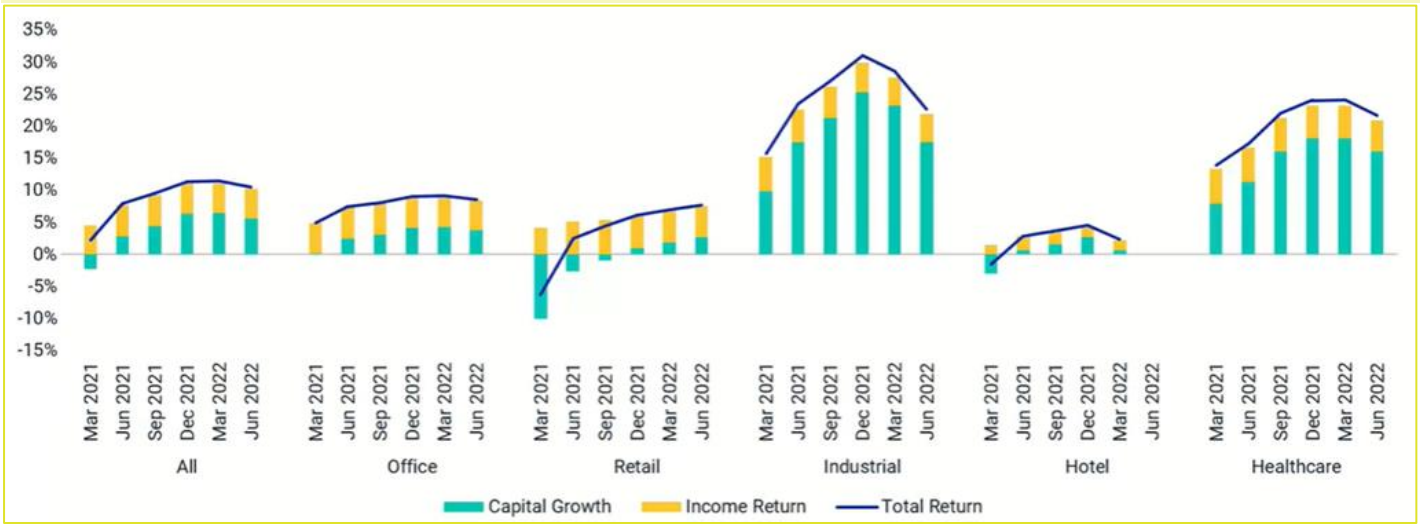
- Knight Frank recently released their Australian Industrial Review for Q3 – 2022 which reported strong sector performance in all the capital cities it covered which are the same as those reflected in our Ratings and Trends table on the front page of this report. This also continues to reflect the MSCI research and data contained in their briefings which are summarised by the graph shown below with Industrial continuing to lead the way with overall returns boosted strongly by capital growth. Other sectors are however improving and this can be seen particularly in Retail which has recovered from significant negative capital growth last year.

- Table 1 opposite shows more recent movement in Industrial yields across the capital cities and these have only recently begun to reflect the pressure of rising interest rates. The separate Knight Frank research report particularly highlights the modest softening of yields has largely been offset by rental growth with examples of Perth experiencing the fastest pace of rental growth nationally with prime rents up by 32% year over year and 14% in the quarter offsetting a 25 basis point rise in yields reported as 4.50% - 5.00%. Other comments for the other four capitals are similarly positive although to varying degrees with Sydney described as evidencing "unprecedented rental growth across the board."

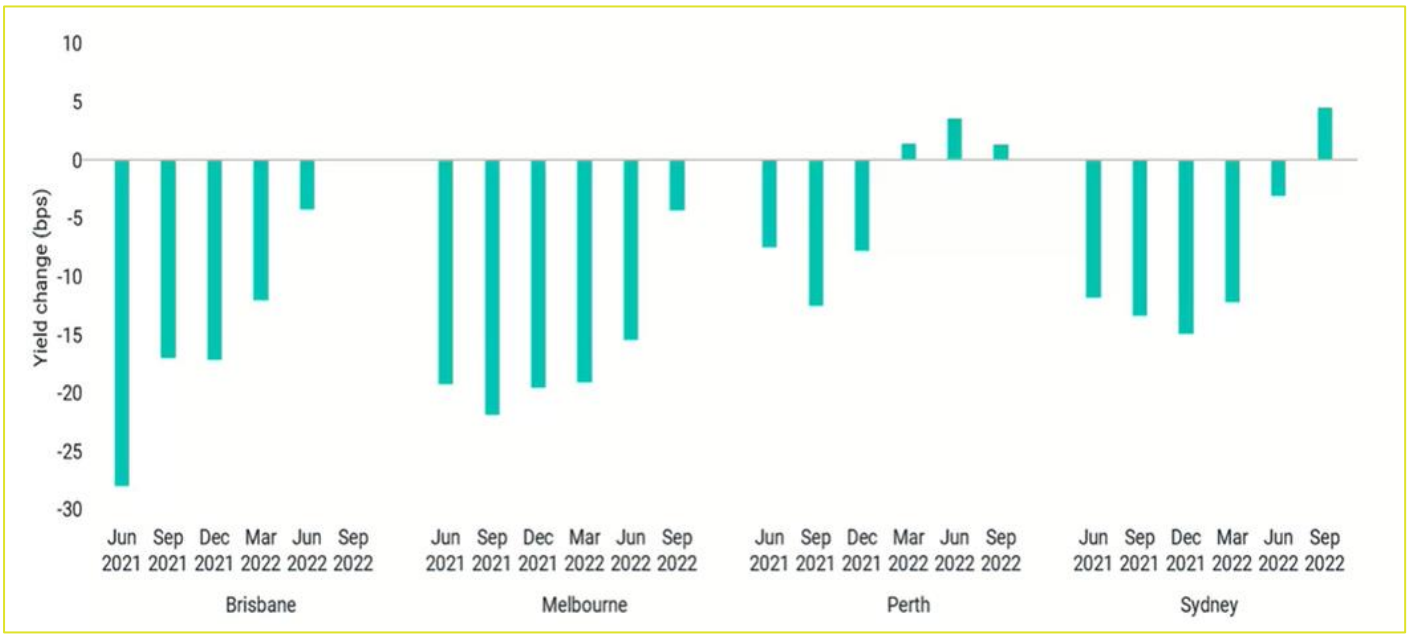
- A recent AFR article featured an interview with MSCI's Ben Martin-Henry who noted that several sectors experienced a rise in yields during the third quarter. Offices in Sydney, Brisbane and Perth but not Melbourne had seen a rise in yields and so did regional, sub-regional and neighbourhood shopping centres; "most notably the Sydney industrial sector saw the first increase in cap rates in six years". He also said "While the December valuations due out over the next month should show a touch of the wind back but only a touch, until further transaction evidence emerges." The article also quoted Barrenjoey's Head of Real Assets Research as saying "Book values would wind back about 11% for Retail, 7.5% for Premium Office but 35% for B-grade buildings however some Industrial values will actually rise".

