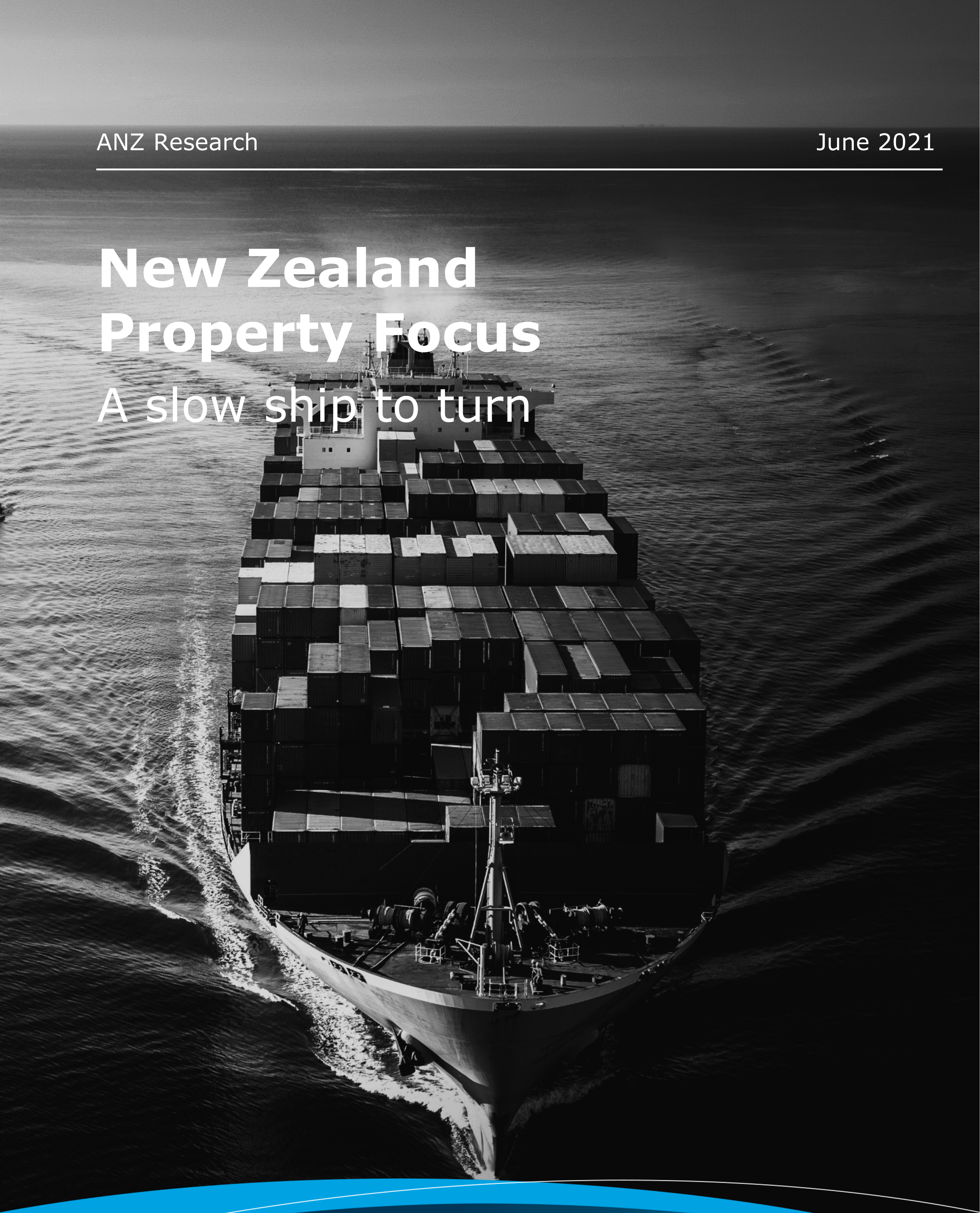


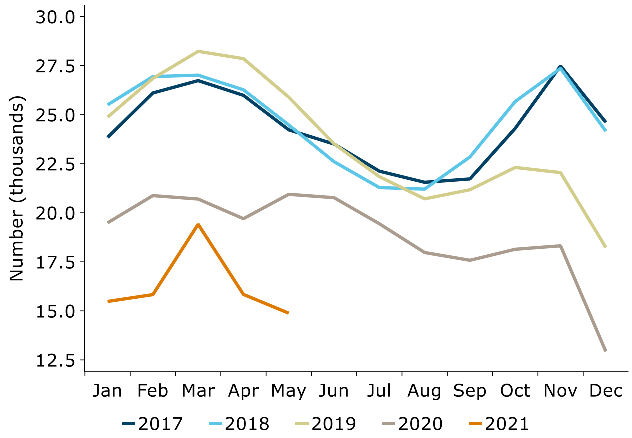
New Zealand Property Focus

A slow ship to turn

At a glance

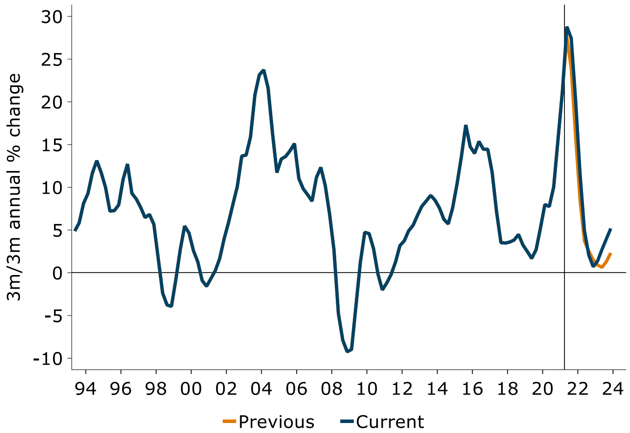
Low inventories

Are making it tough for buyers



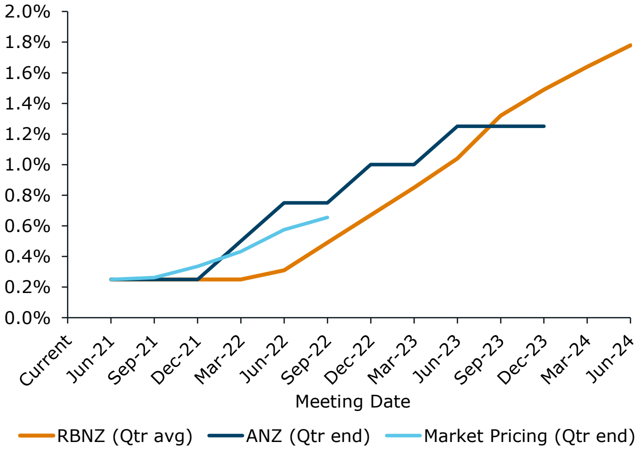
House prices to moderate

A bit slower than we thought for 2021



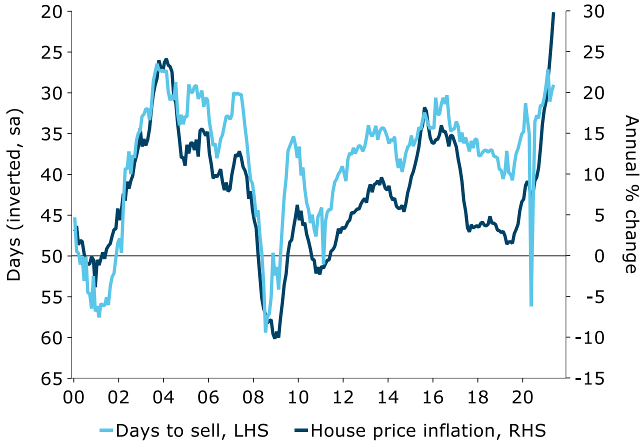
Rates to lift

As the OCR is hiked from February 2022



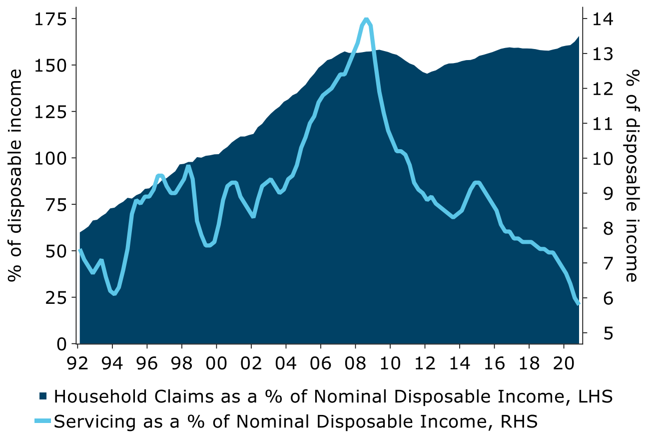
Days to sell remain low

Highlighting ongoing pressure



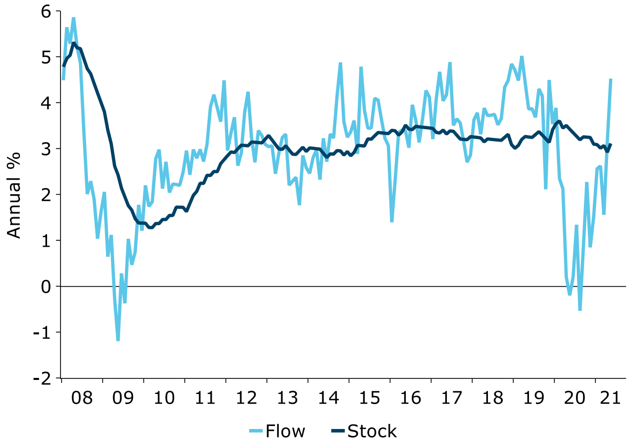
Households remain vulnerable

With record levels of debt



Signs of stronger rent inflation

But it's still early days



Source: RBNZ, REINZ, Stats NZ, Macrobond, Bloomberg, ICAP, RealEstate.co.nz, ANZ Research

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Contact

Sharon Zollner, Miles Workman, David Croy or Finn Robinson for more details.

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INSIDE

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Summary

Our monthly *Property Focus* publication provides an independent appraisal of recent developments in the residential property market.

