MEDIA RELEASE

NAB Residential Property Survey - Q2 2017

Australian housing market sentiment (measured by NAB's Residential Property Index) fell noticeably in the June quarter after climbing to a 3-year high in March.

The NAB Residential Property Index dropped 17 points to +14 and currently sits at its lowest level since mid-2016.

Sentiment fell in all states led by SA/NT. Sentiment was also noticeably lower in NSW and Victoria, but they were still the most upbeat states.

But more modest falls in QLD and WA saw the gap between the best and worst states narrow.

Overall confidence levels also turned down in the June quarter, with the Index expected to rise to just +23 in the next year (down from +38) and to +35 in two years' time (from +40).

According to NAB Group Chief Economist Alan Oster, "Falling confidence reflects weaker expectations for both house prices and rents."

Average survey house price expectations fell to 0.6% in the next year (from 1.8%) and 1.0% in two years' time (from 2.0%).

"Property experts lowered their expectations in all states, except WA, with the biggest cut backs in Victoria and to a lesser extent in Queensland and NSW" said Mr Oster.

Queensland and NSW are expected to lead the country for house price growth in the next 12 months.

But WA is expected to re-emerge as the best state after Queensland in 2 years' time, with Victoria the weakest.

"Rents are also expected to slow, but tipped to outpace house price growth. This suggests that yields may start widening after a long period of compression, especially in Victoria and NSW" said Mr Oster.

The survey results indicate that while first home buyers were more active in both new and established property markets in the June quarter, local investors retreated from the market.

"Clearly, tougher measures on banks announced by regulators to rein in investor lending are being felt in this segment of the market" said Mr Oster.

In contrast, the share of foreign buyers in new property markets increased to 11.6% (10.8% in Q1), driven largely by Victoria where they accounted for around 1 in 5 (20.8%) new property sales.

"Foreign buyers continued to play a role in Australian housing markets in the June quarter despite China's crackdown on capital outflows into overseas property and a raft of new restrictions and taxes on foreign ownership introduced in the 2017/18 federal budget" said Mr Oster,

NAB's forecasts on residential prices

After multiple years of very strong growth, Australia's housing market appears to be entering a cooling phase - although evidence points to an orderly adjustment rather than a sharp deterioration.

According to Mr Oster, "Our expectations around subdued wages growth remain suggesting affordability will be a major constraint on the market, especially if credit conditions continue to tighten. This along with record levels of housing construction activity (mainly apartments) and moves to limit foreign demand for housing will likely limit the potential for future price gains."

"However there are still a number of positive elements supporting the market, which will likely see an orderly adjustment rather than a sharp correction. Interest rates are still quite low, despite recent increases, and pent-up demand for housing remains quite large in some markets, especially Sydney and Melbourne" added Mr Oster.

That said, much softer market sentiment in the NAB Survey and weaker than expected price outcomes in recent months has prompted us to revise down our 2017 forecasts.

House prices are forecast to rise 5% (previously 7.2%) in 2017 unit prices 3% (was 6.8%). Modest growth of 4.3% for detached houses and -0.3% for units is forecast for 2018.

By capital city, house price growth is forecast to remain strongest along the eastern seaboard in 2017. Sydney and Melbourne will both see solid, albeit slower, growth in prices. Brisbane, Adelaide and Hobart will also cool, while Perth will remain very weak. These trends will broadly continue into 2018, with growth in Sydney and Melbourne returning to more sustainable levels.

The under-performance seen in the apartment market is also set to continue, reflecting the heightened supply concerns and uncertainty around the future of foreign demand. Sydney and Hobart units are expected to do relatively well in 2017, but all other markets are expected to decline. Most cities will be fairly flat in 2018, while Melbourne and Brisbane will likely see additional declines.

About 260 property professionals participated in the Q2 2017 survey.

NAB HEDONIC HOUSE PRICE FORECASTS (%)

	2014	2015	2016	2017f	2018f
Sydney	13.4	11.5	16.7	6.7	4.9
Melbourne	8.4	11.7	15.1	7.5	5.5
Brisbane	5.2	4.3	4.0	1.3	1.9
Adelaide	4.5	-0.3	4.5	2.2	1.7
Perth	2.1	-3.8	-4.4	-2.5	0.7
Hobart	3.3	-1.6	11.7	4.7	1.7
Cap City	**8.4**	**7.8**	**11.6**	**5.0**	**4.3**

NAB HEDONIC UNIT PRICE FORECASTS (%)

	2014	2015	2016	2017f	2018f
Sydney	8.3	11.3	9.6	6.4	0.5
Melbourne	1.1	6.9	1.7	-2.6	-2.4
Brisbane	1.2	1.8	-0.2	-2.2	-1.8
Adelaide	2.5	1.4	1.1	-1.9	0.5
Perth	1.9	-3.5	-3.2	-3.6	0.7
Hobart	5.9	8.6	6.7	4.0	0.6
Cap City	**5.1**	**7.9**	**5.9**	**3.0**	**-0.3**

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NAB RESIDENTIAL PROPERTY SURVEY Q2-2017

HOUSING MARKET SENTIMENT WEAKENS IN ALL STATES, BUT GAP BETWEEN BEST AND WORST NARROWS. CONFIDENCE AND PRICE EXPECTATIONS ALSO ADJUSTED DOWN IN ALL STATES (BAR WA).

NAB Behavioural & Industry Economics

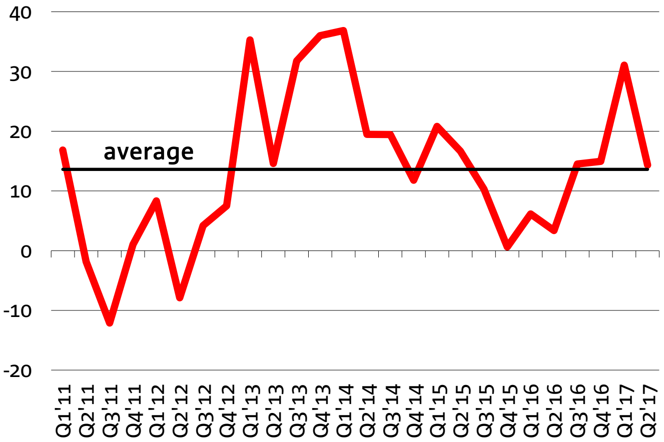
Embargoed until: 11.30 am Thursday 13 July 2017

Housing market sentiment (measured by **NAB's Residential Property Index**) softened noticeably in Q2. Sentiment fell in all states (led by SA/NT, VIC and NSW), but the gap between the best (VIC & NSW) and worst (WA) narrowed. Confidence also moderated as prospects for capital and rental growth slowed. Property experts are anticipating slower price growth in all states in the next 1-2 years (except WA), but particularly in VIC and to a lesser extent QLD and NSW. WA is tipped to re-emerge as the best state for capital growth after QLD in 2 years' time. Rents are also set to slow, but will outpace price growth suggesting yields may start widening after a long period of compression, especially in VIC and NSW. FHBs were more active in both new and established property markets in Q2, but local investors retreated as regulators implemented more measures on banks to rein in investor lending. Despite China's crackdown on capital outflows into overseas property and a raft of new restrictions/taxes on foreign ownership introduced in the 2017/18 federal budget, the share of foreign buyers in new property markets increased to 11.6% (10.8% in Q1), driven largely by VIC where they accounted for 1 in 5 (20.8%) new property sales. NAB Economics has revised down its 2017 housing forecasts based on much softer market sentiment in the NAB Survey and weaker than expected price outcomes in recent months. More modest price growth is also forecast in 2018 (see p.10).

