NEWSLETTER

September 2022

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PRIVATE WEALTH MANAGEMENT

Introduction

Welcome to our September newsletter. Interest rates are at it again, although in this newsletter we discuss evidence that the Australian market is perhaps not as worried about inflation as the US is. Residential property doesn't like higher interest rates, though.

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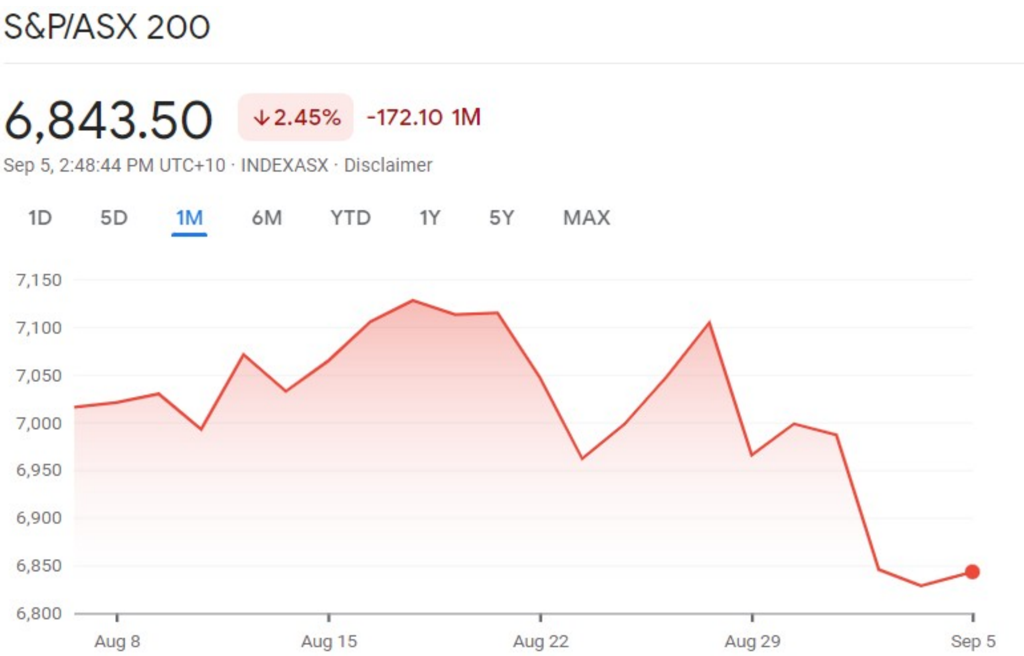
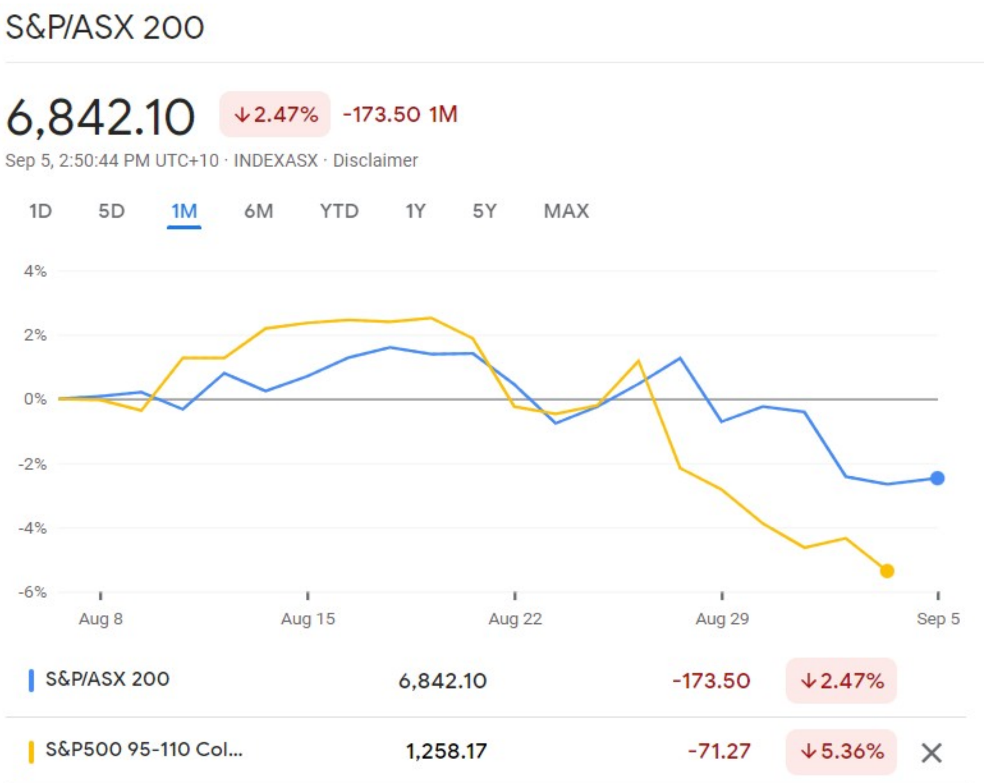
The Share Market

