Boom and Bust: Are housing markets back on the rollercoaster?

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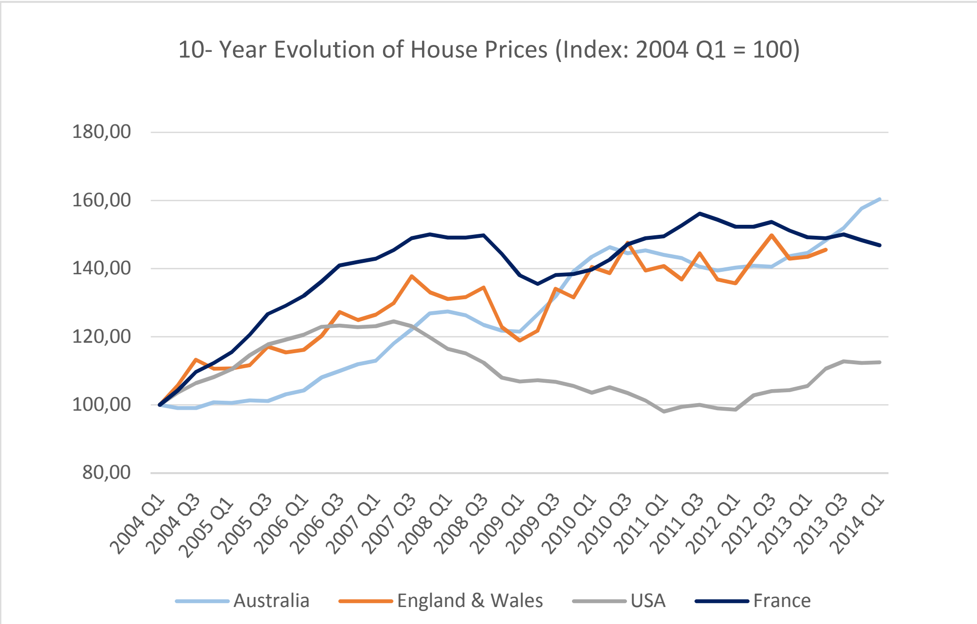
When it comes to investment, one obvious place to put money is in bricks and mortar. Despite the global financial crisis (GFC), house prices have continued to rise in some of the world's largest economies. So much so that in mid-June the IMF warned of property bubbles in Australia, Belgium, Canada, New Zealand and to a lesser extent, France[1]. In fact, looking at figures from four major countries alone, there has been a sharp rise in housing markets in all but the struggling US.



Sources: Australian Bureau of Statistics, Land Registry, FHFA, INSEE.

Boomers: United Kingdom

Also in June, the Deputy Governor of the Bank of England, Sir Jon Cunliffe, raised concerns that there was a British tendency to buy houses as soon as people felt their income was increasing, or indeed felt there was a chance it would increase. This habit, he suggested, meant that supply could not keep up with demand. His was therefore worried that, as house prices surge, household debt could be set to rise yet again[2].

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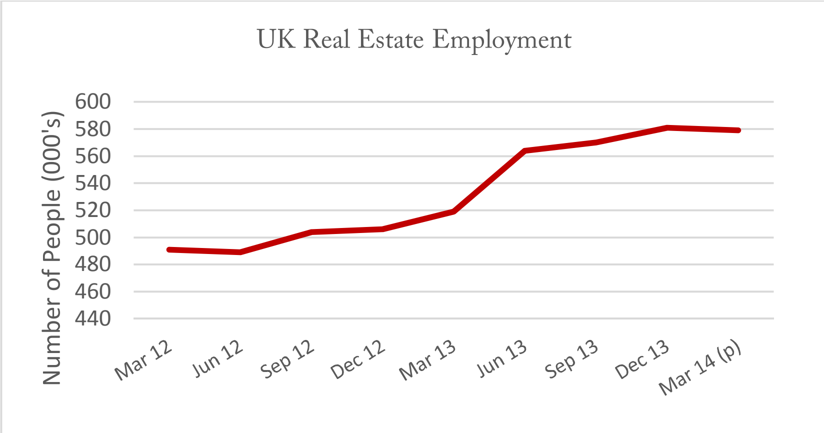
[1] http://www.lesechos.fr/monde/europe/0203561280927-le-fmi-craint-une-bulle-immobiliere-en-france-1012176.php

