Growing concerns about Australia's housing bubble

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Recent weeks have demonstrated the increasing precariousness of Australian capitalism's reliance on soaring property prices, particularly over the past two years, to offset the implosion of the two-decade mining boom and the worsening fallout from the 2008–09 global economic breakdown.

Investment in the mining sector is still plummeting because of collapsing demand for raw materials in China and globally. Australia's economy has so far avoided a recession, unlike other export commodity-dependent countries. But that is largely because of debt-fuelled household spending, undertaken on the basis of record low interest rates and steep rises in housing values.

Last week's national accounts illustrated this unstable situation. As a headline figure, gross domestic product (GDP) rose by 0.6 percent, seasonally adjusted, in the December quarter of 2015. That was a marked slowing of growth to an annualised 2.4 percent, down from the annualised 3.6 percent recorded during the first quarter of 2015.

Treasurer Scott Morrison seized on the headline result of 3 percent growth during 2015 as a whole, falsely claiming it as evidence the economy was successfully shifting from dependence on resources to broader sources for growth. "We are now growing faster than every economy in the G7 and well above the OECD average," he said.

In reality, most of the growth in the last three months of 2015 came from household consumption expenditure, which contributed 0.4 percentage points to GDP, and public fixed capital formation (government spending), which added 0.2 percentage points.

Without those two factors, the economy would have registered nil growth. Business investment, which has been falling for two years, continued to plummet—an indicator of the underlying economic deterioration. Private business investment fell 3.3 percent during the quarter, driven by a 12.3 percent drop in engineering construction.

Falling wages are making the housing bubble all the more unsustainable, and socially explosive. Homes are being priced further and further out of the reach of millions of young and working-class people. Since 2008, average house prices in the two most populous cities, Sydney and Melbourne, have risen 80 and 50 percent, but real wages have now been declining for three years.

The consumer price index (excluding volatile items) increased by 7.2 percent over the three years from December 2012, while the wage price index—a measure of wages per hour excluding bonuses—rose by only 7 percent.

Average wage income per person continued to fall, by 0.6 percent, in the December quarter, reflecting the ongoing attack on wage levels by employers and the elimination of thousands of full-time jobs in the mining industry, car and steel plants, retail stores and other basic industries.

Revealing the growing disarray in Prime Minister Malcolm Turnbull's government. Immigration Minister Peter Dutton directly undercut Treasurer Morrison's effort to shore up business and consumer confidence. Trying to discredit a Labor Party pledge to confine "negative gearing" tax incentives to new houses, Dutton said the policy would be a "disaster" because it would lower house prices and lessen the capacity of property investors to take out margin loans to buy shares. "I think the economy will come to a shuddering halt and I think the stock market will crash," he declared.

Dutton's remarks underscored the extent to which the economy now depends on this speculative activity. Former Victorian Liberal Premier Jeff Kennett added to the sense of crisis, denouncing Turnbull as a self-interested and cowardly leader who was raising the possibility of calling an early federal election "simply to cover up [the government's] own failings."

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The government's in-fighting and mounting criticisms by the corporate elite of its failure to impose pro-business austerity measures are compounding nervousness about the danger of a property crash. Westpac bank's consumer confidence index dipped below 100 for January, indicating that pessimists outnumber optimists. The share of survey respondents who believed real estate to be the wisest place for their savings plunged to 14.7 percent, from 23 percent in December.

Concerns that Australia's housing market resembles that of the United States on the eve of the 2007–08 "sub-prime" loan crash were aired in the *Australian Financial Review* last month. Hedge fund Variant Perceptions released a report comparing the dubious lending practices and sky-rocketing house prices in western Sydney to those documented in the film *The Big Short*. The report described meetings with 20 mortgage brokers where prospective borrowers "were coached on how to get things through banks" and told that banks did not check pay slips in assessing loan applications.

There are signs that the bubble is due to burst. In the past two years, Australia's housing stock has surged $900 billion in value to $5.6 trillion, or 3.6 times Australia's GDP—a larger ratio than either Japan or Ireland exhibited before their housing markets crashed in 1989 and 2006.

Australian household debt as a share of GDP has surged to 120 percent, the highest ratio in the industrialised world. Almost half of new loans are being written by third parties, mostly mortgage brokers, who are paid on commission with little incentive to ensure the loan is ultimately repaid.

More than 40 percent of loans (about 70 percent for investor loans) being issued are "interest only"—that is, the lenders are not required to pay the loan amount for decades to come—all on the expectation of endlessly rising house prices.

Between 2011 and 2015, housing investment more than doubled, temporarily offsetting the mining crash, but it began to drop last April, with the biggest fall-off in apartments. Corporate economic forecaster BIS Shrapnel has warned of a "very messy end" to the apartment boom, with all cities, except Sydney, expected to be in over-supply by 2017.

The acceleration of mortgage debt appears to have reached its limit. Both the value and number of new housing loan approvals fell in January from December, by 3.4 percent and 3.9 percent respectively. Investors continued to withdraw, with the value of their loans falling by 14.8 percent to $11.4 billion, compared with averages of about $14 billion a month last year. Building approvals also dropped 7.5 percent in January—twice the fall economists had expected.

Average rents are already falling in mining-dependent states—down by 8.4 percent in Perth, the capital of Western Australia, over the past year—and are predicted to start dropping in Sydney and Melbourne in coming months. Average weekly Sydney rents stand at $598, up just 1.5 percent over the past 12 months.

Australia's big four banks have grown fat on the back of home lending. They are in the top 25 banks globally by market capitalisation. They are also among the most leveraged. From 1880 to 1940, Australia's major banks had equity and retained earnings of 15 to 25 percent of their assets, but today they have little more than 5 percent.

This week, Reserve Bank of Australia (RBA) deputy governor Philip Lowe sought to hose down fears of a housing bubble but admitted that the rapid surge in house prices was starting to slow. In a speech to the Urban Development Institute, Lowe insisted that the central bank had "a high degree of confidence that the Australian banking system is resilient to house price fluctuations."

An RBA report last year argued that wealthiest 40 percent of households hold 80 percent of the mortgage debt and most could survive a 25 percent fall in house prices. This only proves that it is the richest layers of society that have benefited from the housing boom, at the expense of working class people unable to buy homes. In any crash, however, as in the US, it would be the poorest and most vulnerable households that would lose their jobs and homes.

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