REFERRER NEWS

with Tony Alexander

Housing Policies to accentuate a slowing market

Late in 2017 Labour won the general election and made many promises with regards to improving many things, including housing affordability. But since September of that year, we have seen these developments.

· House prices on average have risen 32%.

· Rents on average have risen 30%.

· The state house waiting list has grown from 5,000 to 23,000.

· The proportion of dwellings being sold to investors with mortgages has risen from 24% to 30%.

Housing goals for the government have not only not been met, the starting points for all the things they want to achieve have become a lot worse. Because of this, and the extreme 14% rise in average house prices over the past five months (over 30% annualised), the government has promised to announce a range of measures aimed at curtailing housing demand and boosting supply.

Supply-side policies are likely to be announced in the Budget due in May, but unless most controls are removed on land use it is very unlikely much acceleration in the pace of construction will be able to be achieved. It is worth noting however that since September 2017 the annual number of consents issued for the construction of new dwellings has risen from 30,000 to almost 40,000.

It is on the demand side that the government is likely to continue to focus its attention, despite the fact that all policies which have done so over the past two decades have failed to stop house prices rising strongly. The Budget will likely contain some policies, and in mid-March the Finance Minister will announce something new.

New Reserve Bank Instruction

But already we have seen the Finance Minister attempt to make a big change through issuing a new instruction to the Reserve Bank on February 25. When setting its policies, the Reserve Bank must now take into account the government's housing policies – specifically around affordability for first home buyers and reducing purchasing of existing properties by investors.

Does this mean higher interest rates? After all, it is largely because mortgage and deposit rates are at record lows that demand for property from investors has surged. No.

The official cash rate will continue to be set to achieve goals on inflation and employment. Responsibility for achieving housing goals will be left in the hands of other tools. Already one of those tools is well known – Loan to Value Ratios (LVRs).

There is a chance the 40% minimum deposit for investors will be lifted to 50% if investor demand remains rampant in the next few months. There is also a chance that new rules on interest-only lending by banks to investors will be introduced.

The Finance Minister has asked the Reserve Bank to give him information on such rules and how they could be restricted to affecting only investors. The Minister has also asked for advice on how Debt to Income rules (DTIs) could be introduced and structured to again affect only investors.

Momentum is Turning

What actually happens and when we shall simply have to wait and see. But one strong rule of thumb when it comes to implementing government policies is that they have their best impact if well explained and if the target is moving in the desired direction in the first place. Momentum counts for a lot – or strike while the iron's hot one might say – and in this case of the residential real estate market we can see some early signs of things easing slightly.

Each month I conduct a number of surveys of the 18,000 people signed up to receive the weekly Tony's View publication, and of two subsets in particular. One of those subsets is people that I have been able to identify as mortgage advisers.

In the most recent mortgages.co.nz & Tony Alexander Real Estate Survey a net 5% of advisers said that they are seeing fewer investors coming forward looking for advice. This was a substantial turnaround from a net 24% in January seeing more investor enquiries and the first time that this measure has been negative since the survey started in June last year.

Another subset I survey is real estate agents and in the March REINZ & Tony Alexander Real Estate Survey a net 5% of agents said that they are seeing more investors coming forward looking to sell a property. This is the first time that this measure has been positive since the survey started in June, though the turnaround from a net 2% seeing fewer investors looking to sell in February and 7% in December is not that substantial.

But there are some other measures in the survey with REINZ showing some easing.

A net 15% of agents said that they are seeing more investors in the market looking to buy. This means growth – but the speed of that growth is slowing. In the February survey a net 31% of agents said that they were seeing more investors, in December 45%, and in November 59%.

From the survey we can also see that the speed of increase in first home buyers coming forward to make a purchase is easing. In March a net 32% of agents were seeing more first home buyers, down from a net 46% in February, 50% in December, and 64% in November.

And finally, the survey also tells us that in March, when asked why investors are looking to buy, a gross 10% of agents said they aren't – that they are instead looking to sell. This was the highest result so far and up from 7% in February and 3% in December.

But we also have the official data on real estate activity released by REINZ telling us of some easing in the speed of growth. During January average house prices around the country increased by 1.3%. In December the rise was 2.2%, and in November 3.9%. The pace of price growth has been slowing for two months.

Further, whereas in November nationwide property sales were 34% ahead of a year earlier, and in December growth was 46%, in January annual growth was only 3%.

None of these measures mean that the market is going backwards. But they do suggest that if the government and perhaps Reserve Bank use the next few weeks and months to mid-year to warn about the need for further easing and the potential for anti-investor policies, the actual requirement for new punitive policies may not be great.

Having said that, as noted above, it would be reasonable to think that if the market is still fairly active mid-year that the 40% minimum deposit for investor buyers borrowing from a registered bank could rise to 50%. And we could easily see some restrictions on interest-only lending to investors. Plus, there is the mid-May Budget to come and that could easily contain an extension of the Brightline test from five years to ten, along with some measures (better understood by accountants than economists) reducing the after-tax returns of investors.

Will any of the measures to come cause house prices to fall on average? That is very unlikely. The Prime Minister last year noted that the constituency for rising house prices is greater than the numbers favouring house price falls. Plus, house price falls tend to be associated with economic weakness and job loss and the government and Reserve Bank will not want to do anything which disturbs the economy's post-lockdown recovery.

In particular, the government will not want to make changes so drastic as to make people fearful of falling prices because that will cause orders for new houses to decline.

All up, we can see early, tentative, signs that the frenzy in residential real estate activity and prices growth is ending. The government primarily, and the Reserve Bank almost reluctantly, are likely to look to hasten the pullback of investors over the remainder of this year.

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By Tony Alexander