Data snapshot

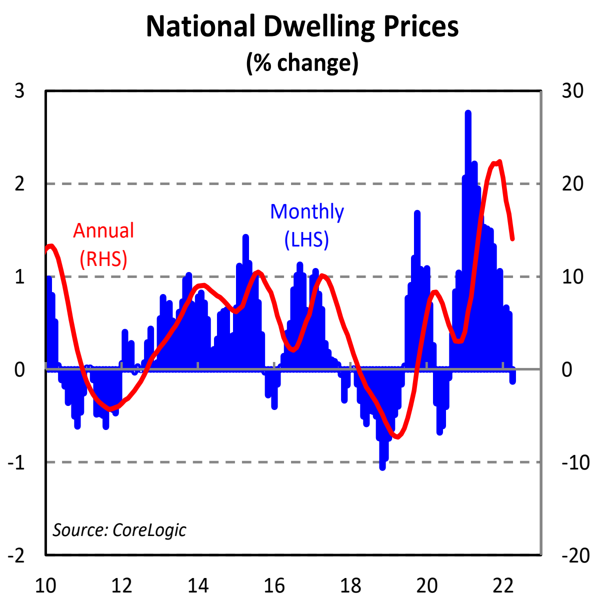
Bank of Melbourne

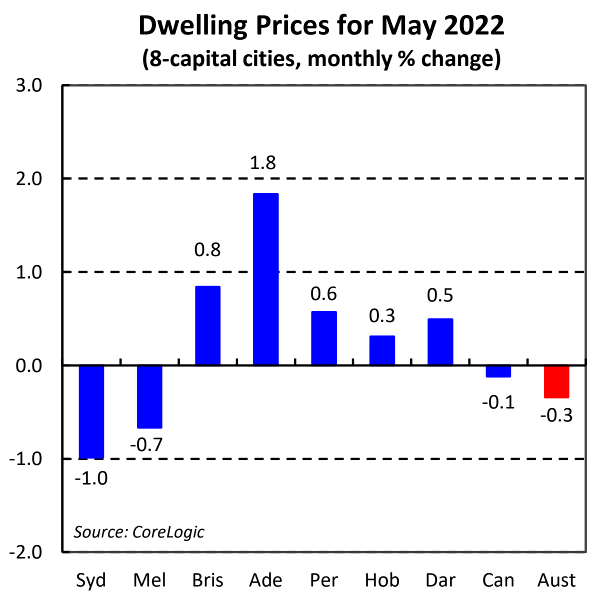
Wednesday, 1 June 2022

Dwelling Prices

Prices Slip for First Time in 20 Months

- **Dwelling prices declined by 0.1% in May as the first increase in the cash rate in 11½ years and a range of other headwinds impacted the market. This was the first national drop in dwelling prices since September 2020.**
- **Stretched affordability, higher fixed interest rates, an increase in listings across the two largest capital cities, and the prospect of interest rate hikes by the Reserve Bank (RBA) have all been weighing on housing market sentiment over recent months.**
- **In May, the fall in the national index was driven by decreases in Sydney (-1.0%), Melbourne (-0.7%) and Canberra (-0.1%). For Sydney, this was the largest monthly fall since January 2019. Other capital cities and regional areas continued to report gains in the month.**
- **Despite a decline in the national index, conditions across the country remain quite varied. The relatively more affordable capital cities of Brisbane and Adelaide have been performing strongly. However, momentum slowed considerably in Brisbane, where prices rose by 0.8% in May. Monthly price growth in Adelaide also slowed but remained elevated (1.8%).**
- **Regional areas continued to outperform capital cities. The combined regional index rose by 0.5% in May, compared to a 0.3% fall across the combined capitals index. House and unit prices both declined by 0.1% in May.**
- **The housing market is facing a range of headwinds, including future expected increases in the cash rate. Momentum is projected to continue to slow further and price falls are expected to become more widespread through the rest of the year and into 2023.**





Dwelling Prices

Dwelling prices declined by 0.1% in May as the Reserve Bank's (RBA) first increase in the cash rate in 11½ years and a range of other headwinds impacted the market. Since monthly growth peaked at 2.8% in March 2021, the housing market has been consistently losing steam. That loss of momentum has now translated into the first national drop in dwelling prices since September 2020.

Stretched affordability, higher fixed interest rates, an increase in listings across the two largest capital cities, and the prospect of interest rate hikes by the RBA have all been weighing on housing market sentiment over many months.

In May, the fall was driven by decreases in Sydney (-1.0%), Melbourne (-0.7%) and Canberra (-0.1%). Other capital cities and regional areas continued to report gains in the month. However, those gains only partly offset the falls.

