BNZ Weekly Overview

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Mission Statement

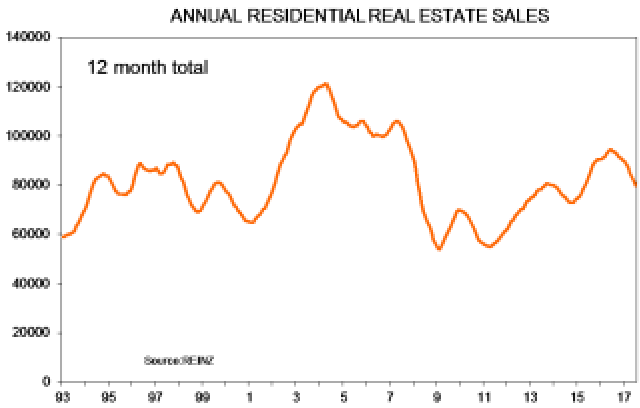
To help Kiwi businesspeople and householders make informed financial decisions by discussing the economy and its implications in a language they can understand.

Residential Real Estate

The REINZ released their residential real estate sales data last week and what the numbers show us is what we already knew – falling sales almost everywhere, prices flattish to falling in Auckland, prices still rising in most other locations.

Nationwide the number of dwellings sold in the three months to July was down by 22% from a year earlier. This continues a trend of falling sales ever since the Reserve Bank made banks implement their minimum 40% deposit rule for investors from the third week of July last year. This trend has further to run and as we wrote here a few months back, the chances are that annual sales will continue to fall over the remainder of this year and next until 12 month sales total something less than 65,000.

In the year to July sales totalled 80,000 and the peak was 95,000 in the year to June last year. The low before that was 55,000 in 2011 and before that 54,000 early in 2009. The risk is that sales fall below 65,000 and this means people exiting the real estate industry.



Recently some parties have started lobbying the Reserve Bank to ease LVRs for first home buyers. Is there evidence that FHBs are being excluded by LVR rules? We could try to answer this by looking at mortgage data gathered and reported by the Reserve Bank each month in their table C31. But the new lending data they show includes refinancing and is not restricted to completely new lending. For instance, they show total loans in the year to June of 304,000. But the actual number of dwellings sold was 81,000. So most lending done by banks is actually refinancing.

Instead we look at data from Core Logic contained in their monthly report. http://www.corelogic.co.nz/news-research/item/share-of-sales-to-investors-dropping-across-the-country/

They show that in the June quarter the proportion of dwellings sold which went to first home buyers was 21%. This was the same proportion as just before the LVR relevant to them appeared in October 2013 when annual sales numbers were basically exactly the same as now. Compared with a year ago when annual dwelling sales were near 95,000 the proportion accounted for by FHBs was around 20%. So there is no obvious disproportionate fall in sales to FHBs.

Note that during the year to April 2017 15,400 people used the KiwiSaver HomeStart scheme which lets KiwiSaver members access their funds and receive a grant to purchase a first house. There were 85,000 dwelling sales by REINZ members in the year to April. HomeStart users therefore accounted for 18% of all sales.

Feedback we get suggests that the reasons FHBs are buying fewer dwellings now than one, two and three years ago is that the house prices are too high and the loans they would need to take out too frighteningly big. Meeting debt servicing requirements from lenders (which are being steadily tightened) also means some cannot qualify for a loan even if they have a 20% deposit.

In fact it pays to remember that banks can still make up to 10% of their lending with deposits less than 20% of the purchase price and it looks like 25% of FHBs do have less than 20% deposit. Plus they account for almost half of all loans with less than 20% deposit, up from one-third a couple of years ago.

Therefore, even without debating whether the housing market has slowed enough for the Reserve Bank to make special exemptions for first home buyers we can reasonably say that LVR rules don't necessarily seem to be what is holding all of them back.

