[JUSTIN FABO, SENIOR ECONOMIST, AUSTRALIA AND NEW ZEALAND, MACQUARIE] I'm Justin Fabo, Macquarie Senior Economist that looks at Australia, New Zealand. When we look at 2020, clearly the biggest cloud hanging over the property market and the economy has been the coronavirus, and that's created this uncertainty. So we've seen some modest price falls in property. As we now look forward to 2021, things are looking brighter from both the economic and housing market perspective. Interest rates are low, we're expecting that to give a big tailwind to price growth this year and actually, even though we're expecting prices to rise solidly, the biggest risk in our view is that things actually take off a bit faster than most people expect.

HISTORICALLY INTEREST RATES HAVE PLAYED A BIG ROLE IN THE HOUSING CYCLE, HOW DO YOU THINK THAT'S GOING TO PLAY OUT OVER THE NEXT YEAR?

Interest rates have fallen quite significantly since the start of 2019, as the RBA has cut rates a number of times over that period. So now that the economy has settled down in recent months, we think these low interest rates are going to lead to some solid price growth over the next year because repayment affordability for most households has improved significantly.

WHAT ELSE IS PROVIDING SUPPORT TO HOUSING DEMAND?

There's a number of other factors providing support to housing demand, including in established markets. So number one is, we've got some pent up demand from the fact that COVID, or the coronavirus, the restrictions associated with that meant that people couldn't get out and buy a house in most parts of Australia, including in Victoria more recently. Those restrictions are now by and large gone. So we've got this pent up demand, this is going to be unleashed into housing, so we've got some catch up to do.

Secondly, we've had some restrictions on other types of spending. So there's a lot of households in Australia, not all, but a lot, who were sitting on an additional amount of cash that they wouldn't have had if these restrictions weren't on types of spending. The main one there being overseas travel, but also domestic travel. So think about how much you spend on travel each year on average, it's a lot of money that people have got in their bank accounts now, that they wouldn't have had. We think some of that is going to flow into housing demand as well.

The third factor providing support to housing markets including prices, is government support. So we've seen across the states particularly, different policies but some of those policies have been aimed at stamp duty concessions, for example, not just for new construction, but also for the purchase of established homes. And history tells us when we get that, combined with low interest rates, that puts upward pressure on housing prices, and we're seeing that already.

WITHIN THE RESIDENTIAL PROPERTY MARKET, DO YOU SEE ANY HEADWINDS FOR HOUSING?

Within the residential property market outlook we do see a couple of key headwinds to that outlook. The most obvious headwind is the fact that our international borders are shut, so we don't have people coming into the country, or not many people at the moment. So we've got a slight net outflow of people from Australia at the moment. So to the extent that persists, that is a headwind to household formation and housing demand and house prices. Now the negative end of the spectrum, is federal Treasury where they think we're going to have a net outflow of people for a couple of years. If that were to eventuate, then that would clearly be a headwind for the outlook for the housing market and demand and prices. We actually aren't as negative as them though, we think that our borders won't be shut for that period of time and we're going to get some better news next year where we start to see a trickle of people coming into the country again, not a flood, just a trickle. But while this does persist though, the demand, particularly for apartments as opposed to detached housing, is very weak and that is going to persist in the near term. We've seen rental markets are quite weak, particularly in Sydney and Melbourne and the inner areas, that is having an impact on the price side for apartments. The detached market though is taking on a life of its own, and that's a bit more driven by interest rates.

The other potential headwind I guess, is that we could have a recurrence of the virus in Australia – we've done well, but that could get worse again, we don't know. I guess in that space with a bit of luck, the better news we're getting on several potential vaccines, and there's a lot of water under the bridge here, but that gives us some confidence as well that even on the virus side that the news going through next year might be better and that might help us get the borders open a little bit sometime next year as well, which will help for housing demand.

WHAT IS THE OUTLOOK FOR HOUSE PRICE GROWTH?

When we're thinking about the outlook for housing prices, our base case or our central scenario, is that over the next couple of years we're probably going to see something like 10-12% growth at the national level.

The risk though, in our view, is that actually we might get a lot of that growth a lot faster than we expect. That's where the risk lies to our forecast. The incoming information is kind of telling us that things are picking up quite quickly in terms of housing prices, particularly detached housing prices. And this time, rather than over the last 10 years where a lot of that volatility is in Sydney and Melbourne prices and the rest of it a bit more stable, this time it's pretty much across the board. Prices are going up in Brisbane, they're going up in Adelaide quite fast, picking up fast in Perth, they've just started picking up in Sydney and Melbourne. And then the regional areas of Australia as well, they fared really well through COVID and price growth there is probably the strongest of anywhere in the country at the moment.

WHAT DO WE EXPECT IS GOING TO HAPPEN TO INTEREST RATES?

The million-dollar question is what will happen to interest rates over the period ahead. It's actually pretty easy one to answer at the moment to be honest. I mean the level of the cash rate, which the RBA sets, is effectively zero. They've also started targeting effectively some other interest rates at longer durations over the three-year rate. That's effectively zero as well. They've said that interest rates are highly unlikely to go negative in Australia for the rates that they set. They've also said, listen to us, we think for the next three years the rates they set are not going to go up, they're not going to change, so let's take it at face value. So what that means for mortgage rates is that they're probably not going to go up, whether it's a variable rate or fixed rate for the next couple of years at least. So for people buying a house, you can see these exceptionally low mortgage rates at the moment and actually have some confidence that they're going to stay around where they are, or even a little bit lower actually for fixed rates, for a couple of years. That's a key reason why we think that's going to be a key tailwind for housing price growth over that period.

So in summary, while the news on the virus could turn negative again, we look overseas and things have turned bad again on the virus, but I guess we've got some hope going into 2021 in Australia that we have done quite well with the virus, and we're hoping it stays suppressed. We've got some vaccines coming and hopefully they work quite well. So we’ve actually become increasingly positive on both the economic outlook and relatedly, the outlook for the property market going into 2021.