Housing market overview

May housing data suggest recent Government policy announcements are weighing on overall housing activity. Sales fell 11.8% m/m in May (seasonally adjusted). But with listings also sparse, reduced investor demand hasn't yet been enough to slow the monthly pace of house price inflation. This came as a bit of a surprise and we have upgraded our near-term house price forecasts to include a little more momentum. We have also brought forward our expectation for OCR hikes by six months to February 2022. That means mortgage rates are expected to rise a little sooner than before, taking some of the steam out of the housing cycle a bit earlier. See our Market Overview.

Mortgage borrowing strategy

Longer-term fixed mortgage rates continue to rise and are now well above lows seen earlier in the year. In contrast, shorter-term rates continue to edge lower, taking the average 1-year rate to yet another record low. Appealing as lower short-term rates are, they don't offer certainty for long. To echo the thoughts we have had for some months now, we think there is merit in considering fixing for longer, even if rates have risen slightly. Since our last edition, the RBNZ has signalled that they expect to hike the OCR in 2022, and we expect the first hike to come in February. That's less than a year away, and if we are right, it could be more expensive to fix in a year's time, which supports the idea of fixing for longer now. See our Mortgage Borrowing Strategy.

Housing market overview

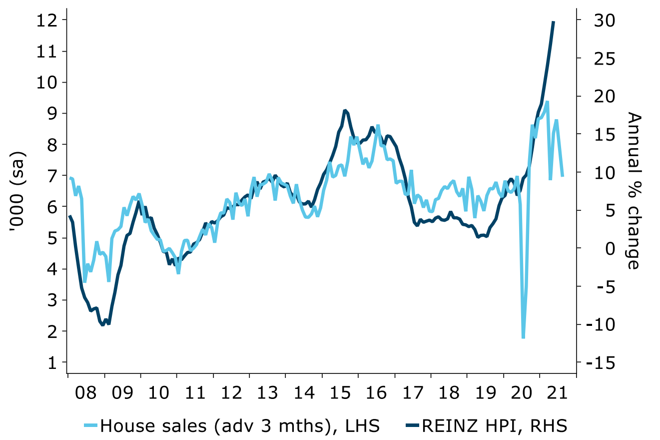
Summary

May housing data suggest recent Government policy announcements are weighing on overall housing activity. Sales fell 11.8% m/m in May (seasonally adjusted). But with listings also sparse, reduced investor demand hasn't yet been enough to slow the monthly pace of house price inflation. This came as a bit of a surprise and we have upgraded our near-term house price forecasts to include a little more momentum. We have also brought forward our expectation for OCR hikes by six months to February 2022. That means mortgage rates are expected to rise a little sooner than before, taking some of the steam out of the housing cycle a bit earlier.

