NEWSLETTER
March 2018

Introduction

Welcome to our March newsletter. This newsletter includes a property and share market update – what a month February turned out to be! And later this month we will be releasing our e-book on budgeting, so keep an eye on our website for details of that.

A look at history… 'Mr Watson, come here. I want you'

Mr Watson, come here. I want you. Such were the first words spoken – 142 years ago this month - by Alexander Graham Bell. The really interesting part: he was using his new invention, the telephone. When we stop to consider how ubiquitous telephone technology has become, this invention must stand as one of the most important in all of history.

Intriguingly, Bell's mother and later his wife were both deaf. It was through researching ways to assist them that he developed the technology that became the telephone. Necessity really was the mother of invention (and the mother of the inventor).

In the spirit of things to come, Bell himself considered the invention to be a distraction! He refused to have one in his private study. As his wife put it after his death "the telephone, of course, means intrusion by the outside world."

The more things change…

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Property Market

As we have reported in previous newsletters, property markets appear to be cooling, especially in the more populous markets of Sydney and Melbourne. As well as being a natural response to the prolonged and substantial rise in house prices over the previous several years, this cooling is also a consequence of deliberate government policy. In particular, lending restrictions placed on property investment have been just one government measure designed to reduce demand in the housing market.

In February, the Australian Bureau of Statistics released data further confirming that government policy is having some of its desired effect. Overall, there was a slight reduction in the amount of money being borrowed for housing in the month of December. This reduction was entirely due to a 0.5% fall in the amount borrowed by property investors. Owner occupiers increased the amount borrowed by 0.1%.

While these percentages aren't enormous, they do tell us that the mix of demand in the property market is changing. This is further demonstrated by the fact that first home buyers now account for approximately 18% of all loan demand. This is a substantial increase. In December 2016, 7707 first home buyers borrowed money to buy that first home. In December 2017, the number had increased to 9743. This is an increase of 26.4%. Perhaps unfortunately, the average loan size had grown by December 2017, by which time it had risen to $334,700, up from a level of $319,500 twelve months prior. This represented an increase of 4.75% in the average amount of money being borrowed by first home buyers.

The December figures confirmed an ongoing trend. For the 12 months of 2016, 88,822 first home buyers borrowed money. For the 12 months of 2017, this number grew to 104,030. This means that for the 12-month period the increase was 17.1%.

Most property commentators agree that housing affordability was becoming unmanageable and that first-time buyers were the ones suffering most. And those first home buyers had left the market in substantial numbers. Throughout 2016, first home buyers never represented more than 14% of all property borrowers. By the end of 2017, they represented 18% of the borrowing market (in terms of the number of borrowers, not the amount borrowed).

Second and subsequent home buyers and property investors can typically afford to pay more for their properties. So, when these buyers are more prominent in the market, house prices grow more quickly. For existing property owners, this might seem like good news. However, as a long-term proposition it becomes quite dangerous if younger first-time buyers choose never to enter the market. All markets benefit from large numbers of buyers and sellers. When first-time buyers put off or don't enter the market at all, they can never 'graduate' to buying a second or subsequent home and their chances of becoming property investors are remote.

So, if you are lamenting the fact that property prices are not growing as quickly as they have done in previous years, try to remind yourself that as a long-term proposition the market benefits from having more participants, not less. The fact that more first home buyers are entering the market is a good thing.

The Share Market

Many commentators have referred to the month of February as a rollercoaster ride in the sharemarket. Actually, ‘rollercoaster’ is probably the wrong metaphor. The market had one big drop, followed by a gradual and sustained rise. If you don’t mind us murdering a metaphor, the market had more in common with downhill skiing than with any rollercoaster - a quick trip down the mountain, followed by a leisurely return on the chairlift. Here is how it looks on Google (the red figure of 0.65% was the fall in the index on the

last day of the month):

The ASX 200 started the month of February on 6037 points. Trading closed on February 2 at 6120 points. By the close of trade the following Tuesday, the market dropped to 5833 points - a fall of 4.7% in just two days. The market stayed at this level until the middle of the month, from which it started to track back into positive territory. The market closed at 6017 points – a fall of just 0.3% for the month.

So… what was all the fuss about in those first two weeks? Effectively, the Australian market took its lead from the American market throughout the month. This is quite a common phenomenon. Somewhat perversely, the sharp drop at the start of the month came from the release of some *good* economic data in the United States. That’s right. Something that most commentators had pegged as good news took 5% off share prices.

What exactly was this good news? Well, for about five years employment has been growing in the United States. At first, following the lingering effects of the GFC, there was plenty of ‘spare’ labour to absorb this growth. That meant that the growth in demand for labour was matched by growth in its supply. The result? Real wages did not really change.

But supply cannot grow for ever. When supply fails to keep pace with demand, prices rise. For the 12 months to January 2018, American wages grew by 2.9%. This is the highest rate of growth since 2009, when wage growth was being smashed in the aftermath of the global financial crisis.

Real wage growth is a sign of a growing economy. The growth in the American economy has seen its Federal reserve raise interest rates five times since the start of 2016. Rising interest rates make defensive asset allocation (that is, assets other than shares, such as bonds or fixed interest deposits) more rewarding. Given a fixed amount to be invested, a rise in demand for defensive assets must mean a fall in demand for growth assets such as shares. When these rises and falls are substantial enough, the sharemarket falls overall.

This is what happened in early February. Rising interest rates saw a small amount of investor panic as some shareholders sought to get ‘out’ of their investments before prices fell further.

Happily, it did not take long for people to realise that good news is good news. That is why the market quickly began its correction to finish the month almost back where it started.

If you have been following our newsletters, you will have heard us refer time and time again to the need for investors to take a long-term approach and not become distracted by short-term noise in the market. Hopefully, this was you in February 2018.

The Legal Stuff

General Advice and Tax Warning

The above suggestions may not be suitable to you. They contain general advice which does not take into consideration any of your personal circumstances. All strategies and information provided on this website are general advice only.

We recommend you seek personal financial, legal, credit and/or taxation advice prior to acting on anything you see on this website.

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