MOODY'S ANALYTICS

News

MOODY'S ANALYTICS: AUSTRALIAN HOUSING MARKET REQUIRES STRESS TESTING AT STATE LEVEL

GLENN LEVINE
Associate Director / Senior Economist
Moody's Analytics
+612 9270-8159
glenn.levine@moodys.com

FRED GIBSON
Associate Economist
Moody's Analytics
+612 9270-8146
fred.gibson@moodys.com

MEDIA

HECTOR LIM
VP Communications Manager
+612 9270-8141
hector.lim@moodys.com

SYDNEY – March 18, 2014 – Moody's Analytics says that it is important to examine house prices and vulnerabilities at the state level rather than national level, when stress testing the Australian housing market.

"While Australian house prices are near fair value, they differ substantially at the state level, given the large degree of heterogeneity across state economies and housing markets," says Glenn Levine, a Moody's Analytics Associate Director and Senior Economist.

"Household investors typically invest in only one state, while institutional investors, lenders, mortgage insurers, and others connected to housing will have varying levels of exposure across states," says Levine.

"This suggests that state-specific housing policies could be beneficial, particularly when the market is overheated," adds Levine.

Levine was speaking on a just-released report titled, "Stress Testing Australia's Housing Market."

The report models the Australian housing market at the state level to study the effects of substantial but plausible external and domestic shocks.

Similar studies have examined Australian housing as a single market, ignoring the very important differences among the states.

According to the report, house prices in Victoria are slightly overvalued and particularly vulnerable to adverse shocks, while South Australia and Western Australia appear undervalued currently.

In its stress testing, Moody's Analytics subjected its house price model to a range of external and domestic shocks.

While international scenarios are designed to stress test local housing markets to a global slowdown as well as to a global recession of similar magnitude to that in 2009, domestic shocks help to isolate the sensitivity of house prices to interest rates and supply at the state level.

The model shows that Australian house prices are sensitive to a shift in global GDP and commodity prices.

This finding was common across the larger states, while the Australian Capital Territory and the Northern Territory showed a muted reaction.

Western Australia was the most sensitive, as it has a large export-facing mining sector that would turn down sharply under a global recession.

Victoria was also hit hard, reflecting its larger manufacturing component and overvalued housing market.

Interest rates are also a notable long- and short-run driver of house prices in Moody's Analytics' model, confirming that the structural fall in interest rates over the past 20 years has had a substantial impact on house prices.

House prices are affected if interest rates are lifted too quickly in the current cycle. As expected, house prices fall sharply across all states when interest rates are lifted to 18%, the highest rate on record.

Finally, prices are also sensitive to changes in the unemployment rate. This broadly reaffirms the consensus around the Australian housing market, which suggests that it has not been properly stress tested and that higher unemployment would likely trigger lower prices.

ABOUT MOODY'S ANALYTICS

Moody's Analytics helps capital markets and risk management professionals worldwide respond to an evolving marketplace with confidence. The company offers unique tools and best practices for measuring and managing risk through expertise and experience in credit analysis, economic research and financial risk management. By providing leading-edge software, advisory services, and research, including the proprietary analysis of Moody's Investors Service, Moody's Analytics integrates and customizes its offerings to address specific business challenges. Moody's Analytics is a subsidiary of Moody's Corporation (NYSE: MCO), which reported revenue of $3.0 billion in 2013, employs approximately 8,400 people worldwide and maintains a presence in 31 countries. Further information is available at www.moodysanalytics.com.

###