Sales and inventories down, prices up

Housing data clearly show the market is going through an adjustment period following recent Government policy announcements. But exactly what things will look like when the dust settles remains uncertain. May data brought yet another significant monthly decline in house sales, down 11.8% m/m following a 10.4% decline in April (ANZ seasonal adjustment), suggesting overall activity is waning. And while sales tend to lead prices by around three months (figure 1), the acceleration in the pace of monthly house price inflation in May (1.8% m/m vs 1.5% in April) suggests house price momentum is holding up for now.

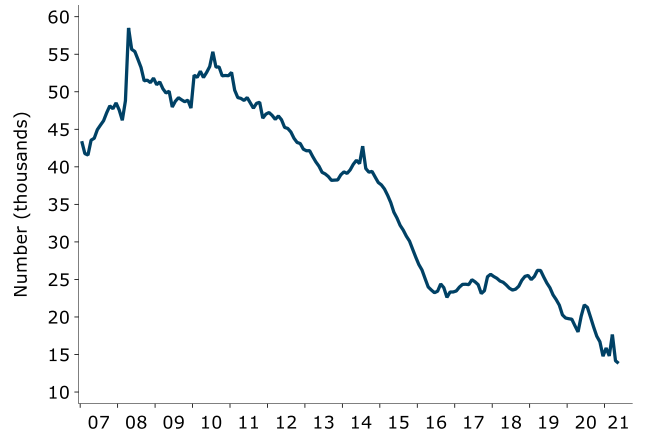
Figure 1. House price inflation and sales



Source: REINZ, Macrobond, ANZ Research

The significant decline in the number of properties available for sale in May (to very low levels by historical standards) goes a long way towards explaining the persistence of price pressures. Seasonally adjusted inventories fell 5.1% m/m in May following a 10.5% decline in April. Compared to a year ago, there were almost 30% fewer properties on the market for sale. A continuation of this trend (figure 2), represents an upside risk to our house price outlook (all else equal).

Figure 2. Number of properties available for sale

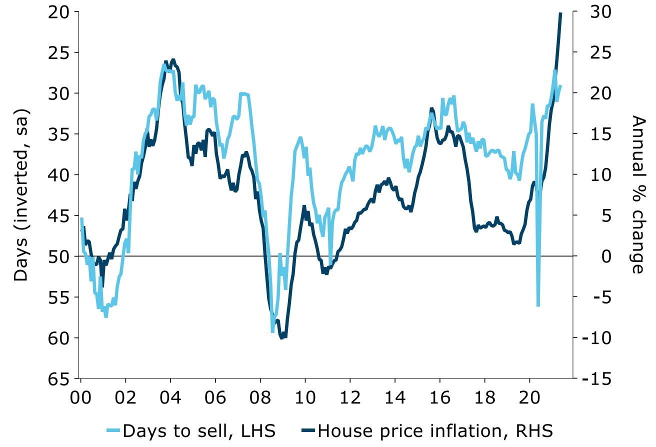


Source: RealEstate.co.nz, Macrobond

Overall, while there may well be fewer investors in the market following recent Government policy changes, there are also fewer houses available for those who are still looking. That appears to be keeping competition fierce and prices rising for now.

Indeed, tightness in the market has also been confirmed by the recent decline in the number of days it takes to sell a house – that fell by 1 day in May to 29, well below its historical average of 39 (figure 3).

