New Zealand Property Focus

Playing by the rules

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Summary

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

Feature Article: Playing by the rules

The rules and regulations governing the New Zealand rental property market have undergone a number of changes over the past few years, and it looks like more are on the way. Law changes have generally focused on improving the lot of renters and first home buyers. And while some, such as the Healthy Homes Standards, have broader economic benefits (eg fewer sick days), there's no such thing as a free lunch. Higher-than-otherwise rents and a lower-than-otherwise stock of rental properties are costs that from a social perspective are just as difficult to quantify as the benefits. But for now, let's look at the coal face; at how some of the rules have changed for residential property investors, and how they might change further. Given some of the costs of non-compliance, it is pretty important stuff of which to be aware. Regarding their impact on the housing market (and the economy more broadly), we think policy changes have been – and will remain – a key headwind. But the fundamentals (a shortage of houses and downward pressure on mortgage rates), suggest there are enough supports out there to keep things from rolling over.

Property gauges

Regional divergences remain a key theme in New Zealand's housing market. Auckland house price growth slipped further into negative territory in June. House price inflation in the capital is still high but falling back in line with the rest of the pack. Canterbury inflation has made a small run back into positive territory and some of the small centres, like Manawatu-Whanganui and the deep south, are seeing prices tick up again. House price inflation isn't expected to roll over at the national level as OCR cuts should help keep mortgage rates under pressure, LVR restrictions will likely be loosened gradually and supply shortages remain. Conversely, several headwinds are capping the upside: banks are cautious and LVR limits remain binding; investors are wary of policy changes; and affordability constraints are biting.

Economic overview

The synchronised slowdown in global growth has become more pronounced, against a backdrop of below-target inflation in many economies. Major central banks are to set to ease policy rates further, but many have little monetary policy ammunition to spare. Back home, the direct impacts of slower global growth on the New Zealand economy have so far been muted. But confidence effects are likely weighing on business sentiment, employment and investment intentions. Domestic growth looks set to trough at 2% in Q2, but the outlook from there is murky. Fiscal and monetary stimulus should provide a bit of a boost, which we expect will support a gradual acceleration in growth. But downside risks are heightened. The inflation outlook is troubling – we've likely seen the peak in domestic inflation pressures, and more is needed from the RBNZ to help met their employment and inflation objectives. We think cuts in August and November, taking the OCR to 1%, should do the trick.

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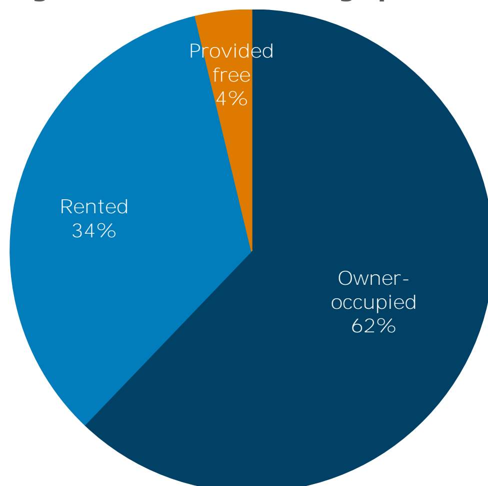
Playing by the rules

There are an estimated 650,000 rented dwellings in New Zealand, making up just over a third of all private dwellings (figure 1). This share has been steadily increasing for quite some time, lifting from 30% 10 years ago and just 28% 20 years ago, as the home ownership rate has fallen. Seen in this context, there are a fair number of people out there who need to be aware of the changing landscape regarding the rules and regulations governing the rental property market.

Figure 1. Private dwellings provision



Source: Statistics NZ, ANZ Research

This month we take a look at some of the recent policy changes and discuss how the rules might change in the not too distant future.

The regulatory backdrop has changed…

First up, let's take a look at some of the significant changes to legislation from the past few years.

The Residential Tenancies Act was amended in June 2016 to make rental properties safer and healthier by requiring smoke alarms and insulation. The smoke alarm requirement is hardly a game changer from a property **investor's point of view**, given the fact that **smoke alarms don't cost an arm and a leg,** and having an alarm installed was already best practice – smoke alarms not only protect the occupants, they also reduce the risk of significant fire damage. That said, there are now very specific requirements and responsibilities, which if not met could see the landlord fined up to $4,000. Conversely, tenants can be fined up to $3,000 for not meeting their responsibilities too**, so it's important that both parties** are aware of this one.

Complying with insulation regulations requires a bit more effort. For private rental properties, both ceiling and underfloor insulation needed to be installed by 1 July 2019 (where reasonably practicable). For many social housing properties, insulation has been mandatory since 1 July 2016. Landlords are now also required to include a signed insulation statement with all tenancy agreements, specifying what insulation the property has and where it is. Those who fail to comply with the insulation standards are liable for exemplary damages of up to $4,000, so the incentive for landlords to tick this box is reasonably high, given the cost to insulate a home (in most cases) **isn't** too different to the cost of non-compliance.