VIEW FROM PROPERTY EXPERTS

Market sentiment softer in all states. Confidence also falls on expectations for slower house price growth and rents (except in WA).

NAB RESIDENTIAL PROPERTY INDEX



RESIDENTIAL PROPERTY INDEX BY STATE

	Q1'17	Q2'17	Next 1yr	Next 2yrs
VIC	58	36	44	53
NSW	58	36	38	38
QLD	13	12	22	36
SA/NT	42	-6	-6	17
WA	-43	-46	-24	19
AUST	**31**	**14**	**23**	**35**

VIEW FROM NAB ECONOMICS

Softer market sentiment and weaker price outcomes in recent months has led NAB to revise down its price forecasts for 2017 and 2018.

NAB HEDONIC HOUSE PRICE FORECASTS (%)*

	2014	2015	2016	2017f	2018f
Sydney	13.4	11.5	16.7	6.7	4.9
Melbourne	8.4	11.7	15.1	7.5	5.5
Brisbane	5.2	4.3	4.0	1.3	1.9
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NAB HEDONIC UNIT PRICE FORECASTS (%)*

	2014	2015	2016	2017f	2018f
Sydney	8.3	11.3	9.6	6.4	0.5
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Brisbane	1.2	1.8	-0.2	-2.2	-1.8
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Perth	1.9	-3.5	-3.2	-3.6	0.7
Hobart	5.9	8.6	6.7	4.0	0.6
Cap City Avg	**5.1**	**7.9**	**5.9**	**3.0**	**-0.3**

SOURCE: CoreLogic, NAB Economics

Date **July 2017** | **Author: NAB Behavioural & Industry Economics**

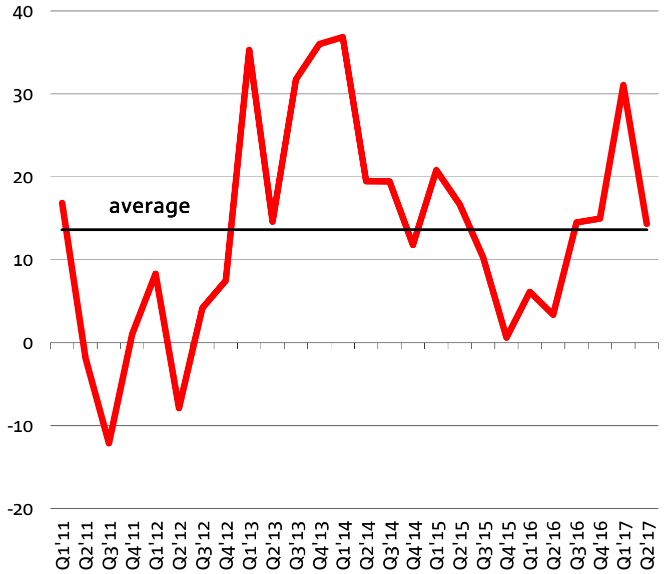
MARKET SENTIMENT EASES

NAB's Residential Property Index - based on survey expectations for capital growth and rents - softened noticeably in Q2'17. The Index fell 17 points to +14, driven by lower expectations for both capital growth and rents, and now sits at its lowest point since mid-2016.

Housing market sentiment fell in all states. VIC (down 22 to +36) and NSW (also down 22 to +36) continue to lead the way in Q2'17 and are still tracking above average. SA/NT saw the biggest fall (down 47 to -6), with modest declines in QLD (down 1 to +12) and WA (down 3 to -46). Consequently, the gap between the best and worst states has narrowed (see chart on the right).

NAB RESIDENTIAL PROPERTY INDEX

Overall housing market sentiment has fallen back to long-term average levels ...



RESIDENTIAL PROPERTY INDEX BY STATE

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VIC	58	36	44	53
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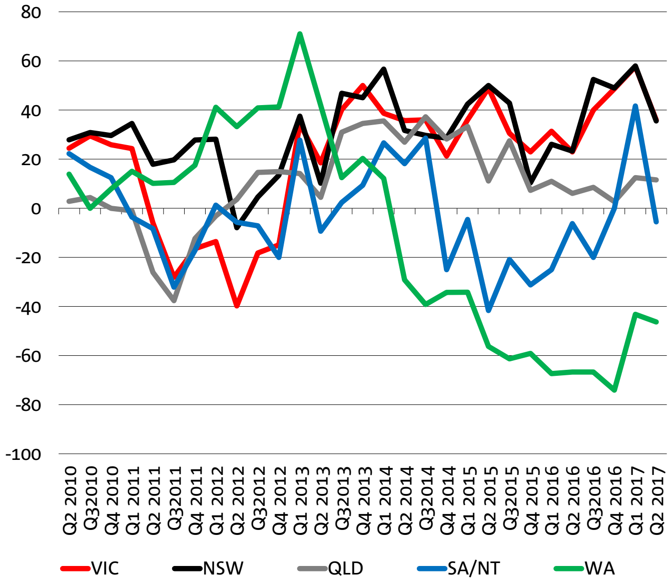
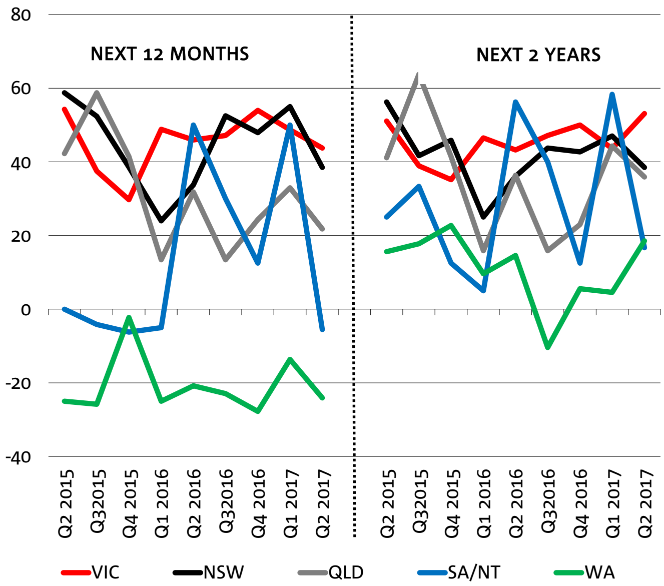
WA	-43	-46	-24	19
AUST	**31**	**14**	**23**	**35**

RESIDENTIAL PROPERTY INDEX: STATE

But the gap between the strongest and weakest states is narrowing...



Property professionals less confident about the future, except in VIC and WA...



Overall confidence levels have also softened. NAB's Residential Property Index is now expected to rise to just +38 in the next year (+23 in the last survey) and to +35 in 2 years' time (+40 in Q1).