Figure 3. House price inflation and days to sell

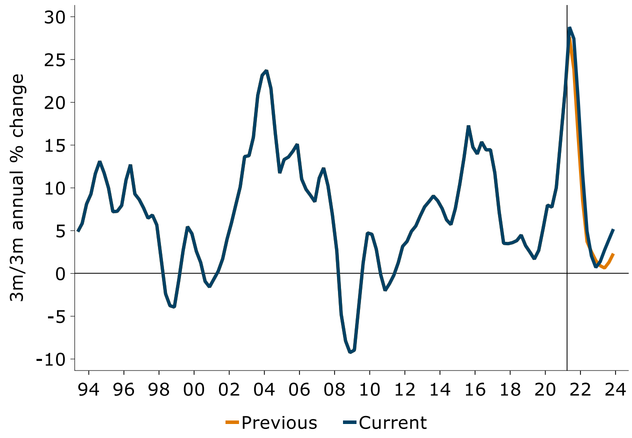


Source: REINZ, Macrobond, ANZ Research

A little more price momentum expected in the near term

House price inflation came in ahead of our expectation in May, and given the market continues to look very tight, we've baked a touch more momentum into our near-term forecast. But we have also recently pulled forward our expectation for OCR hikes by six months (we now expect the first hike in February 2022). This is expected to push mortgage rates higher, leading to an earlier trough in annual house price inflation than previously (Figure 4).

Figure 4. House price forecast

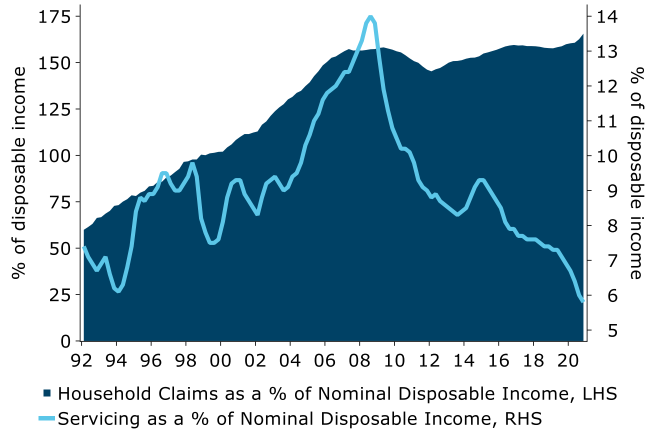


Source: REINZ, Macrobond, ANZ Research

As before, our house price forecasts reflect an expectation that Government policies, credit and affordability constraints, and tighter financial conditions will drive a moderation. But this is now balanced against a better economic outlook, and as we highlighted in last month's edition, an ongoing under-supply of housing, albeit one that's gradually improving with the borders closed.

With so many factors pushing and pulling on housing at the moment, risks around our outlook are wide-ranging. On balance, we think stronger-than-expected house price inflation is probably more likely than weaker, but the lion's share of the 'lower-probability, higher-impact' risks are skewed to the downside. Households' debt serviceability (figure 5) looks like it'll withstand 100 basis points or so of interest rate hikes, but all this debt accumulation means households are very susceptible to an income shock. And of course, even if higher debt servicing cost jumps aren't a problem in terms of households being able to meet mortgage payments, they can still crimp discretionary spending and therefore have an impact on the likes of the hospitality sector.

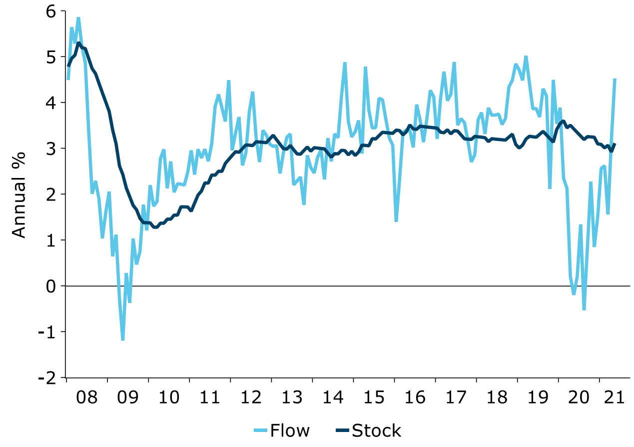
Figure 5. Household indebtedness and serviceability



Source: RBNZ, Macrobond

But it's not just house prices that have been on the up lately. Rent inflation is showing tentative signs of acceleration, with the 0.5% m/m in May the fastest monthly increase since March 2019. That's following a few months of average to sub-par rental inflation, meaning the annual change is nothing spectacular (up 3.1% y/y, within recent ranges) but this is certainly something worth keeping a close eye on over coming months. Higher-than-otherwise rents are a likely unfortunate side effect of recent Government tax policy changes, but the magnitude of the impact is unclear.