Feature Article: Playing by the rules

Going further than the aforementioned insulation requirements, Residential Tenancies (Healthy Homes Standards) Regulations 2019 became law on 1 July 2019. The Healthy Homes Standards sets minimum requirements for rental properties on a few fronts:

- **Heating**. Heating must be provided. A heating assessment tool has been set up to help calculate heating requirements for the living room in a rental.
- **Insulation.** The 2016 insulation requirements remain in force, but there is additional material, such as further detail on where exemptions apply.
- **Ventilation**. Covers requirements around windows, doors, extractor fans, and rangehoods.
- **Moisture ingress**. Includes the requirement for an on-ground moisture barrier if the rental property has an enclosed subfloor space.
- **Drainage**. The standards reinforce existing law that says landlords must have adequate drainage and guttering.
- And **draught stopping**. Gaps or holes in walls, ceilings, windows, floors and doors that cause unreasonable draughts must be blocked. This includes blocking the fireplace or chimney of an open fireplace unless the tenant and landlord agree otherwise in writing.

There are different compliance dates for the above Standards depending on property type. But for private landlords, come July 2021 they'll need to ensure their rental properties comply with the Standards within 90 days of any new (or renewed) tenancy. All rental properties need to comply by July 2024.

Despite having some time up their sleeve to comply with the Standards, there are some things landlords should already be doing. From July 2019, landlords are required to keep records that demonstrate compliance with any healthy homes standards that apply or will apply during the tenancy. They must also include a separately signed statement of intent to comply with the Standards in any new, varied or renewed tenancy agreement. Should a landlord fail to comply, the tenant can apply to the Tenancy Tribunal for mediation. The Tribunal can order the landlord to undertake work to rectify the issue and impose financial penalties of up to $4,000 payable to the tenant.

Then came the Residential Tenancies (Prohibiting Letting Fees) Amendment Act 2018, which, you guessed it, prohibits landlords, property managers etc from charging the tenant a fee for services rendered in relation to tenancy (including granting new tenancies, extensions, renewals and other variations). This one took effect in December 2018. While the costs of advertising, showing, vetting and validating potential tenants is not zero, it is not clear why they should be the new tenants' responsibility. Further, some argued that the typical fee of one week's rent was disproportionate to these costs, and was a possible way of exploiting the situation when rental demand exceeds supply. Now these costs will be incurred directly by the landlord – and likely at least partially recouped by lifting the amount of rent charged. Those found breaking this rule could be liable for up to $1,000 in exemplary damages.

Taxation rules have also changed:

- From 29 March 2018, the bright-line test was extended from two years to five years. Effectively, this policy imposes a capital gains tax on residential investment property sold within five years of its purchase date.
- From April 2019, landlords were no longer able to offset residential rental property losses against their other income, such as salaries and wages. In other words, rental property losses are now "ring-fenced" and losses should therefore be carried forward to the following year to be offset against income derived from the rental property.

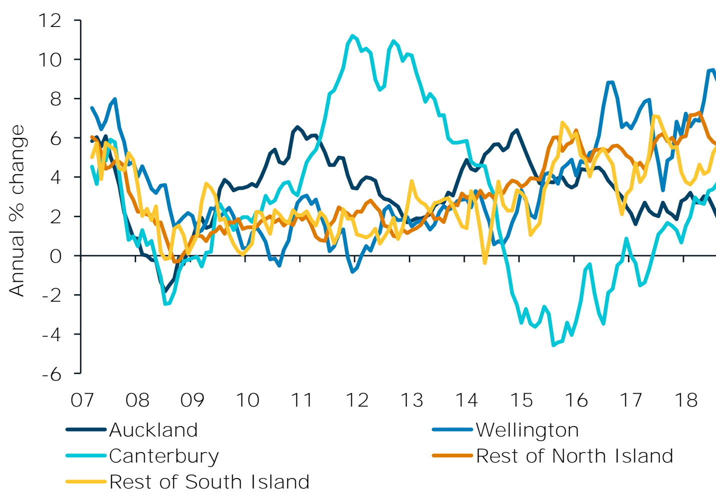
In addition to above, the Health and Safety Work Act 2015 came into force in April 2016, with implications for residential landlords. Under the Act a residential landlord is considered a Person Conducting a Business or Undertaking (PCBU) and therefore must ensure "as reasonably practicable" the health and safety of workers and others within this "workplace". A residential rental property is not always considered a workplace, but it will be when renovations or repairs or even commercial cleaning are undertaken on the premises. And while the landlord is not responsible when the tenant is conducting their own business on the premises, they are if that tenant is working for the landlord. The bottom line here is that residential landlords need to be familiar with their duties and obligations under this piece of legislation. After all, ignorance of the law is no excuse and most rental dwellings will undergo maintenance, repair or renovation at some point. The stakes are high on this one, as an offence of reckless conduct in respect of duty could lead to imprisonment and/or a 6 or even 7 figure fine.