Could the Reserve Bank be close to easing LVR restrictions? By our argument they could for FHBs and it would make little difference. For investors? Minimal chance in the near future. As we noted here last week when reporting on the Reserve Bank's latest review of their 1.75% cash rate, they still see a risk that this market pause could be temporary. The ongoing low interest rates environment will keep gnawing away at investors and could send them newly searching for assets other than term deposits – like property.

If we go back to the August 20 2013 announcement by the RBNZ that LVRs would be introduced from October 1 that year we glean this comment.

"How long LVR restrictions may remain in place depends on the effectiveness of the measures in restraining the growth in housing lending and house price inflation. LVR limits will be removed if there is evidence of a better balance in the housing market and we are confident that their removal would not lead to a resurgence of housing credit and demand," Mr Wheeler said.

http://www.rbnz.govt.nz/news/2013/08/limits-for-high-lvr-mortgage-lending

Annual house price inflation has slowed nationwide from 6.3% back then to 5%. Auckland has slowed from 11% to 2%. But the annual pace of growth in lending for housing purposes was 5.2% in August 2013. It is now 7.7%. It is difficult to believe that the Reserve Bank feels there is yet sufficient restraint in the growth of housing lending. And as already noted, they mentioned in last week's cash rate review statement

"House price inflation continues to moderate due to loan-to-value ratio restrictions, affordability constraints, and a tightening in credit conditions. This moderation is expected to persist, although there remains a risk of resurgence in prices given continued strong population growth and resource constraints in the construction sector."

In other words, they are not yet convinced of "better balance in the housing market." However, this could change if we get an international scare as older people seeking yield tend to be more conservative than younger borrowers.

A Special Message To First Home Buyers

The market is moving in your favour. A lot of investors have over-extended themselves in the past three years and their hopes of new investors taking property off their hands at a tidy profit have been dashed. The next layer of the investor pyramid has been stripped away by the need to raise a 40% deposit and banks steadily tightening debt servicing criteria. In fact when an existing investor with a few properties these days goes to their bank seeking finance for a new purchase, even if they have a 40% deposit banks are saying they need 40% coverage also for their existing portfolio. That means in many cases either the planned purchase by the established investor does not happen, or they achieve it by selling some of their existing stock.

Auckland is interesting in that there is now an over-supply of properties which can be intensified. The finance is not there to allow construction, and neither are the builders. So lots of investors are now sitting on potentially highly geared up properties they cannot get anyone to buy and develop. They, like you young person, are reading things like this. They are hearing the lobbying from real estate agents for LVRs to be removed. Some may be facing settlement soon on an apartment they signed up for a couple of years back.

They are nervous and getting worried that any profit on paper they may have achieved the past year or two could be disappearing fast. They are starting to get stressed. The FOMO which drove them to gear up and buy any old piece of property last year and before is now working in the opposite direction. They are vulnerable as a mass to something. Some trigger. Maybe newspapers catching up with the way power is shifting in the Auckland market and running stories of outright losses, dragging out the usual head on a stick suspects to predict (yet again) a collapse in prices.

The time is ripe for you first home buyer to start taking advantage of their pain.

- Relax. Take a few breaths. Take your time.
- Look at a number of properties.
- Start throwing in low ball offers in case you catch a truly panicked fish.
- Alternatively, simply make an offer for what you think a place is really worth – and stick with it. Don't let the agent work you. They know that at this point in the housing cycle the effort they need to put in is on the vendor – convincing them that the days of stupid prices have ended.
- Stick with your price and walk away if they won't budge. If they spray, walk away!

Now, go back and read that little list again. Think about it, and then ask yourself this. As someone with no previous experience of home ownership, essentially no experience of housing cycles, little insight if any into the mind of someone selling, what would you do when your offer is rejected in an environment where LVRs were relaxed especially for you as the real estate agents want? You will borrow more money simply because it is there, you are being told to do so, and you have not felt the stress yet of worrying about debt and keeping your home when your income falls.

The last thing you need now that the market is moving in your favour is for extra demand to be thrown into the market with LVR reductions simply to bail out investors who have over-committed themselves.

