Your window into the future of the construction industry

AUSTRALIAN CONSTRUCTION INSIGHTS
Research powered by HIA Economics

Construction Brief

20 August 2018

Labour market showing signs of life

Last week the ABS released two key updates on the labour market, with both providing a glimmer of hope that growth in real incomes – what has been the Achilles heel of domestic economy for the past six years or so – might not be far off.

The unemployment rate dipped to 5.3 per cent in July, a level not seen since November 2012. This result was due to a fall in the participation rate, which more than offset a loss of 3,900 jobs during the month. The job shedding was concentrated in part time jobs, while encouragingly, a very respectable 19,300 full time jobs were created during the month.

Changes in the labour market tend to be a slow grind. After hitting a post-GFC high of 6.4 per cent in October 2014, it has taken nearly four years for the rate to grind down to where we are now, just more 1 percentage point lower.

The glimmer of hope here is that wages growth could finally be picking up. Since reaching a post-GFC peak rate of annual growth in December 2010 (of 3.9 per cent), that pace tumbled over the following years, dropping to just 1.9 per cent in the September 2016 quarter – once you account for general inflation, wages were actually shrinking.

So is this the beginning of a comeback? At best a very slow one. International, rather than our own historical experience is likely to be instructive. Previous occasions in the last two decades when Australia's unemployment was down at 5.3 per are back in late 2012, early 2010 and mid-2004. Wages growth during each of these occasions was around 3 per cent per annum. So current wages growth obviously way below historical experience.

The current experience of other advanced economies internationally is that despite record-low unemployment rates (the UK's the unemployment rate is the lowest since 1975, while in the US the unemployment rate reached an 18-year low in May this year), real wages are barely growing. There are likely to be structural forces at play keeping a lid on wages growth internationally and here in Australia.

In particular it is clear that the 'natural' rate of unemployment is lower than what has previously been the case of around 5 per cent. So we need to see these latest improvements in our unemployment rate to gather momentum and fall further to help spur on an acceleration in wages growth and reverse a pernicious trend that has been in train for around five years now.

RBA rewrites history

On Friday 17 August, the Governor of the RBA, Philip Lowe, gave an address to the House of Representatives Standing Committee on Economics.

In this speech he has retold the story of housing finance, but with a very different interpretation from ours.

Over the past two years governments and regulators have intervened in the housing market (through APRA, punitive rates of stamp duty, additional fees) thereby restricted access to finance for investors. This was an explicit intervention in the market by federal and state governments that was clearly targeted at investors and has clearly impeded investor activity in the market.

Investors are existing the market because of government restrictions.

It was surprising therefore, to hear the Governor say: 'The slowing in the housing market has reduced the demand for credit by investors.'

This is a concern as he went on to say: 'There has also been some tightening in the supply of credit, partly in response to the Royal Commission, although the main story is one of reduced demand.' We can only presume that he is concluding that it is a fall demand for housing is causing a slowing of the supply of credit.

It is our opinion the causation is the other way around. It is the constraints on investors that is slowing investor activity.

The key to the mis-representation of facts is the following statement: "The average variable interest rate paid by borrowers has declined further over the past six months, to be about 10 basis points lower than a year ago. You would not have expected to have seen this if supply constraints were the main reason for slower credit growth.

In this statement the Governor is saying that the slowing in credit growth is not caused by constraints on the availability of finance but on a slowing in demand for new housing, caused by a slow-down in demand. There may be an element to truth to this, but it is not the main cause.

A flight to quality

In our opinion this conclusion is wrong.

The constraints imposed on investor lending through APRA have seen banks respond, not by raising rates though this has occurred, but by tightening their collateral requirements for new borrowers particularly higher risk borrowers, therefore limiting access to finance.

It could have been expected that the banks would respond to the APRA restrictions by imposing higher interest rates on higher risk investors. Instead, they are simply not lending to these higher risk investors due to the higher collateral requirements they have imposed.

