

Rate rise to prompt investor activity

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By Robert Carry

The Reserve Bank of Australia (RBA) has raised interest rates by 25 basis points taking the current cash rate from 3.25% to 3.50%. It's the second consecutive 0.25% rate increase introduced since the beginning of October. The latest move lifted the average variable rate to 6.26%, which is still well below its July and August 2008 peak of 9.6%. Tim Lawless, head of research at RP Data said that a slowing in house price value growth in September may have prevented the RBA from implementing a 0.50% increase. RP Data's results for September revealed property values increased by just 0.1% over the month. "The residential property sector had been surprisingly strong over the first eight months of 2009 and a further surge in values in September would have almost certainly resulted in double the rate rise," he said. Lawless added that rising mortgage rates will have a dampening effect on the market, particularly in the mortgage belts of Australia's capital cities. "First home buyer demand is already winding back, as evidenced by the number of housing finance commitments which fell for first home buyers by 23% in August," he said. RP Data also believes that the rise in rates is likely to hit the price sensitive segments of the market the hardest. "First home buyers and low income households will feel the rise the most, whereas less price sensitive mortgage holders and prospective buyers will be less affected. In fact, investors are probably welcoming the rise in the mortgage rates as it means less competition in the market place," said Lawless. The move suggests the RBA is becoming increasingly confident that the Australian economy is through the worst of the global economic crisis. The RBA's rate rise has been widely predicted by experts after the group said in the wake of the last increase in October that the cash rate was at an "unusually low level", adding that there was a necessity to return to a "more normal setting". The rate hike will spell a significant increase in monthly repayments for people with variable rate mortgages. Mortgage holders can expect to pay an extra \$57 a month on a \$300,000 loan spread out over 30 years. Looking ahead, economists including Craig James of CommSec and Shane Oliver of AMP Capital Investors believe that RBA is likely to stick to a gradualist approach in raising interest rates given the potential vulnerability of the economy to a too hasty removal of stimulus and given that the September quarter inflation figures were not bad enough to justify a more aggressive approach.