- Graph 2 opposite was the topic of further discussion in the AFR article noted above. The headline was "With the market slowdown well under way, buyers and sellers are quietly testing each others determination". The graph provided by MSCI Real Assets compares commercial property sales priced over $1 million settled thus far this quarter and shaping up as the slowest since 2016. Ben Martin-Henry said " While the numbers are preliminary and further deals are expected, at this point in time a significant slowdown is underway with sales 43% below the average of the past decade." He went on to say the slowdown is caused by "the various global macro-economic pressures pervading the economy, a general feeling of uncertainty, and, of course the substantial increase in capital cost.

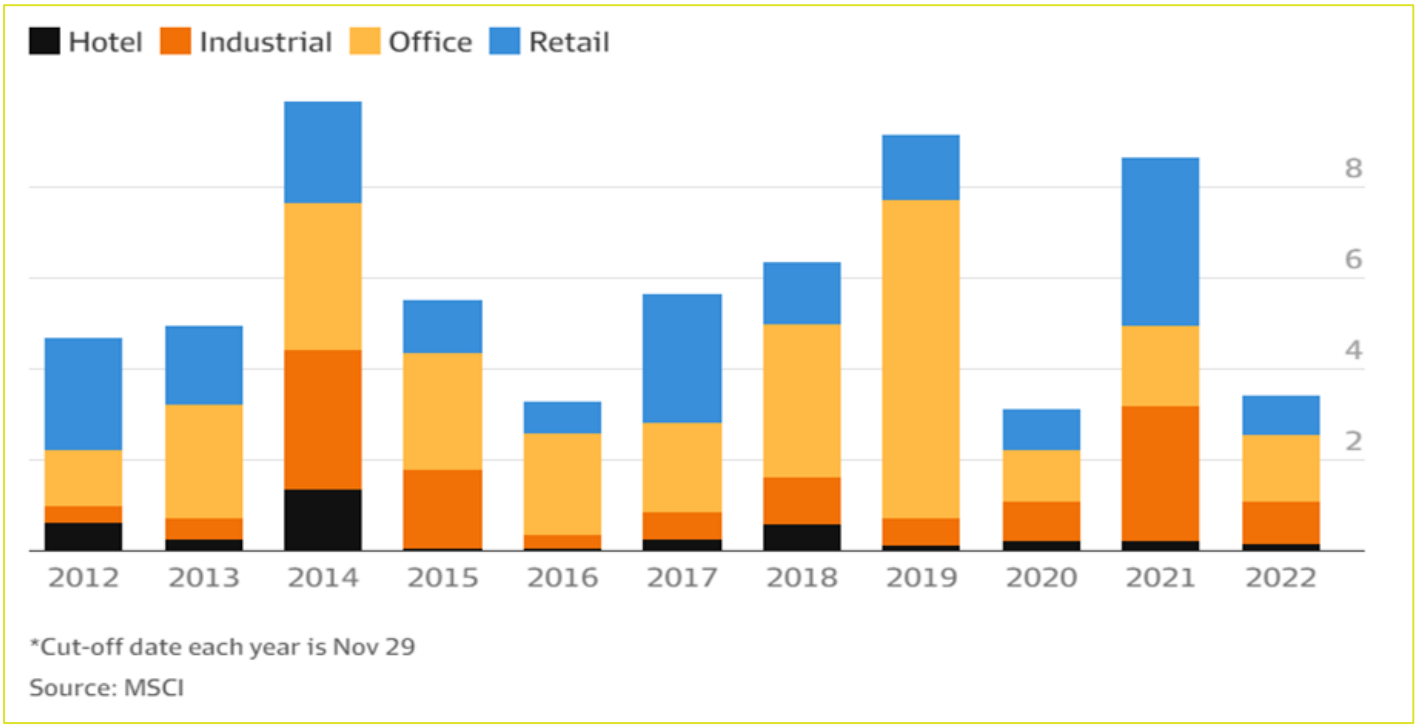
Australian Commercial Property Sector Total Returns: Q2 2022, MSCI



Graph 1: Australian Industrial Yields



Graph 2: Fourth quarter* tallies in commercial property deals ($b)



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