Figure 6. Rental price inflation



Source: Stats NZ, Macrobond, ANZ Research

Housing market overview

Housing market indicators for May 2021 (based on REINZ data seasonally adjusted by ANZ Research)

	Median house price			House price index		# of monthly sales	Monthly % change	Average days to sell
	Level	Annual % change	3-mth % change	Annual % change	3-mth % change			
Northland	$688,226	29.3	5.9	24.8	6.9	164	-28%	34
Auckland	$1,131,684	26.6	4.9	26.4	6.6	2,555	-11%	31
Waikato	$730,035	21.8	6.7	33.8	10.0	628	-19%	27
Bay of Plenty	$831,748	33.0	6.6	30.1	6.8	437	-11%	31
Gisborne	$638,528	49.7	18.2			49	+34%	33
Hawke’s Bay	$745,734	34.8	9.9	35.7	8.0	208	-6%	29
Manawatu-Whanganui	$584,184	38.8	8.6	52.1	9.6	273	-17%	24
Taranaki	$556,123	29.2	6.7	33.5	9.4	153	-13%	22
Wellington	$887,660	30.5	4.5	41.8	9.0	707	-9%	30
Tasman, Nelson & Marlborough	$723,637	22.4	6.7			186	-16%	28
Canterbury	$582,883	26.6	6.9	25.6	7.6	1,030	-10%	27
Otago	$677,273	33.2	6.5	24.0	4.8	363	-4%	30
West Coast	$291,534	33.6	4.8	28.8	8.1	59	+12%	31
Southland	$404,645	16.6	5.1	21.5	6.1	136	-16%	24
New Zealand	**$810,753**	**32.3**	**5.1**	**29.9**	**7.5**	**6,956**	**-12%**	**29**

Mortgage borrowing strategy

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Summary

Longer-term fixed mortgage rates continue to rise and are now well above lows seen earlier in the year. In contrast, shorter-term rates continue to edge lower, taking the average 1-year rate to yet another record low. Appealing as lower short-term rates are, they don't offer certainty for long. To echo the thoughts we have had for some months now, we think there is merit in considering fixing for longer, even if rates have risen slightly. Since our last edition, the RBNZ has signalled that they expect to hike the OCR in 2022, and we expect the first hike to come in February. That's less than a year away, and if we are right, it could be more expensive to fix in a year's time, which supports the idea of fixing for longer now.

Our view

Mortgage rates have continued grinding slowly higher, with 3 and 5-year rates now 0.12%pts and 0.33%pts above where they were a month ago respectively, and 0.23%pts and 0.63%pts above their respective lows. This move was sparked by an earlier move in wholesale rates, with mortgage rates catching up. In contrast, 6-month and 1-year rates have continued to fall, taking the latter to a new record low. Although the fall in the average 6-month rate was bigger, this rate isn't seen by most borrowers as attractive, and we share those sentiments, with the 1-year rate both lower and offering increased time certainty.

Pleasing as it may be for borrowers to observe falls in shorter-term rates, the trouble is, these rates don't offer certainty for long, and at the moment, that's likely to be what people want. Given our expectation that the RBNZ will lift the OCR sooner rather than later (with the first hike likely in February), we think that certainty is of greater-than-usual value at present. Households have collectively been very savvy borrowers since 2008, having kept their fixed terms short, allowing themselves to re-fix at ever cheaper rates as interest rates have fallen. However, that strategy starts to come unstuck as interest rates rise, and to echo comments made over the past few months, we think it is worth considering fixing for a longer term, even if it costs more. In short, we worry that simply selecting the cheapest rate now could work out to be more expensive in the long run.