Anecdotally, we often hear that the costs associated with policy changes are putting upwards pressure on rents. **But looking at the regional data, there's no obvious synchronised bump across the regions that you** might expect to see in the event of a significant policy-induced cost shock (figure 2).

However, there are many reasons why this could be the case**, meaning an impact can't be ruled out**. Policy changes have been staggered in terms of both their effective date and when they were first signalled by policy makers, and landlords have some flexibility in terms of how (and how much) they pass through higher costs. **And for some landlords, policy changes wouldn't have changed much anyway because their properties were** compliant before changes were made.

Further, regional markets have had their own housing cycles to account for, particularly Christchurch, which suffered a significant drop in rental supply as a result of the Canterbury earthquakes. The macroeconomic fundamentals need to be accounted for too. Migration-led population growth has boosted housing demand significantly in recent years, which alongside relatively constrained supply has put upward pressure on rents (and house prices). Disentangling this impact from policy impacts is nigh-on impossible given the timing and complexity of policy changes and the fact that migration data is now rather noisy.

Figure 2. Regional rents (new bonds lodged)



Source: Stats NZ, ANZ Research

...and it looks like more changes are on the way

A number of additional changes to the Residential Tenancy Act have been proposed. The consultation period for this is now closed, with landlords and possibly would-be property investors waiting for decisions to be announced.

Some of the more significant proposed changes include:

- Ending no-cause terminations (ie removing the ability for a la**ndlord to issue a "no fault" 90**-day termination notice to the tenant). This is one of the more significant proposed changes, particularly given the process a **landlord needs to follow to prove a tenant is "at fault"** can be both a lengthy and uncertain one.
- Increasing the amount of notice (from 42 days to 90) that a landlord must generally provide tenants to terminate a tenancy in the event of sale or if the landlord requires the property for personal use.
- Rules around rent-setting, including:
  - Limiting rent increases to once per year;
  - Prohibitions **on the practice of 'rent bidding'**;
  - Introducing a **"fair rent" determination process**;
  - Clarifying when tenants can challenge rent increases at the Tenancy Tribunal.
- Tenants' rights and obligations regarding pets. Clarifying the circumstances under which tenants should be allowed to keep pets and the protections the landlord has if they do.
- Making it easier for tenants to make non-structural modifications and alterations to a rental property.

- Possible changes to fixed-term agreements to improve security of tenure, including:
  - Providing tenants with a right to extend their fixed-term agreement;
  - Setting minimum tenancy durations; or
  - Introducing open-ended tenancies

In addition to above, the Residential Tenancies Amendment Bill (No. 2) contains proposed changes to the Residential Tenancy Act, including:

- Changes to how much a tenant should be liable for damage (including careless damage), proposing liability be limited to the lesser of 4 weeks rent or the amount of insurance excess.
- The requirement for a Tenancy Agreement to include a written statement covering:
  - Whether the premises is insured;
  - The amount of the insurance excess;
  - What the property is insured against; and
  - What actions by the tenant/s would void insurance cover
- Changes around property contamination, including landlord rights around entering, testing, and terminating a tenancy if contaminated. And also prohibiting offering contaminated premises for rent.
- Changes around Unlawful Residential Premises (eg dwellings constructed for a purpose other than living in, such as a garage, or which do not comply with building health and safety legislation) that give the Tenancy Tribunal jurisdiction to order refunds, damages, work orders to upgrade, or terminate the tenancy.

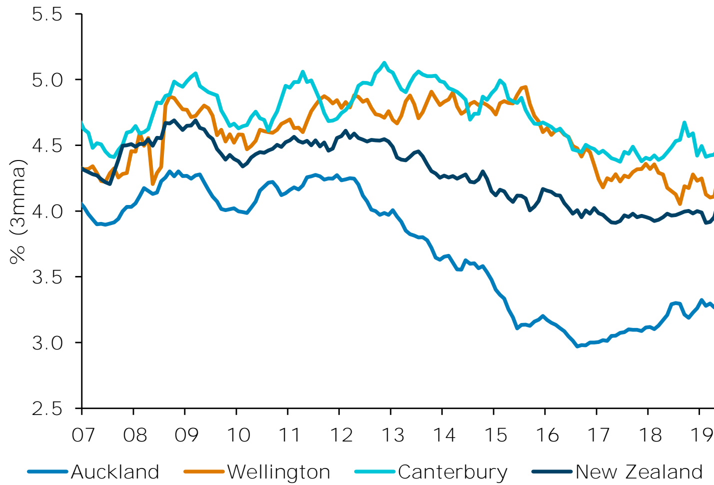
The recent and proposed rule changes listed above are by no means an exhaustive list of what's going on in this space, but we have tried to be thorough. One thing's for sure, residential property investors certainly have a lot to stay on top of to ensure they're playing by the rules – a possibly daunting task for smaller-scale 'mum and dad' type investors.