Banks are responding to the constraints imposed by government, not by raising rates, but by limiting access to finance through other lending practices.

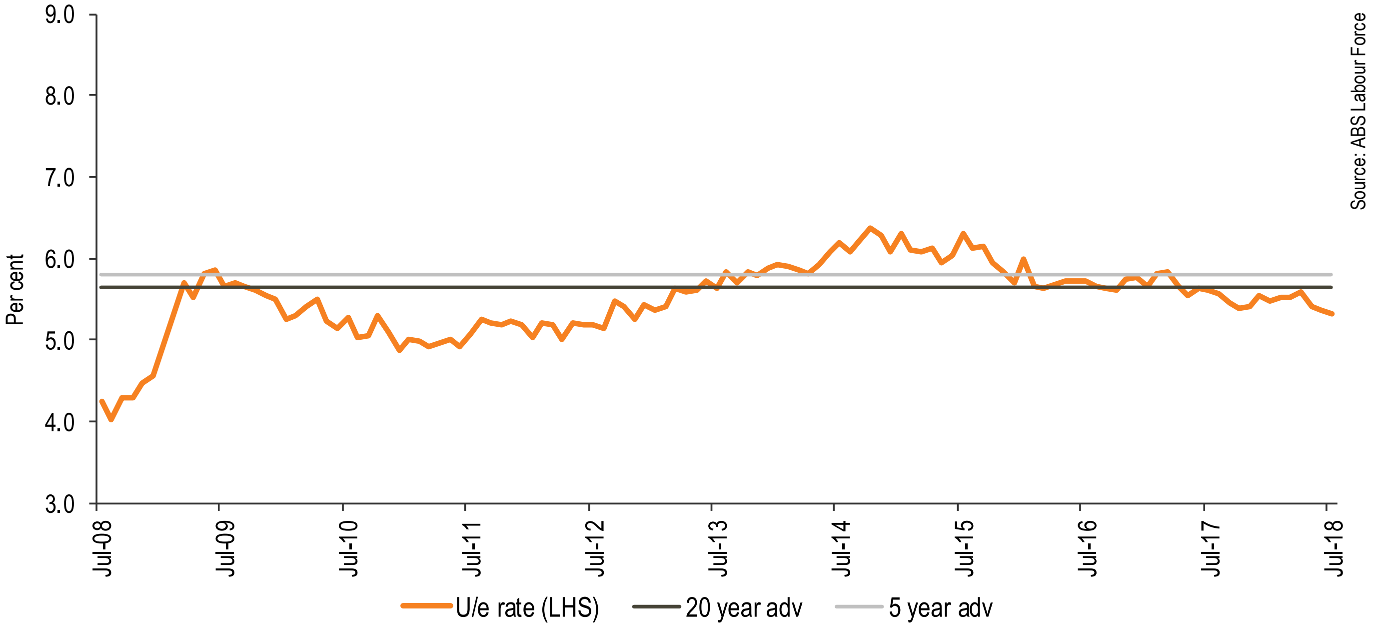
This is a flight to quality as banks limit their lending to quality investors only.

This response is in part due to the APRA restrictions, but also more broadly to a change in market conditions, where the record volume of new housing is resulting in a decline in house prices in Sydney and Melbourne.

This is an obvious and perhaps necessary response from the banks given the circumstances they face.

The concern is, if the RBA believes that there is not an access to finance problem, then we may see the repeal of the APRA restrictions delayed well beyond their useful expiration date.

Australia's Unemployment Rate



The fortnight ahead – key dates and releases (AEST)

Wednesday 22 August

ABS Construction Work Done, Preliminary, June 2018, 11.30am

Wednesday 29 August

HIA New Home Sales, July 2018, 11.00am

Thursday 30 August

ABS Building Approvals, July 2018, 11.30am

ABS Private New Capital Expenditure and Expected Expenditure, June 2018

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