Before we get into the analysis, it is worth spending a little more time talking about the RBNZ, and the US equivalent, known as the Federal Reserve (the "Fed"). That's because since our last edition, both of these central banks have forecasted that they may lift their respective cash rates in 2022 or 2023. And that matters a lot, because what the RBNZ does directly affects shorter-term rates, and what the Fed does tends to affect longer-term interest rates (because global financial markets are highly correlated). Regular readers will be aware that we at ANZ have been calling for RBNZ OCR hikes for a little while now, so what's all the fuss? Well, it's mostly that wholesale markets have really started to take note now that both the RBNZ and the Fed have themselves suggested they might hike. And in both cases, the hikes they signalled were more than what markets were pricing in, causing interest rates to lift in response.

So, what does breakeven analysis show? Let's compare, say, a string of back-to-back 1-year fixes to the 2-year and 3-year. Breakeven calculations show that the 1-year rate would need to remain below 2.97% in 1 years' time and 3.81% in 2 years' time in order for the back-to-back strategy to be cheaper over 2 and 3 years. That implies that the 1-year rate needs to rise by 0.78%pts over the next year and a further 0.84%pts the following year. That's more than we expect the OCR to rise by over the next year (we expect 0.25%pt hikes in both February *and* May). So the maths doesn't fully validate fixing for longer. However, it isn't far off, and if you are worried that the RBNZ might hike sooner rather than later (or faster), or you value certainty, a longer term could be worth considering for at least a portion of your debt.

Figure 1. Carded special mortgage rates^

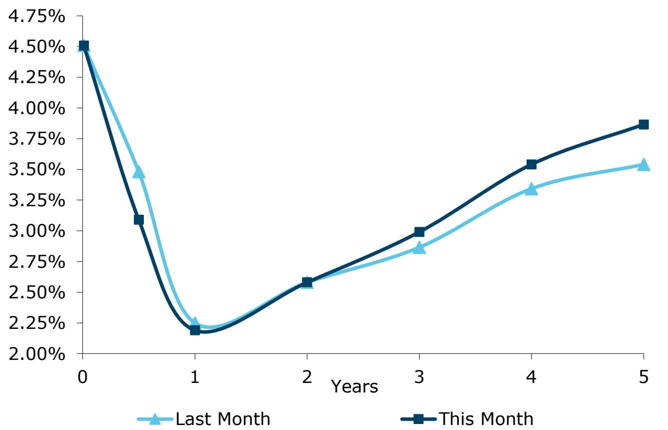

Table 1. Special Mortgage Rates

		Breakevens for 20%+ equity borrowers			
Term	Current	in 6mths	in 1yr	in 18mths	in 2 yrs
Floating	4.51%				
6 months	3.09%	1.29%	2.78%	3.17%	3.61%
1 year	2.19%	2.03%	2.97%	3.39%	3.81%
2 years	2.58%	2.71%	3.39%	3.93%	4.50%
3 years	2.99%	3.29%	3.99%	4.36%	4.72%
4 years	3.54%	3.78%	4.28%		
5 years	3.87%	#Average of "big four" banks			

^ Average of carded rates from ANZ, ASB, BNZ and Westpac.

Source: interest.co.nz, ANZ Research

Key forecasts

Weekly mortgage repayments table (based on 25-year term)

	Mortgage Rate (%)													
Mortgage Size ($000)	2.00	2.25	2.50	2.75	3.00	3.25	3.50	3.75	4.00	4.25	4.50	4.75	5.00	5.25
200	196	201	207	213	219	225	231	237	243	250	256	263	270	276
250	244	251	259	266	273	281	289	296	304	312	320	329	337	345
300	293	302	310	319	328	337	346	356	365	375	385	394	404	415
350	342	352	362	372	383	393	404	415	426	437	449	460	472	484
400	391	402	414	426	437	450	462	474	487	500	513	526	539	553
450	440	453	466	479	492	506	520	534	548	562	577	592	607	622
500	489	503	517	532	547	562	577	593	609	625	641	657	674	691
550	538	553	569	585	601	618	635	652	669	687	705	723	741	760
600	587	604	621	638	656	674	693	711	730	750	769	789	809	829
650	635	654	673	692	711	730	750	771	791	812	833	854	876	898
700	684	704	724	745	766	787	808	830	852	874	897	920	944	967
750	733	754	776	798	820	843	866	889	913	937	961	986	1,011	1,036
800	782	805	828	851	875	899	924	948	974	999	1,025	1,052	1,078	1,105
850	831	855	879	904	930	955	981	1,008	1,035	1,062	1,089	1,117	1,146	1,174
900	880	905	931	958	984	1,011	1,039	1,067	1,095	1,124	1,154	1,183	1,213	1,244
950	929	956	983	1,011	1,039	1,068	1,097	1,126	1,156	1,187	1,218	1,249	1,281	1,313
1000	978	1,006	1,035	1,064	1,094	1,124	1,154	1,186	1,217	1,249	1,282	1,315	1,348	1,382