Indeed, we think the policy landscape is already deterring some investors. While this decreased demand will be weighing on house price inflation (and therefore making houses more affordable than otherwise for first home buyers), it could also be reducing the incentive to build new houses, and that's not a great outcome in what's already widely touted as an under-supplied housing market.

And in the very long run (once supply has had a chance to catch up, policy impacts have been worked through, and credit and affordability are less of a headwind), the law of supply and demand tells us that a lower-than-otherwise supply of housing will result in a higher-than-otherwise price of houses. In other words, the near-term dampening price impacts are not a sustainable solution to housing affordability. But it will at least give incomes a chance to play catch-up.

All that said, these policy changes certainly don't mean it's the end of traditional residential property investment altogether. Through a mix of lower property prices (in the near term) and higher-than-otherwise rents, rental yields will likely adjust to a point that justifies investing – this point may just need to be a little higher than previously. In fact, falling house prices in Auckland are already improving the implied rental yield in the region (figure 3), but there will be substantial variances between locations and properties within the region. In addition, making analysis more complicated, some of the policy changes are difficult to assign a cost to (eg the additional return on investment a would-be investor might require to forego their ability to terminate a tenancy at their discretion).

Figure 3. Rental yields



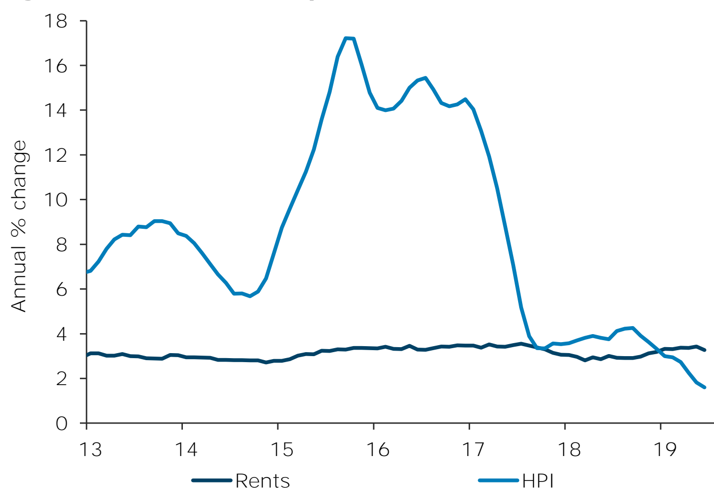
Source: REINZ, Stats NZ, ANZ Research

As well as seeing some investors leave (or not enter) the market, another possible implication of an increasingly complex regulatory backdrop is that it could see a swing towards greater corporatisation of the rental market – fewer 'mum and dad' type landlords and more 'only available during office hour' landlords.

All up, when considered alongside other policy changes and settings, such as the banning of foreign buyers and LVR restrictions, the overall policy landscape does appear to be quite a significant headwind to house price inflation at present – but one that is difficult to account for with econometric modelling. (Of course, the RBNZ can (and probably will in November) loosen LVR restrictions, but we think this will happen only gradually). We think the lengthy list of policy changes, alongside ongoing affordability and credit headwinds, will prevent national house price inflation from taking off any time soon – despite recent declines in mortgage rates and the Government taking a broad-based capital gains tax off the table. However, the fundamentals supporting demand (such as modestly rising household incomes and low interest rates), combined with a shortage in supply, should keep the housing market from rolling over.

But it does appear the recent trend of rents inflation outpacing house price inflation is set to continue for a while yet (figure 4). And that implies some gradual uplift in rental property yields.

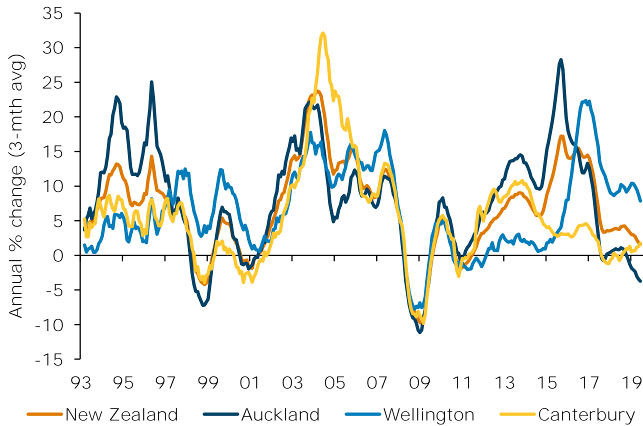
Figure 4. Rent and house price inflation