In quarterly terms, national dwelling price growth declined to its slowest pace since October 2020, as dwelling prices rose by 1.1% over the three months to May. In annual terms, dwelling prices rose by 14.1% over the year to May. This was the slowest rate of annual growth since June 2021. The annual growth rate continues to decline as months with high rates of growth from early in 2021 drop out of the annual growth calculation.

Despite a fall in the national index, conditions across the country remain quite varied. In May, prices across the largest capital cities of Sydney and Melbourne declined by 1.0% and 0.7%, respectively. For Sydney, this was the largest monthly fall since January 2019, while it was the largest monthly decline since September 2020 in Melbourne. Prices in Sydney are now 1.5% below the peak in January 2022 and prices in Melbourne are 0.8% below their peak in February 2022.

Higher levels of supply (i.e. the stock) across Sydney and Melbourne have contributed to the weakening conditions in those markets. Listings across the two cities are above levels a year ago and also above their respective five-year averages. However, supply remains low and below average across other regions, contributing to continued price appreciation in other parts of the country. Nationally, listings remain almost 30% below their five-year average.

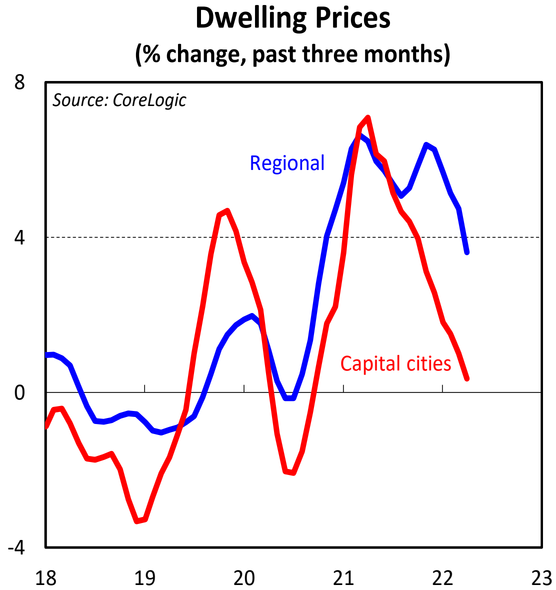
The relatively more affordable capital cities of Brisbane and Adelaide have been performing strongly over recent months. Supply levels across these two cities are almost 40% below their respective five-year averages, contributing to upward price pressure in these markets. Prices continued to increase in May. However, momentum has slowed considerably in Brisbane, where prices rose by 0.8% in the month. This was the slowest rate of monthly growth since November 2020 and broke a run of 15 consecutive months of growth above 1%. Monthly price growth in Adelaide also slowed but remained elevated in May. Dwelling prices grew by 1.8% in the month, down from the 1.9% rate of growth in April and March.

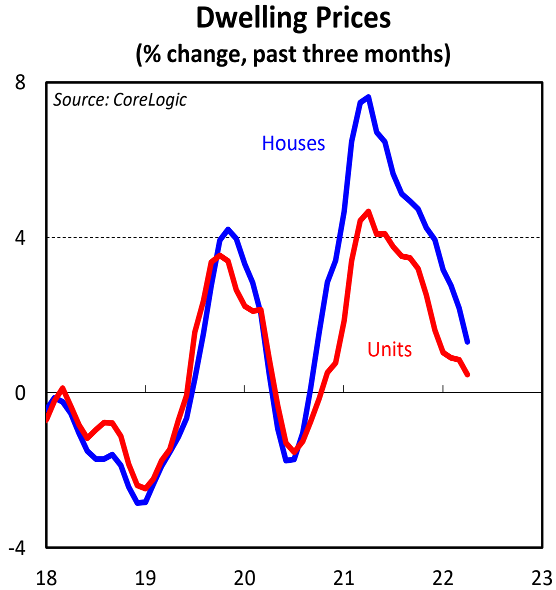
In quarterly terms, growth in Brisbane slowed to 4.6% over the three months to May, down from 5.7% over the three months to April. Bucking the trend, quarterly growth over the three months to May accelerated to 5.7% in Adelaide, up from 5.4% over the three months to April. However, quarterly growth remained below the peak of 7.4% over the three months to January.

Other capital cities reported growth in May. Dwelling prices grew by 0.6% in Perth, 0.5% in Darwin and 0.3% in Hobart.