The share market fell on average during August. One of the leading indicators, the ASX 200, was down by almost 2.5% between August 5 and September 5, when we went to press for this newsletter. Here is how it looked thanks to Google and the ASX:



That said, our market did better than the US, whose major indicator was down more than 5.35% for the same period:



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The two markets started to diverge towards the end of August. The culprit in the US again seems to be inflation, or, more particularly, the steps that central banks take to fight inflation. On the 19th of August the chairman of the US Federal Reserve signalled to all and sundry that inflation targeting was still very much going to be pursued. Prior to his speech, the US market was actually up for the month, perhaps on the back of recent information that the rate of inflation in the US might be slowing. While it was still at very high levels, for the month of July (the most recent month for which figures are available), annualised inflation was lower than it had been in the previous two months and was back at the same level it had been in March 2022 (source: Trading Economics):

US Inflation Rates for the last Twelve Months

These annualised figures are worth understanding because a lot of people misunderstand them. And, at times when inflation is rising, this misunderstanding can lead to panic. As the graph above suggests, inflation in the US is actually calculated monthly. However, each month the figure that is calculated is the inflation rate for the previous 12 months – hence the term 'annualised.' For example, in the graph above, the figure for June 2022 is 9.1%. This means that prices as measured by the relevant index rose by 9.1% between the 1st of July 2021 and the 30th of June 2022.

The next figure, for July, gives the change between 1 August 2021 and 31 July 2022. So, it includes the month of July 2022 and removes the month of July 2021. Other than that, in comparing June and July, 11 of the 12 months in the comparison are the same. So, when there is a significant monthly change, as there was in the US between June and July 2022, that is due to the particular effect of either (i) the month that was removed from the calculation and/or (ii) the month that was included in the calculation.

To bring this back to the Australian context, our inflation data is reported quarterly, not monthly. What's more, there is a lag of almost a month from the end of each quarter to the time when the results are reported. So, the inflation data for the three months to June 30 2022 was not released until almost the end of July 2022. And the data included price rises that took place in the first weeks of April.

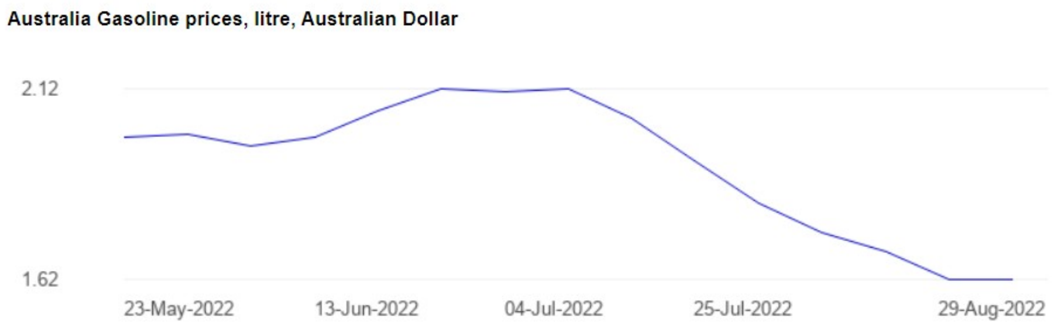
At the end of April 2022, our ABS reported inflation of 5.2%. Then, at the end of July 2022, it reported inflation of 6.1%. A lot of people are tricked into thinking that prices first rose by 5.2%

and then rose by another 6.1%. However, in truth, the 6.1% included most of the 5.2% that had already been reported in April.

This is one potential reason that our market is not reacting the way the US market is. The data in Australia indicates that prices are perhaps not rising all that fast and indeed that the rate of increase is slowing.

This kind of thinking is somewhat vindicated by the 'driving around' effect of observing petrol prices. The March annualised inflation figure of 5.2% included the really significant impact of rising transport prices. Based mostly on increased fuel costs, transport prices had risen by 13% over the previous twelve months.

But, as you may have noticed while driving around, prices have fallen back somewhat from their earlier peaks. Here is how the three months to the end of August looked, according to global petrol price monitor, globalpetrolprices.com:



Interest Rates

The above made for a particularly fascinating and important meeting this week by the RBA. As you probably know, the RBA has raised interest rates for the last four months, in a bid to take spending power away from households and thus reduce demand for goods and services.

Well, this week they made it five months in a row. Even though most people were expecting it, this may be a little surprising given that there is some indication that inflation in Australia is perhaps not rising as fast as it was.

To come back to the way we started this article, the Australian share market is clearly not as spooked by the prospect of further rate rises as the US market.

For market observers, these are interesting times indeed!

The Residential Property Market

The trend continues. Median residential property prices are falling in all but one of Australia's capital cities. The falls identified in June and July continued in August, with respected market analyst Corelogic reporting the following changes to prices in the capital city and regional markets.

