

Home Truths

11 March 2014

A neat twist

The housing market is continuing to slow in response to the Reserve Bank's restrictions on high-LVR mortgage lending. And it is now fairly clear that the market slowdown has been more acute than the Reserve Bank anticipated.

The best way to take the pulse of the market is to seasonally adjust the sales data recorded by the Real Estate Institute of New Zealand (REINZ). By our reckoning, seasonally adjusted sales fell 2.4% in February. The total decline in sales since the mortgage restrictions were introduced now sums to 13.4% - as sure an indication of a slower market as any.

To be fair, secondary data relating to the month of February was mixed. The REINZ's record of the time taken to sell a house fell. And individual real estate agencies and websites have reported quite mixed experiences. But running one's eye across the general trend in this more volatile data does yield a consistent story. The housing market unambiguously took a hard slap immediately after the high-LVR mortgage restrictions came into force last October.

The decline in market turnover has been heavily concentrated in the bottom end of the market - again, consistent with the idea that it is the first homebuyer part of the market that has taken the hardest knock.

This change in the composition of house sales is skewing much of the house price data. The median sale price has clearly been impacted by the paucity of sales at the bottom end of the market. We normally pay close attention to the Real Estate Institute's House Price Index, but we now suspect it too has been polluted by the sudden shift in the composition of sales.

The best available take on house prices at this juncture is probably Quotable Value's Monthly Property Value Index, which is unaffected by the composition of sales. However, because QV records sales upon settlement, the information is effectively two months older than other price data. In any case, after rising 10% in 2013 the QV index suddenly flattened off in January and February of this year, with the weaker price increases manifest across most regions of the country.

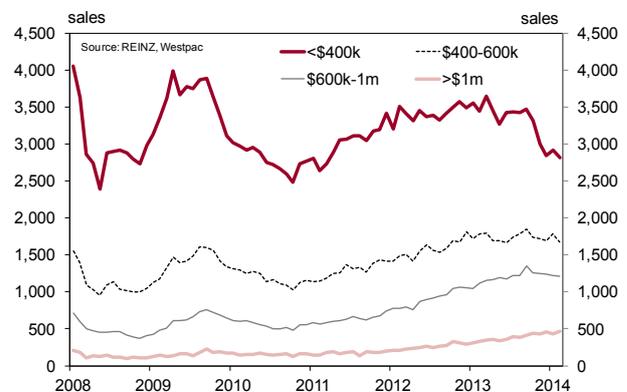
RBNZ reaction

The housing market is clearly slowing more sharply than the Reserve Bank anticipated, a fact that will probably be mentioned in Thursday's *Monetary Policy Statement*. However, other aspects of the economy have been stronger than the RBNZ anticipated. Inflation is surprising on the upside, GDP has been stronger than anticipated, business confidence is

at a twenty-year high, and the terms of trade are at a forty-year high. So the Reserve Bank has as much reason as ever to persist with lifting the OCR this year, despite the slowing housing market.

We expect this will become a theme over the next couple of years. The economy will remain strong due to Canterbury earthquake reconstruction and high export returns. To suppress inflation pressures from bubbling up, the Reserve Bank will have to lift interest rates. And those higher interest rates will become a very serious headwind for the housing market - perhaps even causing a period of declining house prices later in the decade.

This would be a neat twist on the mid-2000s, when rising house prices and the associated consumer spending party were the cause of inflation pressures, but the resulting interest rate hikes created headwinds for the export sector.

REINZ house sales by price bracket**REINZ housing data, February 2014**

	Feb-14	Jan-14	Feb-13
House sales, number, s.a.	6147	6300	6674
Mth % chg	-2.4	-0.1	-0.7
Ann % chg	-7.6	-4.3	7.5
Days to sell, sa	34.8	35.6	33.0
House Price Index (s.a.)	3861.1	3828.3	3566.7
Mth % chg	0.9	-0.3	0.4
Ann % chg	8.2	7.7	8.1

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