Property bubble bust gathers speed

By Richard Bardon

26 Feb.—The latest numbers on house prices, sales volumes, loan approvals, and aggregate mortgage lending all point in one direction: Australia's housing market is sliding ever faster towards the abyss. Nobody knows how far down the bottom might be, but credible analysis published last week suggests that the collapse of "debt-financed speculation", coupled with the withdrawal of foreign investors, could cut Sydney and Melbourne house prices in half, in a "bloodbath" not seen in Australia since the 1890s. If that happens, it will bankrupt Australia's "big four" banks (CBA, NAB, ANZ and Westpac), and probably all the second-tier lenders as well. And were that not enough, one analyst has warned that the major banks could wind up insolvent even without a housing crash, as lawsuits over widespread breaches of responsible lending laws may end with trillions of dollars in mortgages simply written off.

News.com.au finance editor Frank Chung reported 20 February that according to January data from market research firm CoreLogic, Sydney and Melbourne prices had fallen 12.3 and 8.7 per cent from their peaks in July and November 2017, "with Melbourne falling at 'the fastest rate we've ever seen'". A 24 February ABC News report notes the CoreLogic data also shows there are now 115,000 homes listed for sale across the country, more than any time since 2012. At the same time, sales are down 15 per cent nationwide, and over 20 per cent in Sydney and Melbourne. CoreLogic head of research Tim Lawless told ABC that 80 per cent of properties listed in Melbourne, and over 83 per cent of those in Sydney, have been on the market for more than 60 days. "There's not as many buyers around which simply means the rate of absorption is quite low", Lawless said, adding: "One of the primary factors is access to credit is now much harder, particularly for investors."

According to LF Economics co-founder Lindsay David, the explanation for this investor credit crunch is simple: as soon as prices started to fall, the "Ponzi finance model" that fuelled the bubble was over. "People have to understand that there are simply too many investors already tied up in the housing market and they can't go and buy more real estate unless the value of their home rises," he told Chung. "They bought a $500,000 investment property, 12 months later it's worth $600,000, with that $100,000 equity you're able to go and buy another $500,000 property. You can't do that anymore, it's in reverse." LF Economics has warned since 2015 that this system, known as "cross-collateralisation", had turned Australian real estate into a house of cards. "It's safe to say we have for quite some time been the most hated macroeconomic research company in Australia", he said, "but everything we have warned about has come to fruition."

'Bloodbath'

David's 20 February report *Let the Bloodbath Begin* lists 18 "economic headwinds" likely to send the property market, and thus banking system, over the edge. Echoing concerns raised earlier by Martin North of Digital Finance Analytics, David notes that the return to something like proper lending standards in the wake of the royal commission has seen the rate of mortgage application rejections rise tenfold to 50 per cent, while 90 per cent of those who *are* approved have had their loan size reduced. Refinancing rejections are also way up, from 5 per cent in 2017 to 40 per cent today. Thousands of households are therefore stuck in loans whose interest-only period is set to expire over the next few years, increasing their already unaffordable repayments by between 20 and 50 per cent. The lending restrictions have slowed the growth rate of *total* mortgage debt, from 6.3 per cent in December 2017 to 4.7 per cent a year later, and the *Australian* of 23 February reported that *new* lending for housing has collapsed nearly 15 per cent since mid-2018 (a number that left Westpac chief economist Bill Evans "gobsmacked"). And foreign buyers will no longer be stepping in to fill the gap: citing Foreign Investment Review Board data, *The New Daily* reported 19 February that "Foreign [housing] investment plunged by 58 per cent year-on-year from $30 billion to $13 billion" in 2018, largely as a result of tighter capital controls in China, which accounts for some 30 per cent of total foreign real estate purchases. "We think there's a chance property prices could fall by half in Sydney and Melbourne over the long run", David said. "I wouldn't be surprised by falls of at least 40 per cent. When all hell breaks loose you've only got so many buyers out there."

Martin North being interviewed by David Koch on Sunrise on the impending property bloodbath. Photo: Screenshot

The 'Khoshaba precedent'

According to *Daily Reckoning Australia* editor Nick Hubble, however, the banks have a more immediate problem. Westpac borrowers have just launched a class-action suit over the bank's illicit use of a relative poverty index called the Household Expenditure Measure (HEM) to approve loans, instead of borrowers' declared expenditures. Customers of other banks will likely follow suit. "About 55,000 home loans were written per month in Australia in 2017", Hubble wrote 23 February. "UBS estimated that in 2017, 70-80 per cent of all home loans in Australia used HEM. That gives us a potential compensation claim close to $100 billion, per year. According to the lawsuit, the practice went on for about five years. I know it went on for more than a decade. We're talking a trillion dollars … for HEM-based lawsuits alone."

"But if I'm right", Hubble continued, "[that's] nothing compared to what's coming." In 2006, Sydney couple Albert and Rose Khoshaba won a court case which saw them keep their house while their debt was written off as illegitimate, because their mortgage broker had altered their loan application form without their knowledge. Both the courts and the Financial Ombudsman have since upheld the precedent. "Borrowers who can prove *their loan application was fudged by their broker or banker* can cancel their debt but keep their home", Hubble wrote (emphasis added). As *AAS* has reported, Denise Brailey of the Banking and Finance Consumers Support Association (BFCSA) has documented in thousands upon thousands of cases that the banks have done exactly that—systematically and nationwide.

Wrote Hubble, "Think about what that means for the banking system. … If Australians start asking for their loan application paperwork, and discover it is filled with 'errors', they might be able to join the list of borrowers with a house and a cancelled mortgage. We're talking about wiping off such a large chunk of the bank's assets that it would easily wipe them out. Overnight. Insolvent. Gone."