# ASX sell-off extends on inflation worries

**Equities**

Joshua Peach

Australian shares fell for a third straight session yesterday, as investor risk appetite continued to falter and concerns about the path of inflation once again took hold.

The S&P/ASX 200 closed down 37.4 points, or 0.5 per cent, to 7628, extending the three-week lows touched on Wednesday after a hotter than expected inflation print. The benchmark has now fallen more than 3 per cent since nearing its record high in mid-May.

"With just one trading day left before the month's end, the ASX 200 is now on track for its second consecutive monthly decline after falling in seven of the eight past sessions," said IG analyst Tony Sycamore.

The losses follow similar moves lower on Wall Street after US bond yields climbed following a second day of poor demand at US government debt auctions.

The weak demand came ahead of key US core personal consumption expenditure data, to be released late today (10.30pm AEST). It is expected to shed light on the US Federal Reserve's interest rate path.

Fed member Neel Kashkari earlier in the week said that while the central bank's policy stance was restrictive, more rate increases had not been ruled out. The US 10-year yield was 6 basis points higher to 4.16 per cent.

Mr Sycamore said Australia's hot inflation figures on Wednesday, and the deepening rout in the US bond market, had sent the pendulum of sentiment swinging in a different direction this week.

"The market has fallen under the spell of the bond market genie and higher yields," he said in a note to investors.

"The focus has turned to protecting P&L into month-end along with managing the downside risks should we see firmer than expected US or European inflation data tomorrow evening."

On the benchmark, mining stocks were the worst hit, tracking a 2.9 per cent drop in the price of iron ore futures in Singapore to $US115.24 and sending Rio Tinto 1.5 per cent lower to $127.66 and Fortescue off 3.1 per cent to $24.78.

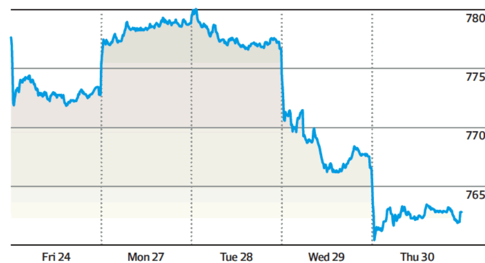
BHP Group fell 1.7 per cent to $44.30. Early yesterday morning, the mining giant decided against making a fourth takeover offer for UK-listed Anglo American after its request for another extension was rejected.

NRW Holdings was among the best performing on the benchmark, climbing 3.5 per cent to $3. The contracting company was raised to a buy rating by analysts at Jarden.

Wearable sports hardware business Catapult Sports jumped 9.7 per cent to $1.70 after narrowing its full year net loss to $US19.1 million and increasing sales 18.5 per cent to $US100 million.

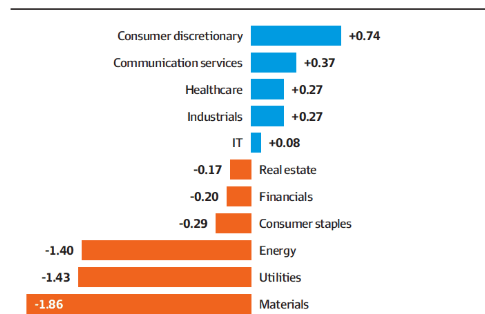
Australian Agricultural Co rose 2.8 per cent to $1.45 after Australia's Minister for Agriculture, Murray Watt, confirmed that China had lifted its ban on Australian beef exporters that were locked out in a trade war in 2020.

**SHAREMARKET** S&P/ASX 200 Index, past five days (points)

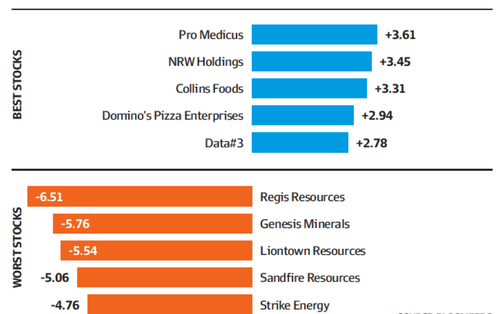



**COMMODITIES** Iron ore ($US/tonne)

**MARKETS** Sector performance, Thursday (%)




**COMPANIES** Stock performance, Thursday (%)




SOURCE: BLOOMBERG

# Let business play role in affordable housing crisis

**Opinion**

Justin O'Brien

Australia has an abundance of space. However, most of us want to live close to a few large cities, a simple fact that has created significant wealth for those lucky enough to own property.