Source: REINZ, Stats NZ, ANZ Research

Property Market in Pictures

Figure 1. Regional house price inflation

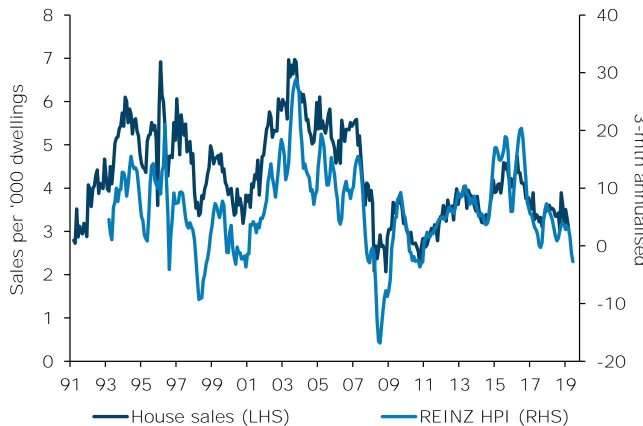


Source: ANZ Research, REINZ

Annual house price inflation moderated further, reaching 1.6% y/y (3mma) in June, having started 2019 with 3% y/y growth. We had expected the firming in prices in late 2018 would prove short-lived and that headwinds weighing on the market would see prices continue their gentle descent, and this has proven to be the case.

House price profiles in the main centres remain quite diverse. Auckland is the epicentre of the price declines, with annual growth contracting further to 3.7% y/y. Wellington prices eased to 7.8% y/y while prices in Canterbury have lifted slightly to be up 1.7% y/y – its highest growth rate since mid-2017.

Figure 2. REINZ house prices and sales

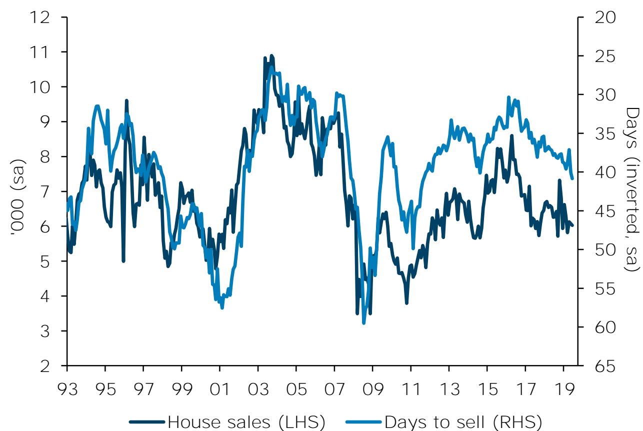


Source: ANZ Research, REINZ

Sales volumes and prices tend to be closely correlated, although at times tight dwelling supply can complicate the relationship.

Seasonally adjusted house sales fell 0.8% in June for the second consecutive month and the fourth in the last six months. The data continued to slow and the 12% January lift – boosted by the RBNZ's relaxation of LVR restrictions – has now fully reversed. House sales remain at a low level, consistent will low house price inflation. On the whole, sales growth has declined 6% y/y with Auckland falling 11% (the most significant decline among all regions). Outside of Auckland, sales are down 3.3% y/y.

Figure 3. Sales and median days to sell



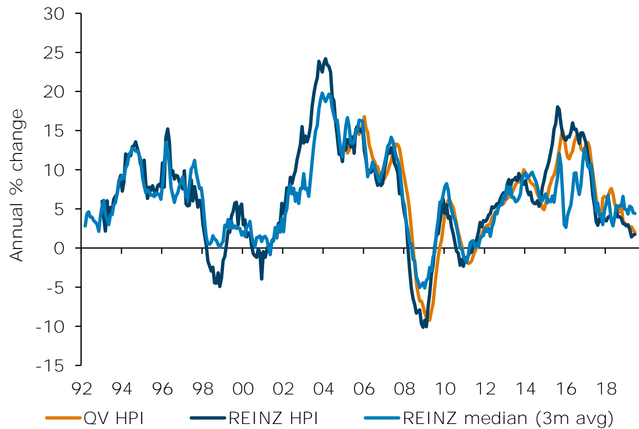
Source: ANZ Research, REINZ

How long it takes to sell a house is also an indicator of the strength of the market, encompassing both demand and supply-side considerations. Larger cities tend to see houses sell more quickly, but deviations in a region from its average provide an indicator of the heat in a market at any given time.

Days to sell are now at 41 days in aggregate, indicating continued loosening in the previously tight housing market. Regional divergences are evident, but the momentum is for longer, particularly in the main centres. The Auckland market in particular shows signs of slack. The days to sell measure lifted again in June to 45 days – above the historical average of 36. Slack around this level suggests that weakness in prices may continue for a while yet.

Property Market in Pictures

Figure 4. REINZ and QV house prices

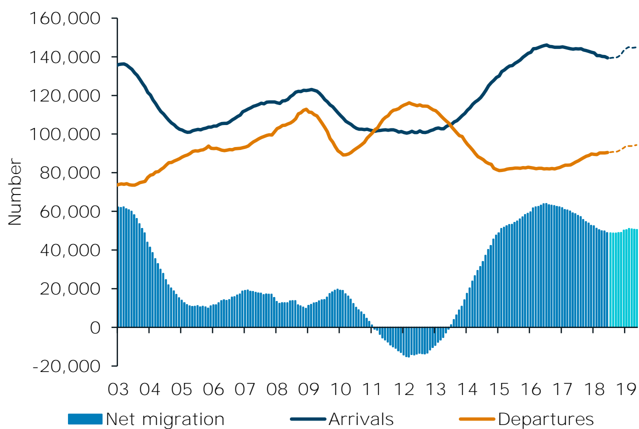


Source: ANZ Research, REINZ, QVNZ

There are three monthly measures of house prices in New Zealand: the median and house price index measures produced by REINZ, and the monthly QVNZ house price index. The latter tends to lag the other measures as it records sales later in the transaction process. Moreover, movements do not line up exactly, given differing methodologies (the REINZ house price index and QVNZ measures attempt to adjust for the quality of houses sold).