The chart above shows confidence levels in the next 12 months are lower in all states. Property professionals in VIC (down 5 to +44) and NSW (down 17 to +38) are however still the most optimistic. Confidence levels fell deeper into negative territory in WA (down 10 to -24) and were also negative in SA/NT (down 56 to -6).

Confidence levels in 2 years' time have also weakened in all states except VIC (up 9 to +53) and WA (up 14 to +19), where more property professionals in both states are expecting to see positive capital and rental growth - albeit moderating in the case of VIC.

SURVEY HOUSE PRICE EXPECTATIONS

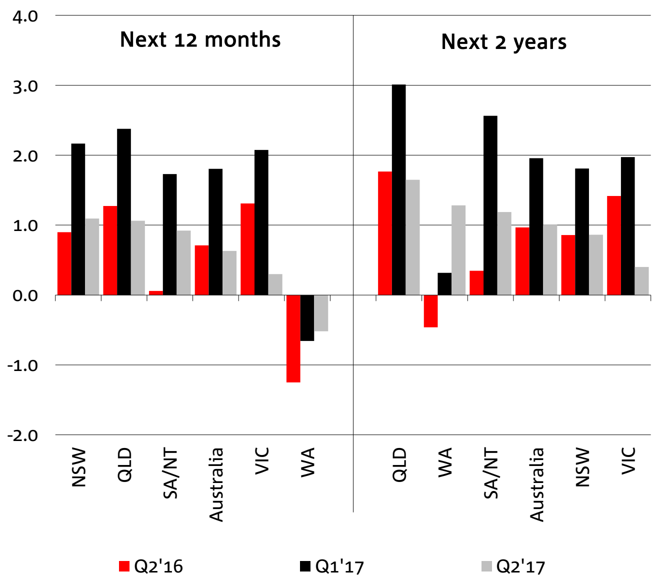
Average survey expectations for national house prices over the next 12 months have softened, with prices now expected to grow by just 0.6% (1.8% in the previous survey).

Property experts on average are tipping weaker house price growth in all states in the next 12 months, except in WA where the expectation is for a modest slowing in the rate of decline to -0.5% (-0.7% in the last survey.

Property professionals are now pointing a significant slowdown in house price growth over the next year in VIC (0.3% vs. 2.1% previously) and to a lesser extent in NSW (1.1% vs., 2.2%). A slowdown in house price growth is also being predicted in QLD (1.1% vs. 2.4%) and SA/NT (0.9% vs. 1.7%), but from a small sample size.

SURVEY HOUSE PRICE FORECASTS

Expectations lowered in all states in the next 1-2 years (except WA), with outlook weakest in VIC & NSW in 2 years' time...



Longer-term prospects have also softened, with average survey expectations now pointing to house price growth of just 1.0% in 2 years' time (2.0% in the previous survey).

Property professional in QLD remain the most bullish, although the average survey forecast has fallen to 1.6% (3.0% in the last survey). In WA, where the local housing market has under-performed relative to Eastern seaboard states following the mining investment slow down, house prices are expected to rebound and grow 1.3% (0.3% in the last survey) - making it the second best state for price growth.

In SA/NT, expectations were scaled back but are still relatively solid (1.2% vs. 2.6%). Property experts in NSW are also somewhat more pessimistic (0.9% vs. 1.8%).

Property experts in VIC are expecting the smallest capital growth of all states (0.4% vs. 2.0% in the last survey), suggesting a period of very moderate but steady house price growth in the next 1-2 years.

SURVEY RENTAL EXPECTATIONS

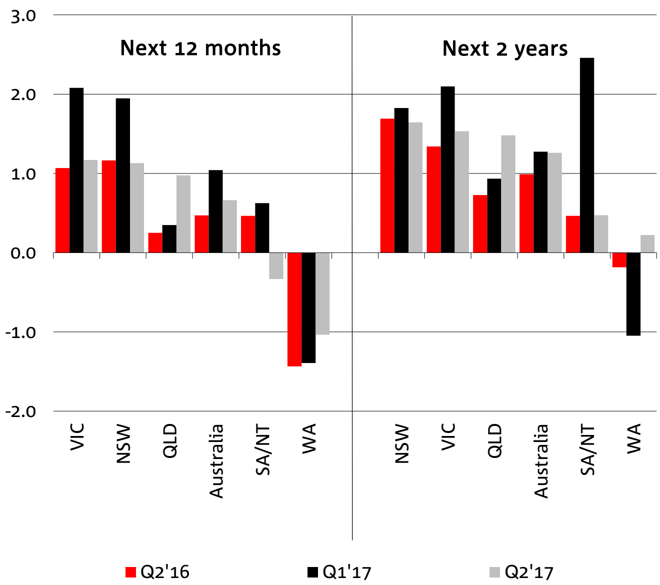
The average national survey outlook for rental growth in the next year was pared back to 0.7% (from a near 3-year high 1.0% in Q1'17). But with rental growth exceeding capital growth, yields may start to widen after a long period of compression, particularly in VIC and NSW.

Property experts on average are tipping slower rental growth in VIC (1.2% vs. 2.1%) and NSW (1.1% vs. 1.9%) over the next year, but these two markets are still expected to provide the best income returns in the next 12 months.

Rental growth expectations were also pared back in SA/NT (-0.3% vs. 0.6%), but have improved in WA, albeit they remain negative (-1.0% vs. -1.4%) and in QLD (1.0% vs. 0.3%).

SURVEY RENTAL GROWTH FORECASTS

VIC & NSW the best states for income growth in the next 1-2 years; WA & SA/NT the worst...



On average, national rental growth is expected to accelerate to 1.3% in 2 years' time (unchanged from the last survey). However, the drivers of growth have changed.

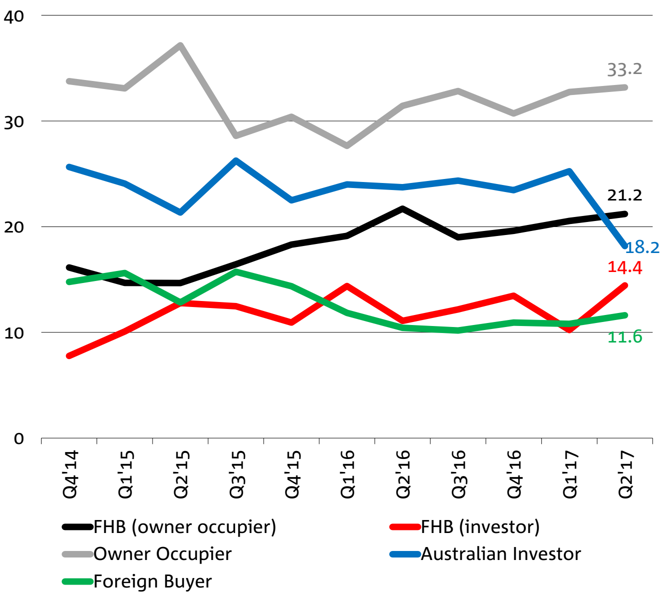
Property experts are still tipping NSW and VIC to provide the best income returns over this period, but expectations have been lowered from 1.8% to 1.6% in NSW and from 2.1% to 1.5% in VIC. Rental expectations were also weaker in SA/NT (0.5% vs. 2.5%) but from a small base.