For others, the Australian dream has become unattainable.

Despite all the rhetoric, governments can't and won't be the panacea for our housing affordability crisis. Like all complex problems, we need multi-faceted solutions, and the corporate sector has an important role to play.

Housing affordability is at its worst level in 20 years and is expected to decline further. Supply, as measured by new housing starts, is at cyclical lows.

However, demand via migration remains high (for now) and demographic trends continue to shift the type of housing needed.

This has led to very low vacancy rates for rentals with the likelihood that rents will trend higher, further stoking the inflation fire.

In a recent presentation to investors, John Carter and David Dixon, the joint chief executives of Aspen, a developer and operator of affordable housing, put numbers to the problem. They highlighted that there were more than four million households with an annual income of less than $90,000 requiring affordable housing, which they defined as under $400,000 to buy or less than $400 per week to rent.

However, building accommodation that meets these criteria is extremely challenging given the high cost of land, building materials and the labour needed to construct – let alone taxes, which are a very high proportion of the cost of new builds.

These costs have risen substantially since the onset of COVID-19 and remain stubbornly high. Given the many and complex reasons underpinning this inflation, it is difficult to see them falling soon.

Perhaps governments will once again lean on subsidies to offset these high costs. But for how long should taxpayers bear the brunt?

Our view is that clever corporates, operating under a profit motive, are one solution to the problem. Aspen has deployed some novel approaches that government can only dream of using, such as buying sites from receivers, or acquiring difficult assets that require repositioning or capital spend to bring them up to scratch.

In an interesting contrast to recent government announcements to demolish and rebuild large apartment buildings in Sydney and Melbourne, Carter and Dixon highlighted the portfolio they purchased in Perth in 2019. Aspen paid $52 million at the time for 17 properties, many with very high vacancy rates. Their most recent refurbishment within this portfolio was the Maylands apartment complex, near the Perth CBD.

Aspen co-chief executives John Carter and David Dixon. Aspen has found novel ways to combat the cost inflation plaguing the sector. PHOTO: BRENT LEWIN

Aspen paid just $58,000 for each apartment, which at acquisition had just 38 per cent occupancy. By spending $131,000 on average, on both the apartments and surrounding area, Aspen has significantly improved the units' "liveability", which has driven occupancy to 100 per cent with the University of Western Australia now an anchor tenant.

For investors, this renovation has generated a circa 50 per cent return on investment.

Had Aspen simply knocked down Maylands and rebuilt, it might have taken five to 10 years to obtain planning permits and complete construction. Not to mention the vast waste of concrete, steel and other energy-intensive materials, or the eventual high rental cost, well outside the affordable level, needed to earn an adequate return. But novel approaches, while necessary, are still not sufficient. To be a low-cost service provider, it is essential to have a low-cost position yourself.

That doesn't just mean providing a service efficiently. Scale is often a vital factor in achieving a low-cost position as it dictates a "structural" level of costs.

For housing operators and developers, this includes overhead costs such as marketing, operations and administration, where bigger translates to lower overhead costs per unit.

For rental providers, the corporate operator owns the bricks and mortar, which is a capital-intensive game. Being listed has an advantage in sourcing capital. But listed companies also benefit from scale.

Bigger stocks often enjoy a lower cost of capital – a fact the real estate investment trusts have taken advantage of for many years.

Given the scale benefits of operating and capital costs to the sector, mergers and acquisitions should be encouraged. Scale achieved via M&A will ultimately lead to better outcomes for consumers and assist in creating long-term sustainable operators.

This is one of the reasons we supported the proposal to merge Aspen with the sub-scale operator Eureka. We were substantial shareholders in both companies until we converted our Eureka shares to Aspen shares. The logic for creating a more scalable business is obvious. Despite the deal's rejection by Eureka shareholders, Aspen remains well-placed to build on its position, while also delivering value for Aspen shareholders.

To us, this is the essence of a sustainable operator and is at the heart of our investment philosophy which seeks good-quality companies, run by management teams and cultures that have a proprietorial or ownership mindset, with the opportunity to create value longer-term in industries with tailwinds.

*Justin O'Brien is a portfolio manager at Cooper Investor.*