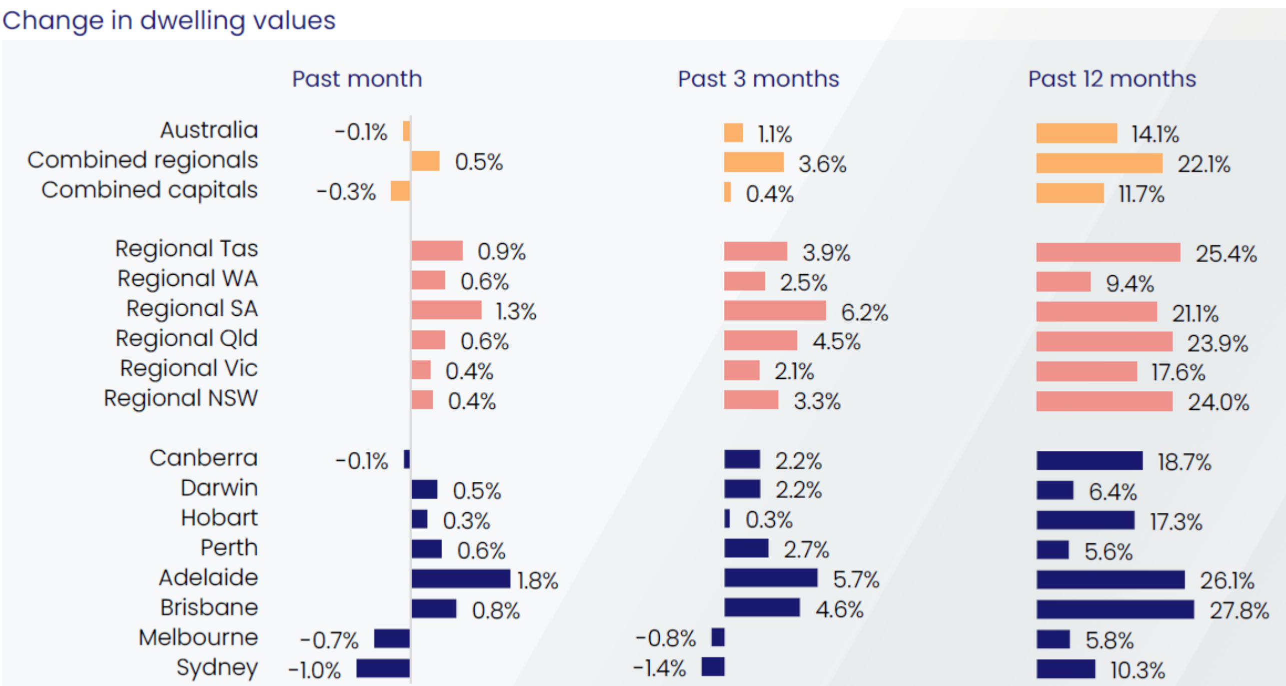
Regional areas continued to outperform capital cities. However, growth in regional areas also lost momentum. The combined regional index rose by 0.5% in May, compared to a 0.3% fall across the combined capital city index. This was the weakest monthly growth rate for regional areas since

September 2020 and broke a run of 18 consecutive months of growth above 1%.





During this property boom, house prices consistently outperformed unit prices. This reflected changing preferences among households, as people sought to move to larger dwellings with more space and took advantage of the ability to work from home to move further from city centres. Over the three months to May, house prices continued to outperform unit prices, rising by 1.3% against a 0.5% increase for units. However, momentum is slowing across both categories. On a monthly basis, house and unit prices both declined by 0.1% in May. As affordability has continued to deteriorate and houses prices have accelerated, units have become relatively more affordable. This relative price differential may add some support to unit demand into the future.



Outlook

A range of headwinds have been facing the market for several months. In May, the RBA increased interest rates for the first time in 11½ years and more rate hikes are expected over coming months. Additionally, affordability is stretched, supply has increased in the largest capital cities of Sydney and Melbourne, and fixed interest rates have risen from low levels seen earlier in the cycle.

Momentum is expected to continue to slow and price falls are expected to broaden as these factors weigh on housing market sentiment through 2022 and 2023. We expect the RBA to increase interest rates to 1.75% by the end of 2022, before continuing to raise rates in the first half of 2023. This will contribute to expected dwelling price falls over the second half of 2022 and through 2023.

Household debt levels are elevated across Australia. Some households have accumulated large savings buffers, which will help provide a buffer against future interest rate increases. However, not all households are in this position. Lower-income and lower-wealth households are likely to have smaller buffers and will face greater pressure from increases in interest rates.

On the other side of the ledger, the labour market is strong and the unemployment rate has fallen to a near 50-year low. Wages growth is expected to pick up, reflecting the tightness of the labour market. These factors will support housing demand and limit the extent of price falls.

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