In contrast, the outlook for average rental growth in 2 years' time was revised up noticeably in QLD (from 0.9% to 1.5%) and in WA (from -1.0% to 0.2%).

NEW DEVELOPMENTS

First home buyer (FHB) owner occupiers accounted for 21.2% of new property sales in Q2'17 (20.5% in Q1'17), while FHB investors accounted for 14.4% (10.2% in Q1). In total, FHBs made up 35.7% of all new property sales in Q2'17, up from 30.8% in the previous quarter - and the largest share since we began tracking this breakdown in Q4 2014.

SHARE OF NEW PROPERTY SALES (%)



Owner occupiers (net of FHBs) were also more prevalent in new property markets in Q2'17, accounting for 33.2% of total sales (32.7% in Q1).

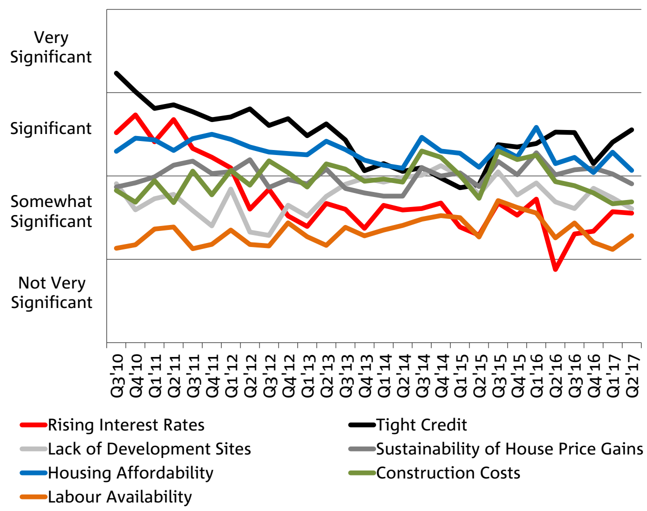
But the share of local investors (net of FHBs) in new property markets fell significantly to just 18.2% - its lowest level since the survey began. Clearly, tougher measures on banks announced by regulators to rein in investor lending are being felt in this segment of the market.

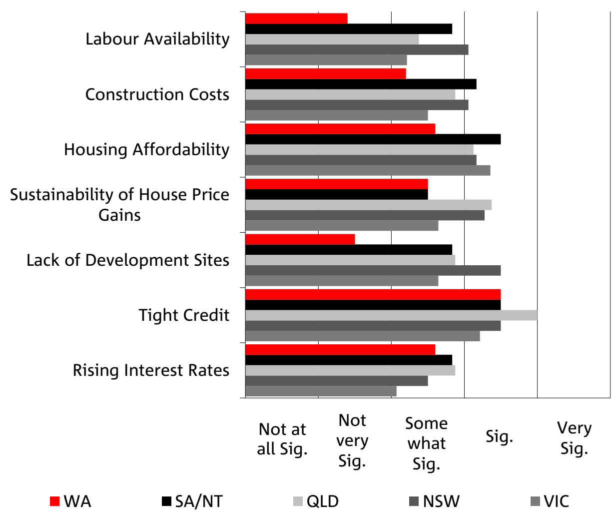
Foreign investors were however somewhat more active in new property markets in Q2, with their market share of total sales rising to 11.6% (10.8% in Q1). However, we again saw a big re-balancing in foreign buyer activity by state. In VIC, the share of foreign buyers in new property markets increased to 20.8% (13.8% in Q1). Foreign buyers were also more prominent in NSW (12.0% vs. 11.6%) and WA (6.9% vs. 5.6%), but less prominent in QLD where their share in the market fell to a 3-year low 8.6% (see section on foreign buyers below for more detail).

NEW HOUSING MARKET CONSTRAINTS

Overall, tight credit was still the biggest issue confronting buyers of new property in Q2 and has become more problematic, according to surveyed property experts. Concerns over housing affordability have eased somewhat, but also remain a "significant" constraint for new property buyers.

KEY CONSTRAINTS - OVERALL & STATES



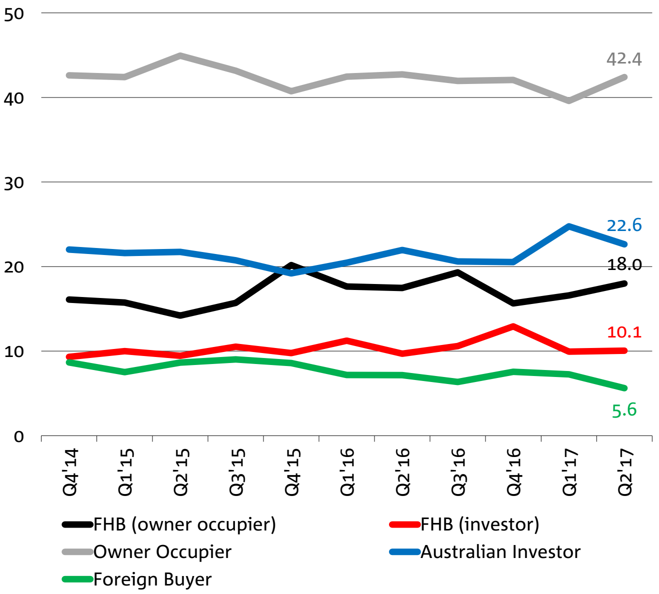


By state, tight credit was the main barrier to new housing development in QLD, WA, NSW (along with a lack of development sites) and SA/NT (along with housing affordability). In VIC, housing affordability was the most significant constraint facing buyers of new property in Q2.

ESTABLISHED PROPERTY

FHB (owner occupiers) accounted for 18.0% of established property sales in Q2'17 (16.6% in Q1). FHB (investors) accounted for 10.1% of all sales (9.9% in Q1). In total, FHBs accounted for 28.1% of established property sales in Q2'17 (26.5% in Q1).

SHARE OF EST. PROPERTY SALES (%)



Owner occupiers (net of FHBs) continued to play the dominant role in established property markets in Australia, with their share of total sales rising to 42.4% in Q2 (39.6% in Q1).

Local investors (net of FHBs) were however somewhat less active in established housing markets during the same period, with their overall market share falling to 22.6% (24.8% in Q1).

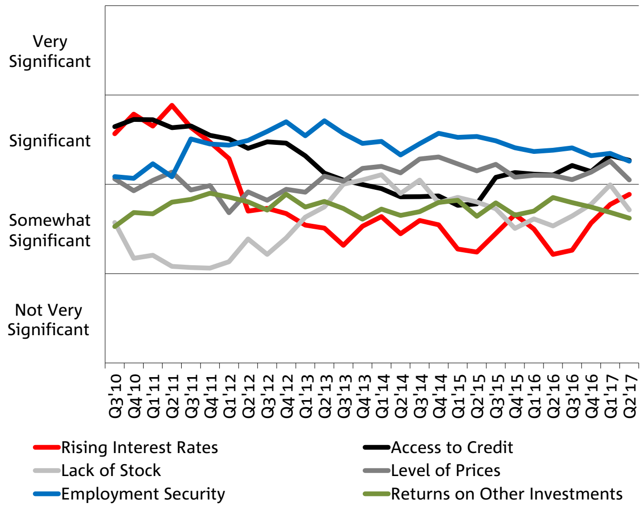
Foreign buyers of established property were also less prevalent in the market, with their overall share of sales falling to just 5.6% in Q2 - their lowest market share in over 4 years.