Mortgage rate projections (historic rates are special rates; projections based on ANZ's wholesale rate forecasts)

	Actual			Projections						
Interest rates	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
Floating Mortgage Rate	4.6	4.5	4.5	4.5	4.5	4.5	4.8	5.0	5.0	5.3
1-Yr Fixed Mortgage Rate	2.6	2.5	2.3	2.3	2.4	2.6	2.8	2.9	3.1	3.2
2-Yr Fixed Mortgage Rate	2.7	2.6	2.6	2.6	2.7	2.9	3.2	3.3	3.4	3.5
5-Yr Fixed Mortgage Rate	3.1	3.0	3.0	3.3	3.5	3.7	4.0	4.1	4.2	4.3

Source: RBNZ, ANZ Research

Economic forecasts

	Actual			Forecasts						
Economic indicators	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
GDP (Annual % Chg)	0.4	-0.8	2.4	15.3	1.8	3.6	2.8	3.4	3.8	3.9
CPI Inflation (Annual % Chg)	1.4	1.4	1.5	2.8	3.0	2.9	2.5	2.2	1.9	1.9
Unemployment Rate (%)	5.2	4.9	4.7	4.7	4.7	4.7	4.6	4.4	4.2	4.0
House Prices (Quarter % Chg)	4.3	7.8	7.8	6.3	3.2	1.7	0.1	-0.1	0.3	0.3
House Prices (Annual % Chg)	10.0	15.7	21.3	28.8	27.4	20.1	11.6	4.9	2.0	0.7

Interest rates	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
Official Cash Rate	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.75	0.75	1.00
90-Day Bank Bill Rate	0.31	0.27	0.35	0.33	0.36	0.56	0.82	0.90	1.07	1.15
10-Year Bond	0.50	0.99	1.81	1.80	2.00	2.25	2.50	2.75	2.75	2.75

Source: ANZ Research, Statistics NZ, RBNZ, REINZ

Contact us

Meet the team

We welcome your questions and feedback. Click here for more information about our team.

Sharon Zollner
Chief Economist

Follow Sharon on Twitter
@sharon_zollner

Telephone: +64 27 664 3554
Email: sharon.zollner@anz.com

General enquiries:
research@anz.com

Follow ANZ Research
@ANZ_Research (global)

David Croy
Senior Strategist

Market developments, interest rates, FX, unconventional monetary policy, liaison with market participants.

Telephone: +64 4 576 1022
Email: david.croy@anz.com

Susan Kilsby
Agricultural Economist

Primary industry developments and outlook, structural change and regulation, liaison with industry.

Telephone: +64 21 633 469
Email: susan.kilsby@anz.com

Liz Kendall (maternity leave)
Senior Economist

Research co-ordinator, publication strategy, property market analysis, monetary and prudential policy.

Telephone: +64 27 240 9969
Email: elizabeth.kendall@anz.com

Miles Workman
Senior Economist

Macroeconomic forecast co-ordinator, fiscal policy, economic risk assessment and credit developments.

Telephone: +64 21 661 792
Email: miles.workman@anz.com

Finn Robinson
Economist

Macroeconomic forecasting, economic developments, labour market dynamics, inflation and monetary policy.

Telephone: +64 21 629 553
Email: finn.robinson@anz.com

Kyle Uerata
Economic Statistician

Economic statistics, ANZ proprietary data (including ANZ Business Outlook), data capability and infrastructure.

Telephone: +64 21 633 894
Email: kyle.uerata@anz.com

Natalie Denne
PA / Desktop Publisher

Business management, general enquiries, mailing lists, publications, chief economist's diary.

Telephone: +64 21 253 6808
Email: natalie.denne@anz.com

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