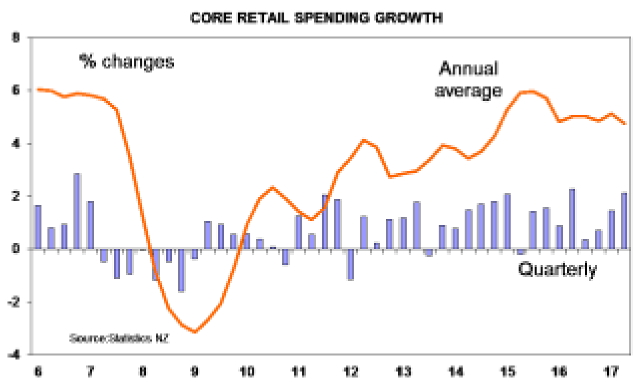
So start your looking, and keep an eye on the words which agents are using in their advertising. Here are some suggestions along with the number of properties for which the full phrase appeared in ads on www.realestate.co.nz last night. I confined my analysis to Auckland.

Total ads for Auckland	11,195
Bargain	88
Desperate	11
Best offer	8
Overseas owner	14
Mortgagee	12
Make an offer	115
Be quick	877
Motivated	496
Sell now	16
Take advantage	455
Must sell	145
Won't last long	159
Will consider all offers	7
Fixer Upper	1
All offers considered	5
Act quickly	36
Priced to sell	279
Vendor says	42

And heck, maybe you don't for the moment even need to consider buying a "compromised" house!

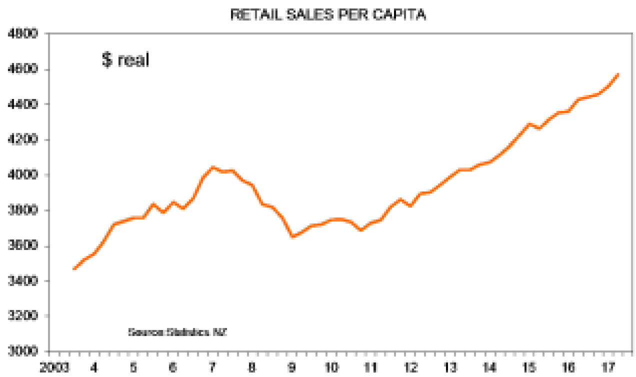
Retail Spending

On Monday we learnt that core retail spending (excludes cars and petrol) rose by a very strong 2.1% in the June quarter to be 4.7% ahead of a year earlier. This is after adjusting for inflation and any seasonal effects.



Much has been made of the impact of the Masters Games then Lions Tour which boosted accommodation and liquor store sales. But we can still conclude that the quarter were strong because sales by electrical stores rose 5.2% after rising near 6% in the March quarter. And sales of stores which tend to sell durable goods which consumers typically only buy more of when they are confident about their futures, rose by 3.3% following a 2.5% rise in the March quarter. These sales were ahead 9.3% for the entire year to June.

Retail spending per capita rose 1.5% to be 3% ahead of a year ago. There has been an upward trend in this inflation-adjusted measure since 2010.



The data do not carry any major implications for monetary policy or the exchange rate. They just show one aspect of the firm growth occurring in the New Zealand economy.

If I Were A Borrower What Would I Do?

Nothing new to say here. Monetary policy looks like remaining on hold for a long time and expectations of rising US rates which would drag rates up globally have been scaled back as fiscal stimulus expectations by the possibly failing Trump administration have been canned.

NZ Dollar

Maybe next week. Nothing truly new to report.

If I Were An Investor ...I'd see a BNZ Private Banker

The text at this link explains why I do not include a section discussing what I would do if I were an investor.
http://tonyalexander.co.nz/regular-publications/bnz-weekly-overview/if-i-were-an-investor/

The Weekly Overview is written by Tony Alexander, Chief Economist at the Bank of New Zealand. The views expressed are my own and do not purport to represent the views of the BNZ. **This edition has been solely moderated by Tony Alexander**. To receive the Weekly Overview each Thursday night please sign up at www.tonyalexander.co.nz
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