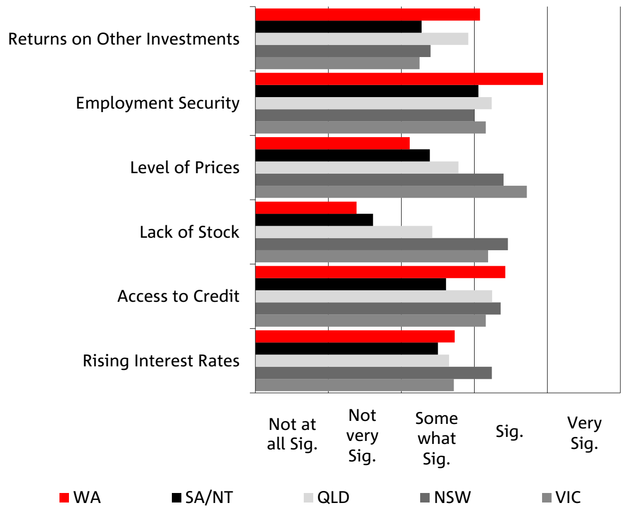
While foreign buyers of established Australian residential property were somewhat more prevalent in VIC (9.0% vs. 7.4%), they were less evident in NSW (5.9% vs. 8.0%), QLD (3.8% vs. 6.1%) and WA (4.5% vs. 7.0%). For more detail see section on foreign buyers below.

ESTABLISHED HOUSING MARKET CONSTRAINTS

Access to credit joined employment security as the most "significant" constraint on buyers of existing property in Australia in Q2, according to surveyed property experts. House price levels were also seen as significant. The level of concern over rising interest rates continued to grow and it has now overtaken a lack of stock and relative returns on other investments as an impediment to buying established property.

KEY CONSTRAINTS – OVERALL & STATE





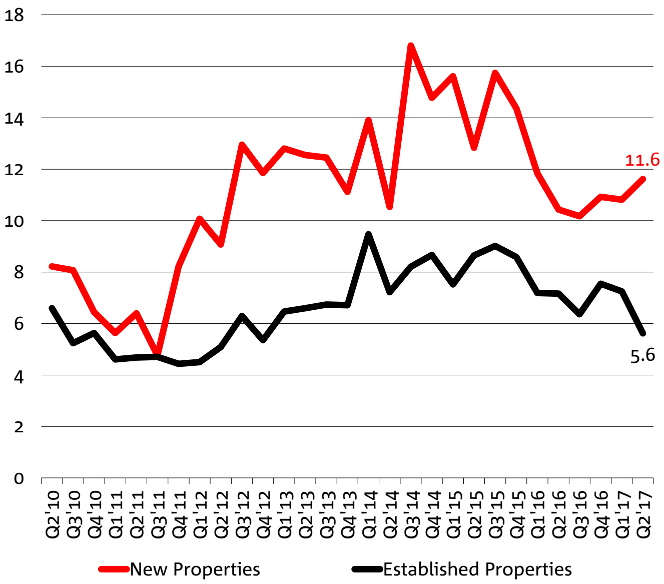
By state, employment security was seen as the number one impediment for buyers of existing property in QLD (along with access to credit), SA/NT and (particularly) WA. In NSW, however, a lack of stock was identified as the biggest issue, while property experts in VIC highlighted price levels as the biggest constraint for buyers of established property.

FOREIGN BUYERS

Despite China's crackdown on capital outflows into overseas property markets and a raft of new restrictions and taxes on foreign ownership of Australian properties introduced in the 2017/18 federal budget, the share of overseas buyers in new Australian property markets increased to 11.6% in Q2 2017, from 10.8% in Q1. But their share of total sales in established property markets fell to 5.6% - its lowest level in more than 4 years.

DEMAND FOR PROPERTY FROM FOREIGN BUYERS (% OF TOTAL)

Foreign buying activity increased in new property markets in Q2, but fell in established markets...

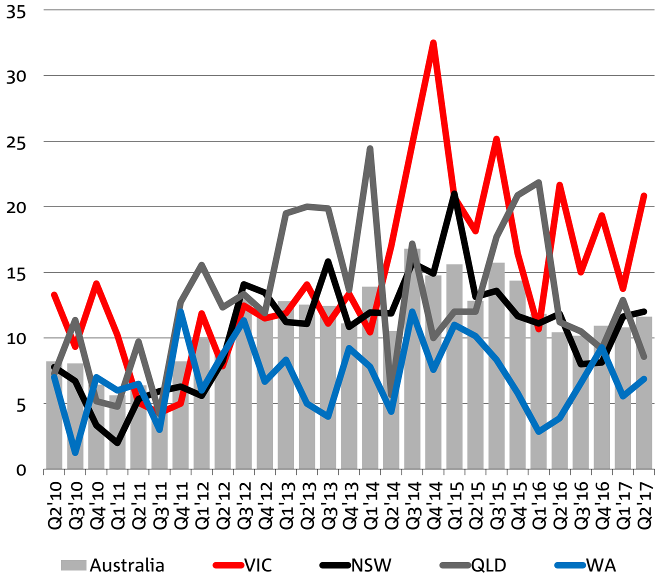


The overall increase in foreign buying activity in new property markets was driven largely by VIC, where foreign buyers accounted for just over 1 in 5 (20.8%) new property sales in Q2 2017 (13.8% in Q1), according to surveyed Victorian property experts. Foreign buyers were also slightly more active in NSW (12.0% vs. 11.6% in Q1) and WA (6.9% vs. 5.6%).

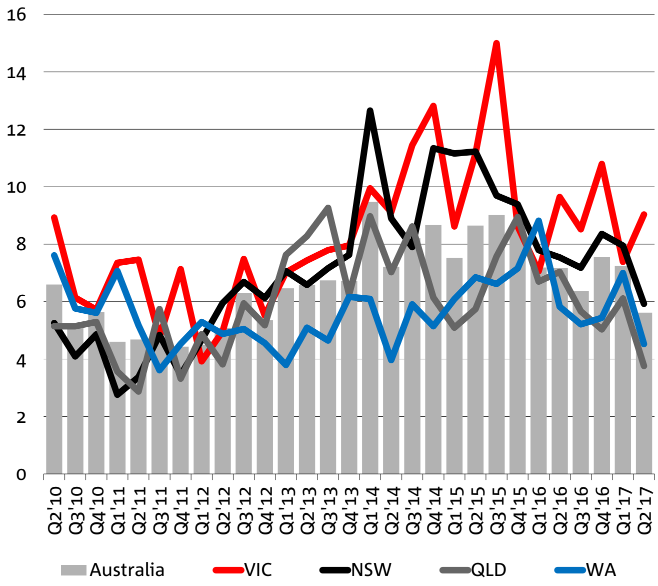
In contrast, foreign buyers were much less conspicuous in new property markets in QLD, with their share of total sales falling to just 8.6% (12.9% in Q1) - its lowest level since mid-2014 and well down on the 21-22% levels seen in late-2015/early-2016.