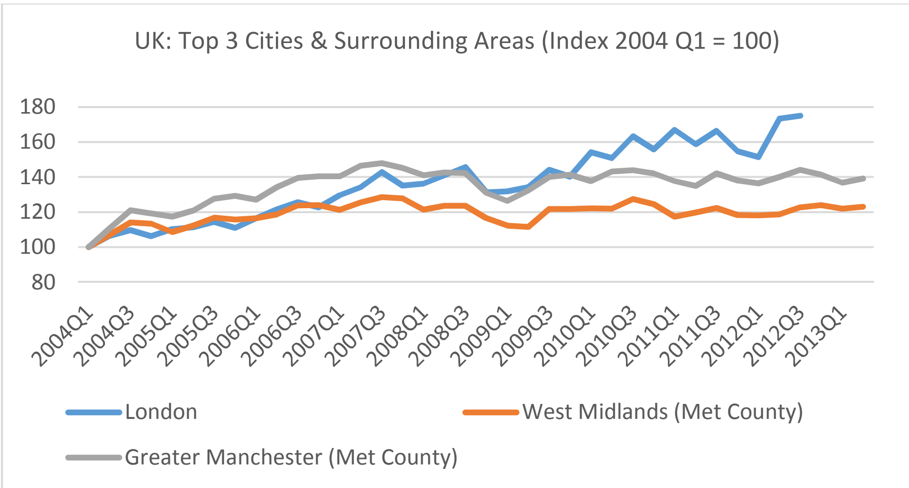
[2] http://www.telegraph.co.uk/finance/bank-of-england/10931956/Jon-Cunliffe-UK-property-obsession-threatens-to-push-up-household-debt-pile.html

One tell-tale sign in the UK is the large increase in the number of people working in the real estate sector. Between Q1 and Q2 2013 alone, there was a 9.9% rise in the number of real estate workers[3]. This was not just a one-off either, nearly 100,000 people more now work in real estate than in March two years ago.



Source: Office for National Statistics

Whilst it's true that, as reported by the press[4], prices in London have increased significantly, the capital cannot take the entire blame for this trend. As the chart demonstrates, the two largest urban conglomerations outside London have also seen important rises.



Source: Land Registry

[3] http://www.ft.com/intl/cms/s/0/866e87c0-1af0-11e3-a605-00144feab7de.html#axzz36Nx2bapT

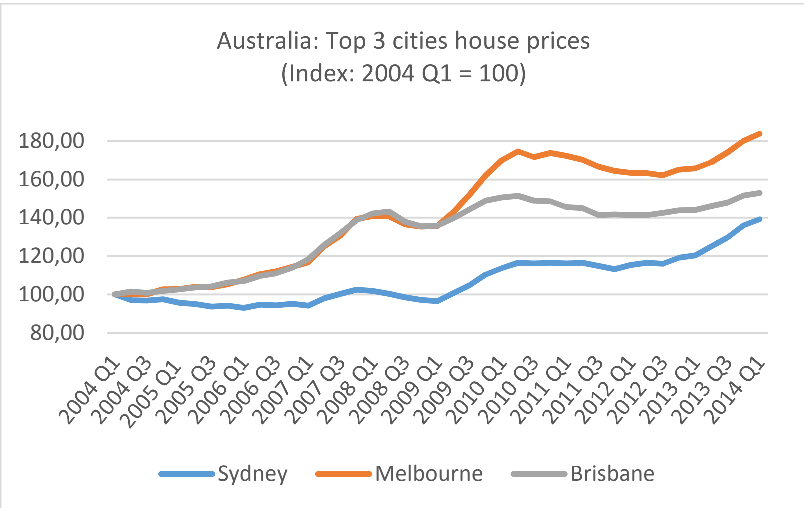
[4] http://www.bloomberg.com/news/2014-07-15/u-k-house-prices-rise-as-london-surge-hits-record-ons-says.html

For example, whilst the West Midlands (i.e. Birmingham) market seems to be steadier than London and Manchester, it has experienced a 20% price increase over the last ten years. This is by no means remarkable but the rise in the Manchester are is quite considerable.

