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A new kind of stress

If ever there was confirmation for the adage "whatever can go wrong, will go wrong", last year was it for the inner suburbs. It started with an affordability crisis, rises in official and commercial interest rates, and a market that had an abundant supply in a period of slackening demand.

Then came the global financial crises, pushing the sharemarket into meltdown, sparking corporate collapses, job losses and edging the economy steadily towards a recession.

Every property boom must eventually fizzle, but the great tragedy of 2008 - and the reason it got so bad - was the unfortunate coincidence that the correction came in the midst of a series of near unremitting financial disasters.

Few experienced the fallout of the global financial risks as keenly or as quickly as the high-income, investment-oriented and debt-dependent constituency that calls - or wants to call - the inner suburbs home.

"People who were counting on income from bonuses, incentives and share returns to help fund their properties found it just wasn't there any more," says BIS Shrapnel analyst Angie Zigomanis. "It created a new kind of stress for the market, something we haven't seen since the late 1980s and early 1990s."

Confidence, in turn, took a beating and prospective buyers retreated from the market en masse. Demand couldn't keep pace with supply, sales levels plummeted and prices quickly followed.

Robert Papaleo, director strategic research at Charter Keck Cramer, says the problems of 2008 were worsened by the intense demand and record-breaking growth of 2007. "The market's peak was based on unrealistic, unsustainable, just unmatchable prices that made the fall that followed all the worse," he says.

Those who had to sell - at a time when clearance rates were in steady decline - faced the choice of dropping their asking prices or risk seeing a property sit on the market. Even drastic cuts to interest rates starting in September proved too little, too late.

By the close of 2008 real damage had been done, according to the Real Estate Institute of Victoria figures. The inner-suburban median house price - which had grown nearly 31 per cent to $726,000 in the 12 months to December 2007 - fell 5.17 per cent to $688,500 in the year to December 2008.

Rather than dominating - and underpinning - the metropolitan property market, the inner suburbs helped drag the metropolitan median house price down by 9.7 per cent.

The inner ring now held five of the top 10 worst performing suburbs in the city, with house prices falling 28 per cent in Kew (second), 22.3 per cent in Balwyn (third), 18 per cent in Richmond (sixth), and 13.9 per cent in Northcote (ninth).*

The drops were sharp enough to see Hawthorn East and Balwyn lose their spots in the million-dollar suburb club. Even prestigious Toorak took a price hit of 8.5 per cent.

Hawthorn was the only inner suburb to gain real ground in those 12 months to December 2008, posting a growth rate of 6.2 per cent. This dismal price performance is mitigated when looking a the REIV's median price figures for the 2008 calendar year, which exclude the peak quarter of December 2007.

In this data set, the inner-suburban median house price grew by 4 per cent and the median apartment price by 4.4 per cent. By comparison, house prices grew 5.6 per cent and 5.2 per cent in the middle and outer suburbs, and apartment prices grew 2.6 per cent and 8.7 per cent in the middle and outer suburbs.

Although far better than the December 2007 to December 2008 results, its still a relatively weak performance for the inner suburbs in historical terms.

Only three inner suburbs made it into the list of top 20 performers for the calendar year 2008, with St Kilda experiencing price growth of 19.3 per cent (eighth), Albert Park 18.7 per cent (11th), and Maidstone with 18.5 per cent (12th).

“But when considering the extent of a downturn, you also have to look at the level of activity, which can be just as important as prices,” says Enzo Raimondo, chief executive of the REIV.

The number of inner suburban property sales in 2008 was 45.37 per cent lower than the previous year, according to REIV data. The inner suburbs clocked up just 29.44 per cent of all sales across the metro area last year, compared to more than 40 per cent in 2007.

Grim, for sure, but figures alone can’t convey the sense of doom and gloom that gripped the market at that time. Auctions of quality properties that once would have attracted multiple bidders were instead often characterised by a deafening silence when no one raised their hands.

Properties passing in after little or no bidding - sometimes following multiple vendor bids - became endemic. By November only about half of properties up for auction were resulting in sales, many of which were done through pre or post-auction negotiations.

That’s not to say some properties weren’t selling well - only that strong, competitive auction sales became notable because they were unusual in a time of overweening caution.

“There was a period where it was absolutely brutal out there (in the auction market), and just when you thought it couldn’t get worse, it did,” says buyers’ advocate Chris Koren, of Morrell & Koren. “Nowhere was this more clear than at the top end, with properties passing in after zero bidding, vendors getting offers that were way, way below what they wanted, and many (properties) just sitting there unsold without the prospect of being sold.”

What compounded the damage for values was an influx of properties in the $1 million-plus range as sharemarket losses and tightening lending conditions put the squeeze on premium offerings.

Australian Property Monitors reports that the number of properties put up for sale at prices of more than $1 million increased more than 114 per cent last year, from 3066 in 2007 to 6581 in 2008. Properties in this price band represented 5.19 per cent of all stock on the market across the metro area in 2008 compared to 3.22 per cent in 2007.

Falling sales and prices created a crisis in confidence that, in turn, has seen potential inner-suburban vendors withhold properties from the market at the start of this year. Auction supply has been at or near historic lows in the months to mid-March, a trend that is likely to continue.

“Low interest rates are the vendors’ saving grace at the moment,” says John Bongiorno, director of estate agency Marshall White. “It’s why we haven’t seen a massive influx of selling this year.”

The inner-suburban auction market has seen an average clearance rate of 73 per cent to mid-March, well above the low point of the mid-50s it hit late last year.

“We’ve recently seen enough activity to believe that demand is now back above supply, and where stock levels are at the moment, I think price levels can be maintained,” Mr Bongiorno says.

But analyst caution that any stabilisation in prices and continued moderation in supply depends on the Australian economy avoiding a repeat of the instability and spreading financial losses seen last year.

* This list includes only suburbs that had more than 30 sales in December quarter of 2008.