In established housing markets, the overall share of foreign buyers rose to 9.0% in VIC (7.4% in Q1), but fell in NSW (5.9% vs. 8.0%) and WA (4.5% vs. 7.0%). In QLD, foreign buyers accounted for just 3.8% of established property sales (6.1% in Q1) - its lowest level since late-2011,

DEMAND FOR NEW PROPERTY FROM FOREIGN BUYERS (% OF TOTAL)



DEMAND FOR ESTABLISHED PROPERTY FROM FOREIGN BUYERS (% OF TOTAL)

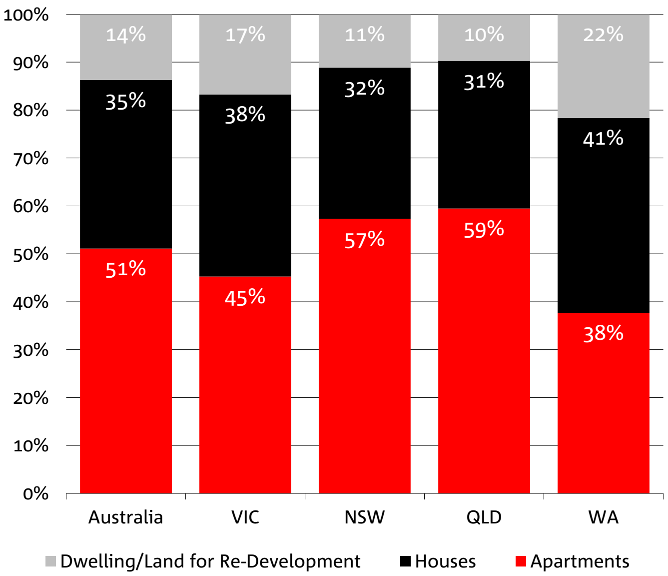


TYPE, SHARE & PRICE OF PROPERTIES BOUGHT BY FOREIGNERS

Property experts noted some changes in the mix of property purchased by foreigners in Q2 2017.

Around 51% of all property purchased by foreigners in Q2'17 were apartments (53% in Q1), 35% houses (28% in Q1) and 14% dwellings or land for re-development (17% in Q1).

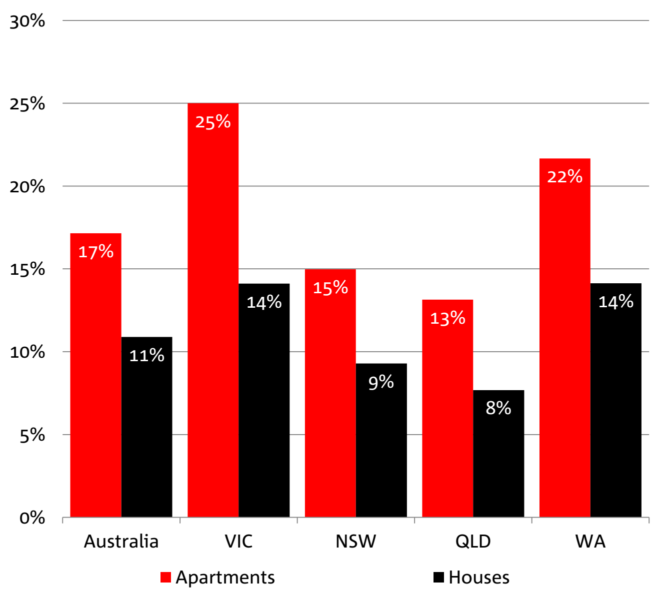
FOREIGN PURCHASES – STATE (%)



But these ratios varied a lot by state. Apartments accounted for a much bigger share of sales in QLD (59%), Sydney (57%) and VIC (51%), but houses accounted for the lion's share in WA (41%).

More than 1 in 5 (22%) residential properties purchased by foreigners in WA and 17% in VIC were for re-development, compared to around 1 in 10 in both NSW and QLD.

SHARE OF FOREIGN BUYERS IN APARTMENT & HOUSING MARKETS (%)



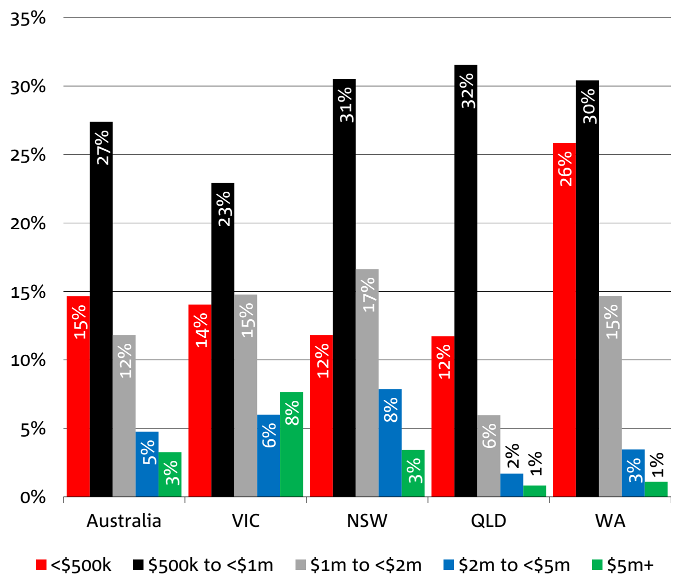
Property experts estimate that foreign buyers in Australian residential property markets represented 17% of all apartment buyers and 11% of all house buyers in the country in Q2 2017.

However, they played a much bigger role in the apartment market in VIC, where they purchased 1 in 4 (25%) properties and WA where they accounted for just over 1 in 4 (22%).

Property experts also estimate that foreigners represented just over 1 in 10 (11%) of all house buyers in Australia in Q2 2017.

They were most prominent in VIC (14%) and WA (14%) and least prominent in QLD (8%) and NSW (9%).

AMOUNT SPENT BY FOREIGNERS BY INVESTMENT LEVEL (%)



Overall, 15% of properties purchased by foreigners were for properties valued at less than $500,000 and 27% valued between $500,000-$1 million.

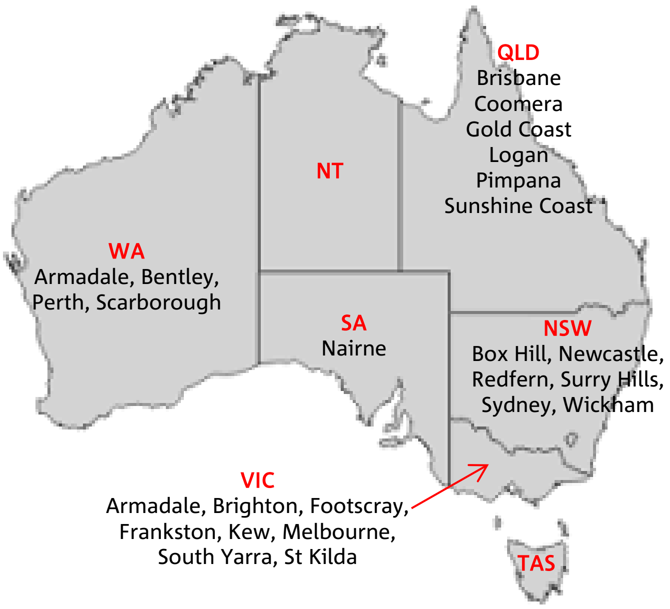
Around 12% invested $1-2 million, 5% between $2-5 million and 3% over $ 5 million.