Boomers: Australia

Australia has been experiencing a house-price bubble for several years. Key economists, such as Steve Keen[5], have long since been sounding the warning bells that a burst will come; and when it does it will be devastating. Over two years ago MBMG co-founder Paul Gambles suggested to CNBC that Australia's huge credit bubble, would at some point burst – possibly pricked by poor results in the Chinese economy, making the Australian dollar and perhaps the banks and property market drop in price[6]. That hasn't happened yet, as Chinese economic results have so far stood up over the last couple of years, but Australia's heavy reliance on the Asian giant means the Sword of Damocles still hangs above its markets.

Looking solely at the property market, since the dip in 2008, Sydney area prices have increased by over 40%. However, Brisbane and Melbourne continued augmenting without experiencing anything close to a dip: over the last ten years the former's house prices have increased by almost 53%; the latter's by a huge 84%.

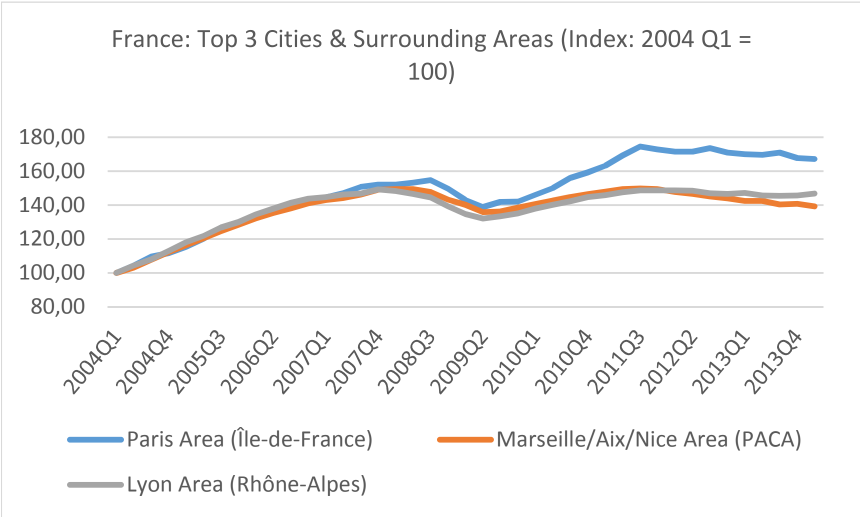


Source : ABS

Boomers: France

[5] http://www.debtdeflation.com/blogs/2014/04/08/a-sudden-conversion-of-property-bubble-doubts/
[6] http://www.cnbc.com/id/47290031#.

Given its culture of low levels of credit and the predominance of fixed-rate mortgages, it would be natural to assume that house prices in the Republic evolve slowly. Whilst there was no boom and bust scenario *per se* before, during and after the GFC, prices are comparatively very high compared with a decade ago.