The REINZ HPI – our preferred measure – is sitting at 1.6% y/y (3mma) in June. The QVNZ measure has moderated even further and is sitting at 2.3% y/y. The REINZ median remained within recent ranges, with annual growth of 6.2%. Since the median does not control for composition, the higher growth rate may reflect a rising proportion of high-value sales.

Figure 5. Annual migration*



Source: Statistics NZ

*Dotted lines show the last nine months of data, which we look through because they are subject to substantial revisions. The data prior to June 2014 is back-casted using Stats NZ's discontinued experimental data.

Migration flows to and from New Zealand are one of the major drivers of housing market cycles. The early-1970s, mid-1990s, mid-2000s and most recent house price booms have coincided with large net migration inflows.

Annual net migration reportedly eased slightly to 50,500 in May, but Statistics NZ's data is subject to substantial revision and is relatively untested, so we would caution about reading too much into it. The most recent data saw substantial revisions to annual net migration (April was first reported as a rise to 55,900, but was revised to 50,700 in May). To avoid unnecessary noise in our economic outlook we're now forecasting net migration with a nine-month lag.

The older, more reliable data suggest the cycle was still easing towards the end of 2018. And we think this gradual easing trend has continued into 2019.

Figure 6. Residential building consents

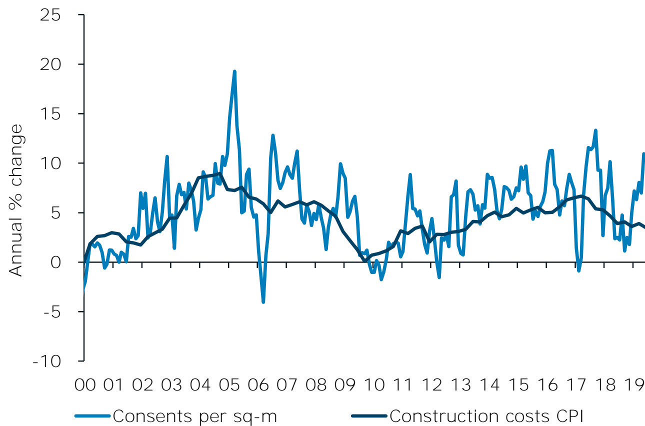
Source: ANZ Research, Statistics NZ

Residential building consents continued along their upward trajectory in May. The data are volatile, particularly for multi-unit dwellings. Given construction firms' activity expectations have turned sour of late, we'll be watching this one closely. Annual consent issuance is still strong, running at 34,700, just above the previous mid-2000s peak (33,200). Growth in Auckland consents drove the strength, with annual consents up over the 14k mark.

Overall, housing demand should be supportive of further construction activity. However, capacity constraints are being felt and the construction industry is facing profitability challenges, which we expect will make it difficult for issuance to push higher.

Property Market in Pictures

Figure 7. Construction cost inflation

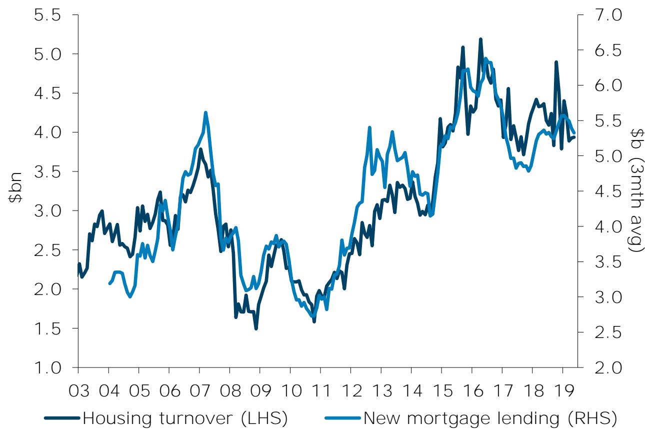


Source: ANZ Research, Statistics NZ

Construction cost inflation has softened since 2017 and we don't expect it to reach the dizzying heights (6.7% y/y) achieved over 2016-2017. That said, growth in the cost of consented work per square metre – a proxy – did pop up to 10.9% y/y (3mma) in May, following a period of weakness in 2018. This compares with CPI construction cost inflation of 3.5% y/y in the June quarter.

Capacity pressures in the industry remain acute, which should continue to support price rises. But with construction growth slower than in recent years, and caution among firms, we don't expect construction cost inflation to surge higher from here.