By state, over 1 in 4 (26%) foreign property investments in WA were less than $500,000, compared to just 12% in NSW and QLD and 14% in VIC.

Around 1 in 3 foreign residential property investments in QLD, NSW and WA were valued at between $500,000-$1 million, compared to just 23% in VIC.

Around 8% of investments in NSW and 6% in VIC were between $2-5 million, while almost 1 in 10 (8%) properties in VIC were above $ 5 million.

SUBURBS TIPPED TO ENJOY ABOVE AVERAGE GROWTH IN NEXT 12 MONTHS



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AVERAGE SURVEY EXPECTATIONS: HOUSE PRICES (%)

	Q1'17	Q2'17	Next 1 year	Next 2 years
VIC	1.7	0.5	0.3	0.4
NSW	2.1	1.4	1.1	0.9
QLD	1.1	0.6	1.1	1.6
SA/NT	0.9	0.1	0.9	1.2
WA	-1.5	-1.4	-0.5	1.3
AUST	**1.3**	**0.5**	**0.6**	**1.0**

RENTS (%)

	Q1'17	Q2'17	Next 1 year	Next 2 years
VIC	1.1	0.7	1.2	1.5
NSW	1.2	0.5	1.1	1.6
QLD	-0.5	-0.2	1.0	1.5
SA/NT	0.0	-0.5	-0.3	0.5
WA	-2.3	-1.7	-1.0	0.2
AUST	**0.2**	**-0.1**	**0.7**	**1.3**

NAB'S VIEW OF RESIDENTIAL HOUSES PRICES

After multiple years of very strong growth, the housing market appears to be entering a cooling phase - although evidence points to an orderly adjustment rather than a sharp deterioration. Prices have continued to push higher, but the near-term growth momentum has eased and other indicators of the market pulse - such as auction volumes and clearance rates - suggest some moderation as well. However, some of the weakness is likely seasonal, while conditions still vary considerably across markets, with both Sydney and Melbourne continuing to out-perform, albeit with a fair degree of variation within market segments. That said, the divide between capital cities seems to have stopped growing as some of the under-performers (namely the mining regions) begin to stabilise, while the divide may soon narrow if the stronger performers begin to cool as expected.

In terms of annualised growth, Melbourne has been the best performing market of late, with prices rising by almost 14% over the year to June. There is, however, a notable divergence in price performance between units and detached houses, with less favourable supply conditions weighing on the former. Meanwhile, Sydney prices have risen almost as much - up around 12% over the year - and while the divergence is less stark, detached dwellings in Sydney are also seeing faster price growth than units. For the other capital cities, both Hobart and Canberra are also seeing reasonably solid price growth, while the Brisbane and Adelaide markets are seeing much more modest gains. Meanwhile, prices have fallen over the past year in Perth and particularly Darwin, although the pace of decline has clearly slowed in Perth.

House prices in Melbourne increased 15% over the year to June 2017, which compares to slightly more moderate growth of 13% in Sydney. Across the other capital cities, Canberra (9.7%) and Hobart (7.4%) saw the next best growth, while Brisbane and Adelaide (both around 2½%) each had modest gains. In contrast, headwinds from the mining sector saw prices in both Perth (-1.7%) and Darwin (-7%) decline - the Perth market appears to be stabilising, but conditions in Darwin do not appear to be improving, and will continue to be challenged as major LNG construction projects in the region reach completion. Reflecting the added risks facing the apartment segment of the market, unit prices have under-performed house prices in most markets by a fairly sizeable margin - a trend that is expected to continue. The difference is largest in markets where apartment supply concerns are greatest, especially in Melbourne (1.5% vs. 15%). The difference is also quite large in Brisbane (-3.2% vs. 2.5%), where unit prices have been falling. Meanwhile, unit prices in Sydney are still seeing solid growth (8.6% vs. 13%), despite also under-performing houses.

Annual aggregate dwelling price growth for the capital cities has moderated slightly from its recent peak, dipping back into single digit rates of growth since May. While it is still too early to call a definitive downward trend, a moderation in prices growth had long been expected, especially given the tightening of credit conditions following moves by banking regulators to contain investor and interest only mortgage growth - to promote financial stability. These measures are expected to be effective in the near-term, but while the longer-term impacts are debateable, they certainly add to the plethora of other headwinds to the market (see below).

Meanwhile, there are still a number of positive elements supporting market fundamentals, which help to form our view that the market is likely to see an orderly adjustment rather than a sharp correction. Interest rates remain quite low, despite recent increases in standard variable mortgage rates, which is keeping mortgage interest payments well down on previous peaks (as a share of disposable income). Meanwhile, pent-up demand for housing remains quite large in some markets. In fact, recent upward revisions to official population statistics meant we had previously underestimated the degree of pent-up demand for housing, especially in Victoria - this is also consistent with quite low vacancy rates in both Sydney and Melbourne.

Property prices rebounded from a seasonal soft patch in May, to hit an all new high in June. NAB Economics expects that property prices could continue to push a little higher over coming months, but tighter credit and prudential conditions are expected to have a more material impact by the end of the year, compounded by other major headwinds. This underlying outlook is largely unchanged from last quarter, although the near-term momentum (which prompted us to revise our forecasts higher last quarter) did not prove to be as exuberant as expected. As a result, accounting for recent price outcomes pushes our price forecast for 2017 lower, while our forecasts for 2018 still anticipate further cooling and are largely unchanged.

Our expectations around subdued wages growth remain, suggesting that affordability will remain a major constraint on the market - especially if credit conditions continue to tighten. This in combination with record levels of housing construction activity (mainly apartments) and moves to limit foreign demand for housing, will likely limit the potential for future price gains. Meanwhile, in light of reasonably resilient growth in investor credit, the potential for additional prudential tightening, or even severe credit rationing by banks (in order to achieve financial stability objectives) is a real risk. These headwinds are expected to more than offset any positive price impetus stemming from policy measures aimed at boosting first home buyer activity - such as recently announced increases and extensions to state first home buyer grants - and is evidenced by the sharp drop in market sentiment seen in the Q2 NAB Residential Survey (the NAB Survey). That said, the 2016 Census revealed that population growth was even stronger than previously expected, and solid growth is expected to continue, especially in Victoria, helping to drive underlying demand and soak-up some of the feared housing stock overhang - our estimates suggest sizeable pent-up demand in both Sydney and Melbourne. Foreign demand on the other hand is much more difficult to ascertain. Policy makers both domestic and overseas have sought to stem the tide of foreign capital entering the Australian property market, but the NAB Survey indicated that foreign demand unexpectedly increased in Q2.