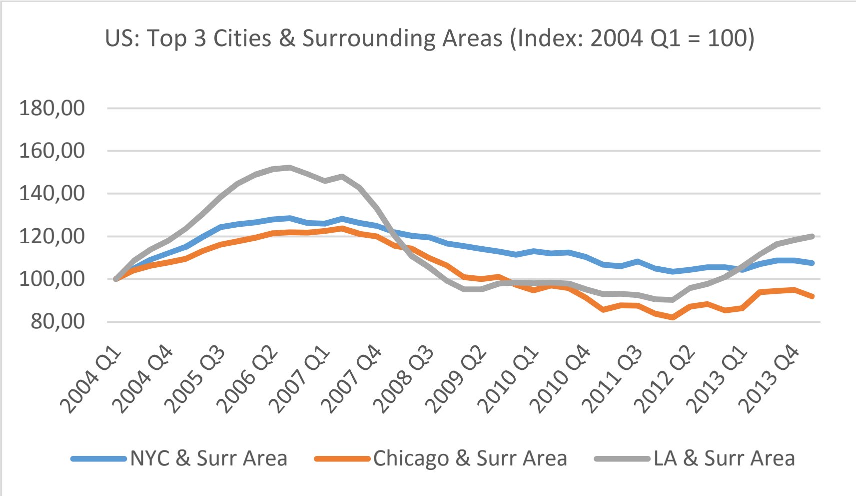


Source: INSEE

Unsurprisingly for such a centralised country, prices in the Paris area have risen at a higher rate than their equivalents in Lyon and Marseille. Whilst property values in France's second and third–largest populated areas have risen steadily in the last decade, they have both seen around a 40% rise – a steady return on investment.

Busters: USA

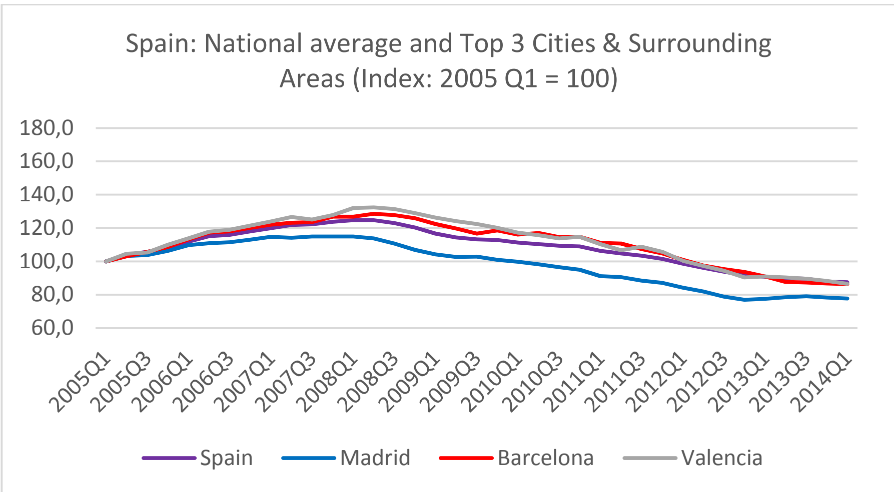
One of the main triggers of the GFC was, of course, the bursting of the US property bubble. The Federal Reserve's reaction to this was quantitative easing (QE) - adding huge sums to the money supply in an attempt to boost markets, such as property, by making borrowing more affordable. It is clear from a real estate point of view that QE isn't working. Whilst prices in the Los Angeles area have grown a respectable 10% in the last ten years, the New York area has gained just 7.5% and Chicago has actually dropped 8% in price.



Source: FHFA

Busters: Spain

Whilst the US housing market is stagnant at best, after the first quarter of 2014, the Spanish national average price was an eighth lower than ten years previously. Breaking this down into the three most populated areas shows a similar story for Barcelona and Valencia; Madrid faired even worse with prices over 20% below their level a decade ago.



Source: INE

Spain's housing bubble had been going on for ten years when prices started to fall in 2007-2008. There had previously been a boom between 1985 and 1990. Whilst this surge levelled out in the 1990's prices were still rising overall. The current situation is totally different, however: the property bubble began to burst a few months before its American equivalent and is still deflating. Analysts may suggest this is a buyer's market; but with prices so low for six years, it raises the question as to what extent property will regain value and thus bring any reasonable return on investment.

The Future

Spain is very much the doomsday scenario, of course, and local policy is constrained by Spain being in the Eurozone – meaning the policy-making central bank is based in Frankfurt and has 17 other countries to concern itself with too.

Nevertheless, it still provides a relevant example of how a housing market can burst uncontrollably. The central banks in Australia, the UK and elsewhere should take heed. So too should investors, when contemplating putting money into bricks and mortar.

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