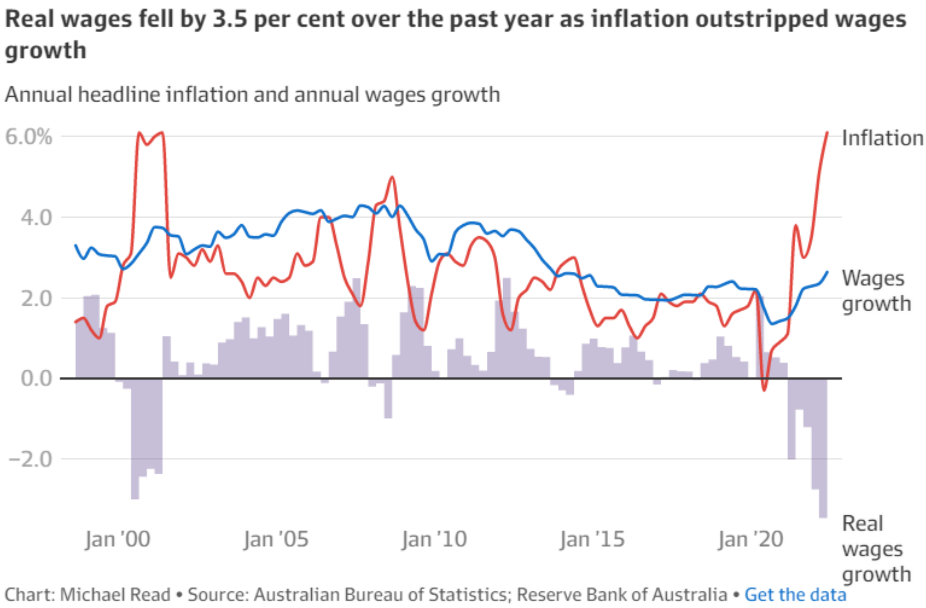
Index results as at 31 August, 2022	Change in dwelling values				
	Month	Quarter	Annual	Total return	Median value
Sydney	-2.3%	-5.9%	-2.5%	-0.7%	$1,066,493
Melbourne	-1.2%	-3.8%	-2.1%	0.8%	$782,053
Brisbane	-1.8%	-2.5%	17.5%	21.7%	$762,284
Adelaide	-0.1%	1.6%	21.8%	25.7%	$652,959
Perth	-0.2%	0.4%	4.9%	9.4%	$561,781
Hobart	-1.7%	-3.3%	5.8%	9.8%	$714,370
Darwin	0.9%	2.3%	6.3%	12.8%	$512,531
Canberra	-1.7%	-2.6%	7.8%	12.0%	$909,748
Combined capitals	**-1.6%**	**-3.8%**	**2.2%**	**4.8%**	**$808,287**
Combined regional	**-1.5%**	**-2.1%**	**13.4%**	**17.5%**	**$594,006**
National	**-1.6%**	**-3.4%**	**4.7%**	**7.5%**	**$738,321**

As you can see, only Darwin property managed to rise in August – and Darwin is actually a very small and unique property market. Prices everywhere else fell, such that the national average median price fell by 1.6%. Once again, the steepest fall was in Sydney, where prices fell by 2.3%. For a monthly fall, this is enormous. The accumulated effects of four months of falls in that market means that Sydney prices are now 2.5% below where they were this time last year. Melbourne, Australia's second largest property market, is the only other market where property owners have, on average, lost capital value over the last 12 months.

In Sydney, the fall in capital value has even offset the rent being received by landlords, such that on average those landlords 'went backwards' in the 12 months to 31 August.

The numbers below depict what is actually the fall in the 'dollar value' of the various markets. When we factor in inflation of more than 6%, it means that, in 'real terms,' the national market is down almost 10%. That is to say, for anyone whose income has 'kept up' with inflation, property is now 10% cheaper in terms of the number of hours needed to be worked to buy it.

Of course, the problem is that relatively few people's incomes have kept track with inflation. This means that real wages have also fallen, as shown in this graph from the Australian Financial Review of August 17:



The red line shows the inflation rate. The blue line shows the rate for wage growth. The grey bars show the difference between these two. Where the grey bars point down, it means that real wages are falling.

As a result, we can't yet say that housing is becoming more affordable for those who are yet to buy. While it is true that the amount actually paid to buy a house or unit is falling, the combination of higher interest rates and higher costs of living everywhere else mean that the 'average purchaser' is still not really better able to make their purchase. As a result, and especially if interest rates keep rising as they have already done this month, many commentators expect house and unit prices to keep falling. Indeed, the ANZ Bank predicts a fall of up to 18% on average across the country during 2022 and 2023.

While people who already own homes are usually happy to see prices rise and are less happy when they fall, people who are yet to buy a home are keen to see prices fall. Given that this generally means younger people wanting to buy a home to live in, most people agree that improving housing affordability is, on balance, a 'good' thing. (Sorry to anyone who bought a house in the last 24 months!)

Just how good will depend on whether personal incomes can keep track with inflation.

The Legal Stuff

General Advice 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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