For the most part, our perception of all these factors has not altered much since last quarter. On balance conditions are expected to soften going forward, contributing to more moderate price growth in the major property markets this year and next. That said, much softer market sentiment in the NAB Survey and weaker than expected price outcomes in recent months has prompted us to revise down our 2017 forecasts (partially unwinding the upward revisions from last quarter). House prices are forecast to rise 5% (previously 7.2%) in 2017, while unit prices are forecast to increase 3% (was 6.8%). The factors mentioned above are then expected to really kick in from late-2017, resulting in more modest price growth of 4.3% for detached houses and -0.3% for units in 2018.

By capital city, house price growth is forecast to remain strongest along the eastern seaboard in 2017, consistent with outcomes in the NAB Residential Property Survey and a relatively solid outlook for their local economies. Sydney and Melbourne will both see solid, albeit slower, growth in prices. Brisbane, Adelaide and Hobart will cool also, while Perth will remain very weak as house prices decline by another 2.5% - although the pace of decline has eased. These trends will broadly continue into 2018, with growth in Sydney and Melbourne returning to more sustainable levels. As usual, it is worth mentioning that the various government measures to combat affordability add another layer of uncertainty to the forecast.

The under-performance seen in the apartment market is set to continue, reflecting the heightened supply concerns in the market and uncertainty around the future of foreign demand. The timing of when new supply will come online and the willingness of potential buyers to shift their preferences towards these types of dwelling (influenced by affordability, cultural shifts, infrastructure and so on) remains a source of uncertainty for the outlook - although the recent Census has shown a material shift towards medium density living in Australia. Sydney and Hobart units are forecast to do relatively well in 2017, while all other markets are expected to decline. Most cities are expected to be fairly flat in 2018, while Melbourne and Brisbane will likely see additional declines.

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NAB HEDONIC HOUSE PRICE FORECASTS (%)*

	2014	2015	2016	2017f	2018f
Sydney	13.4	11.5	16.7	6.7	4.9
Melbourne	8.4	11.7	15.1	7.5	5.5
Brisbane	5.2	4.3	4.0	1.3	1.9
Adelaide	4.5	-0.3	4.5	2.2	1.7
Perth	2.1	-3.8	-4.4	-2.5	0.7
Hobart	3.3	-1.6	11.7	4.7	1.7
Cap City Avg	**8.4**	**7.8**	**11.6**	**5.0**	**4.3**

*Percentage changes represent through the year growth to Q4

NAB HEDONIC UNIT PRICE FORECASTS (%)*

	2014	2015	2016	2017f	2018f
Sydney	8.3	11.3	9.6	6.4	0.5
Melbourne	1.1	6.9	1.7	-2.6	-2.4
Brisbane	1.2	1.8	-0.2	-2.2	-1.8
Adelaide	2.5	1.4	1.1	-1.9	0.5
Perth	1.9	-3.5	-3.2	-3.6	0.7
Hobart	5.9	8.6	6.7	4.0	0.6
Cap City Avg	**5.1**	**7.9**	**5.9**	**3.0**	**-0.3**

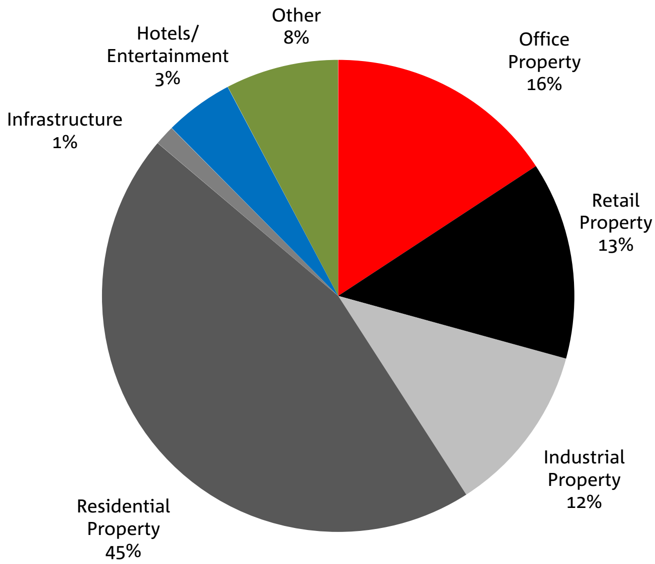
*Percentage changes represent through the year growth to Q4

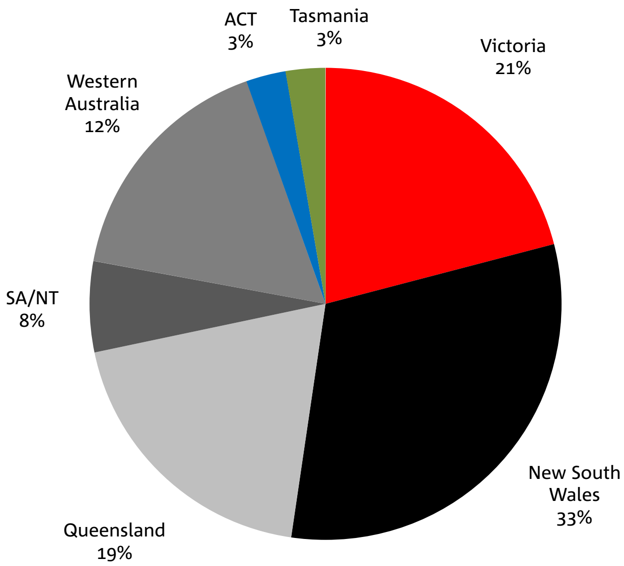
SOURCE: CoreLogic, NAB Economics

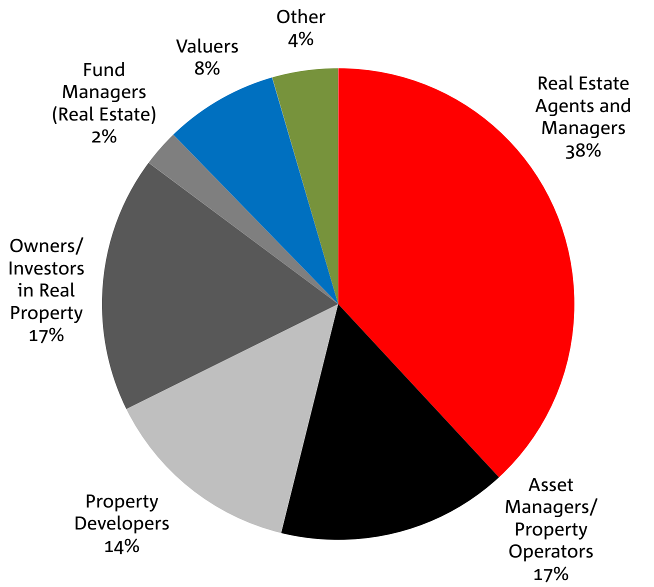
ABOUT THE SURVEY

The NAB Quarterly Australian Residential Property Survey was first launched in Q1 2011. The survey was expanded from NAB's Quarterly Australian Commercial Property Survey, which was launched in April 2010. Given the large number of respondents who are also directly exposed to the residential market, NAB expanded the survey questionnaire to focus more extensively on the Australian residential market.

The large external panel of respondents consists of Real Estate Agents/Managers, Property Developers, Asset/Fund Managers and Owners/Investors. Around 260 panellists participated in the Q2 2017 Survey and the breakdown of our Survey respondents - by location, property sector and business type - are shown below.







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