Figure 8. New mortgage lending and housing turnover



Source: ANZ Research, RBNZ

New residential mortgage lending figures are published by the RBNZ. These are gross (rather than net) flows and can provide leading information on household credit growth and housing market activity.

New mortgage lending has been volatile of late, consistent with the recent noise in house sales. New lending fell 2% m/m (sa) in May, its eighth month-on-month fall in the last twelve months. House sales and new lending were boosted by the easing in LVR restrictions in January, but both have subsequently pulled back. From here, the outlook will depend on where the trend in sales settles. Housing turnover and new mortgage lending have been oscillating around a high level, but headwinds may see this peter out eventually.

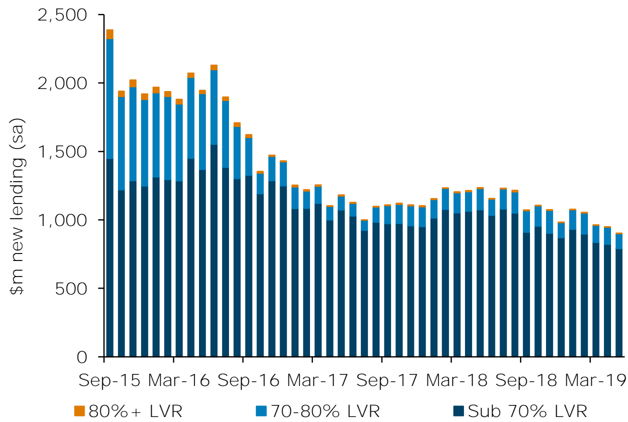
Figure 9. New mortgage lending and housing credit

Source: ANZ Research, REINZ, RBNZ

Household credit has been growing at a pretty consistent monthly pace since early 2017. In monthly terms, household lending eased 1.0% m/m in May. In annual terms, household credit growth was up 9.5% y/y (3mma).

Housing credit growth has been stable in recent months, despite housing market volatility. Banks are behaving prudently, the housing market has cooled, investors are wary and loan-to-value ratio restrictions are expected to still have a dampening influence on credit availability. Proposed tightening in banks' capital requirements would also create headwinds, if implemented. On the whole, we expect credit growth will continue to grow modestly from here.

Figure 10. Investor lending by LVR

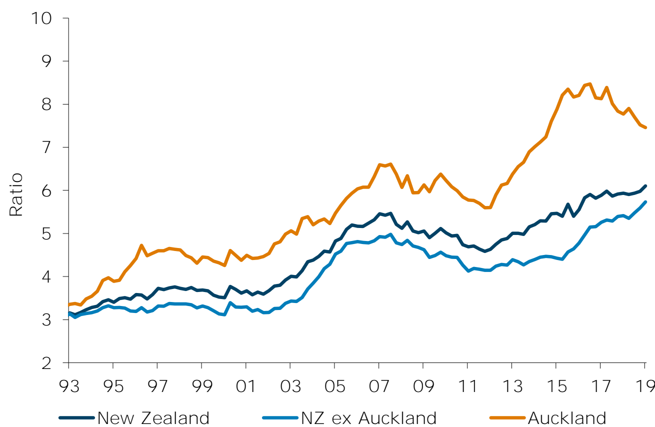


Source: ANZ Research, RBNZ

On a seasonally adjusted basis, new lending to investors fell 4.4% in May, its fourth consecutive monthly fall. The recent slowing follows a strong January rise as loan-to-value restrictions were eased in the month. But recent weakness in house sales since has more than offset the January rise – with lending to investors falling 18% so far in 2019 in seasonally adjusted terms. Underlying this, investors remain wary, which is weighing on the housing market. About 14% of new loans were to investors in May, down from 27% at the start of the year.

The share of investor lending on riskier terms remains low. The share of investor lending at loan-to-value ratios of less than 70% is sitting above 85%. In late-2014 it was about half.

Figure 11. Regional house prices to income

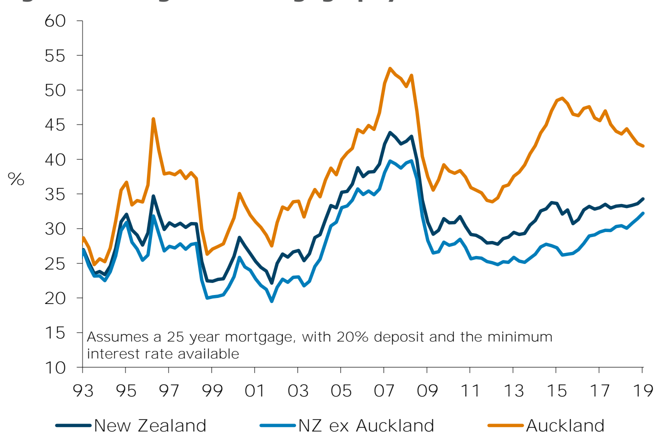


Source: ANZ Research, REINZ, Statistics NZ

One commonly cited measure of housing affordability is the ratio of average house prices to incomes. It is a standard measure used internationally to compare housing affordability across countries. It isn't perfect; it does not take into account things like average housing size and quality, interest rates, and financial liberalisation. Therefore, it is really only a partial gauge as some of these factors mean that it is logical for this ratio to have risen over time.

