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After the boom

Residential real-estate prices are drooping in Canada and the United States and actually falling in the People's Republic of China, greater London, metropolitan Stockholm and—especially—Australia. Now unfolding is a closer look at the action Down Under. In preview, we see in the Lucky Country the symptoms of post-boom deflation syndrome, a kind of macroeconomic katzenjammer.

It's been a storied boom, 27 years young as of Sept. 30, and we think we will not join, or perhaps the word is rejoin, the hapless prognosticators who have tried to call time on it. However, crowding out the news of the latest cyclical milestone was the report that Australian banks rejected just under half of all mortgage applications in November, compared with a year-earlier rejection rate of just 5.2%.

Nothing that the Reserve Bank of Australia has recently done (its policy rate remains 1½%) can explain it. The problem rather seems to lie in what came before—in particular, the bank's efforts to boost house prices to compensate for the slowdown in resource-related investment; between November 2011 and August 2016, the policy interest rate tumbled to the still prevailing 1½% from 4¾%. Perhaps taking their cue from the central bank, the commercial banks' reflexive response to mortgage applications became a hearty "yes."

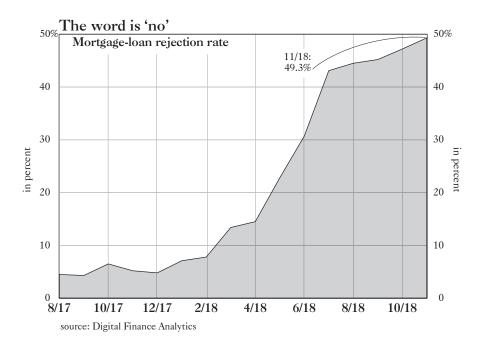
Now—as the data wizards at Digital Finance Analytics have been able to show—the fallback word is "no." Shamed by revelations of Americanstyle lapses in bankerly due diligence, the Aussie lenders have belatedly re-

verted to prudence (*Grant's*, June 15). They are actually said to be checking incomes, expenses, total debt and other such previously unexamined details. It can't be entirely coincidental that, in November, average house prices in the five leading Australian markets fell by 5.6% while Sydney's plunged by 8.1% and Melbourne's by 5.8%. The latter two cities account for "approximately 55% of the value of Australia's housing asset class," according to CoreLogic's head of research, Tim Lawless.

"The rise in mortgage rejections comes at a particularly difficult time for borrowers," colleague Evan Lorenz relates. "At the end of 2015, nearly two-fifths of mortgages were interest-only (IOs). The typical Aussie IO starts amortizing after five years, at which point

monthly payments increase by 30%–40%. The Reserve Bank estimates that around A\$120 billion (\$86.3 billion) of IOs will reset annually in 2018 through 2020. 'About one-third of that won't get refinanced,' says Martin North, the principal of Digital Finance Analytics."

The big four Aussie banks may not be lending, or at least not with their boomtime zeal, but that doesn't mean that every channel of mortgage finance is closed; would-be borrowers are turning to a different class of lender. "To go to the peripheral lenders as opposed to the mainstream lenders, it will cost borrowers more," says Michael Schneider, lead portfolio manager of the soon-to-launch Firebell Australian Macro Fund. "The way I look at it is that it has as similar impact as a tightening in official



interest rates—it is going to cost more."

Certainly, Schneider goes on, the builders and developers are having to pay up. "There is quite a vibrant mezzanine debt market in Australia right now, which is charging far higher interest rates," he says. "I've been told by some lenders in that market that they are lending at rates up to 16% in the mezzanine market to developers."

One of the troubles with prosperity (there aren't so very many) is that uncorrected errors accumulate. "Take, for example," Lorenz writes, "the ironically named Blue Sky Alternative Investments Ltd. (BLU on the Australian Securities Exchange), an alternative asset manager favoring private-equity-style investments, water rights and real estate in Australia and North America."

On March 28, Blue Sky awakened to discover that it was the star of a 67-page analysis by Glaucus Research Group. The report alleged, among other things, that the 15% internal rate of return that Blue Sky claimed to have

earned since its 2006 inception was a near impossibility. And, sure enough, Blue Sky, in calculating assets under management, had managed to lump in debt with equity, thus hugely inflating fee-earning assets. (America's Beardstown Ladies, an Illinois investment club for women of a certain age, had made a similar mistake in the 1980s.) Since the unmasking, Blue Sky's market capitalization has collapsed to A\$74.6 million from A\$885.6 million.

On Oct. 28 came a 176-page broadside by a different research organization, VGI Partners Pty. Ltd., criticizing Corporate Travel Management Ltd. (CTD on the Australian Securities Exchange), an online business-travel roll-up boasting an adjusted operating profit margin of 32% vs. 13% for peers in a highly competitive global industry. CTD had claimed a worldwide network of branch offices; the VGI analysts, traveling to visit them, found half of European and a quarter of U.S. offices to either not exist or to be unoccupied. CTD had bragged about its "patented" proprietary technology; the VGI analysts, combing government databases, couldn't find the patents.

CTD issued a 14-page rebuttal (qualified with the warning, "For personal use only"), contesting some points, acknowledging others (certainly, it should "keep its website updated with its office locations"). It insisted, however, that it has earned margins that—for instance—its much bigger American rival, Egencia, a businesstravel unit of Expedia Group, Inc., has not come close to matching.

The CTD share price, though down by 37% from a Sept. 4 peak, is nonetheless quoted at 29.1 times trailing earnings; the CTD market capitalization is still a formidable A\$2.3 billion. Of the eight analysts who rate the company, six say buy, none says sell. Twenty-seven consecutive fat years can make a bull out of just about anyone.

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