Nationally, the ratio has been stable at 6 times income since early 2017. Auckland has seen its ratio ease from over 8 times in 2017 to an estimated 7.5 times in Q1 2019, reflecting recent weakness in house prices. Ex-Auckland, the ratio has continued to rise; at 5.6 times incomes this is at record highs.

Figure 12. Regional mortgage payments to income



Source: ANZ Research, REINZ, RBNZ, Statistics NZ

Another, arguably more comprehensive, measure of housing affordability is to look at it through the lens of debt serviceability, as this also takes into account interest rates, which are an important driver of housing market cycles.

We estimate that for a purchaser of a median-priced home (20% deposit), the average mortgage payment to income nationally is 34%. However, there are stark regional differences. In Auckland it is 42% and the rest of New Zealand it is 31%. This is not far from historic highs in Auckland, despite mortgage rates being very low. Debt levels are high nationwide. And while home ownership is being made more affordable by low mortgage rates, households could be vulnerable in the event of a lift in interest rates.

Property gauges

Regional divergences remain a key theme in New Zealand's housing market. Auckland house price growth slipped further into negative territory in June. House price inflation in the capital is still high but falling back in line with the rest of the pack. Canterbury inflation has made a small run back into positive territory and some of the small centres, like Manawatu-Whanganui and the deep south, are seeing prices tick up again. House price inflation isn't expected to roll over at the national level as OCR cuts should help keep mortgage rates under pressure, LVR restrictions will likely be loosened gradually, and supply shortages remain. Conversely, several headwinds are capping the upside: banks are cautious and LVR limits remain binding; investors are wary of policy changes; and affordability constraints are biting.

We use ten gauges to assess the state of the property market and look for signs that changes are in the wind.

Affordability. For new entrants into the housing market, we measure affordability using the ratio of house prices to income (adjusted for interest rates) and mortgage payments as a proportion of income.

Serviceability / indebtedness. For existing homeowners, serviceability relates interest payments to income, while indebtedness is measured as the level of debt relative to income.

Interest rates. Interest rates affect both the affordability of new houses and the serviceability of debt.

Migration. A key source of demand for housing.

Supply-demand balance. We use dwelling consents issuance to proxy growth in supply. Demand is derived via the natural growth rate in the population, net migration, and the average household size.

Consents and house sales. These are key gauges of activity in the property market.

Liquidity. We look at growth in private sector credit relative to GDP to assess the availability of credit in supporting the property market.

Globalisation. We look at relative property price movements between New Zealand, the US, the UK, and Australia, in recognition of the important role that global factors play in New Zealand's property cycle.

Housing supply. We look at the supply of housing listed on the market, recorded as the number of months needed to clear the housing stock. A high figure indicates that buyers have the upper hand.

House prices to rents. We look at median prices to rents as an indicator of relative affordability.

Policy changes. Government and macro-prudential policy can affect the property market landscape.

Indicator	Level	Direction for prices	Comment
Affordability	Unaffordable	↔/↓	Affordability constraints are very relevant. It started with Auckland; other regions are starting to join the party, reluctantly.
Serviceability/ indebtedness	High debt, low rates OK – high rates not	↔/↓	Serviceability looks okay provided interest rates stay low and income growth is solid. Debt levels are high.
Interest rates / RBNZ	More cuts coming	↔/↑	We see the OCR falling further in August and November this year, partly to offset upward pressure on rates. Short-term mortgage rates have fallen.
Migration	Peaked	↔/↑	Migration remains elevated. Data for May softened from previous estimates. Data still surrounded with uncertainty.
Supply-demand balance	Demand > Supply	↔/↑	MBIE estimates New Zealand is short 71k houses, but the build-up of pent-up demand is becoming less pronounced.
Consents and house sales	Shortage	↔/↑	We expect consents issuance will struggle to push higher, with the construction sector reaching its limits.
Liquidity	Set to tighten	↔/↓	Credit availability is very relevant. Banks have plenty of cash currently, but know they have to raise a lot more capital.
Globalisation	Weak	↔/↓	The foreign-buyer ban has stymied demand from non-residents, and the housing market is weak in Australia.
Housing supply	Too few	↔/↑	The Government is going to take a more active role, but there are still questions about crowding out other work and labour shortages.
House prices to rents	Too high	↔/↓	Rents are moving up, with pressures on the existing stock apparent. Buying remains relatively expensive.
Policy changes	Dampening	↔/↓	Government policy changes are making investors wary. Easing in loan-to-value restrictions and the ruling out of a capital gains tax has provided a slight offset.
On balance	**In recent ranges**	↔/↓	**We expect the market to remain contained, though volatility may continue in the short term.**

Property gauges

Figure 1: Housing affordability

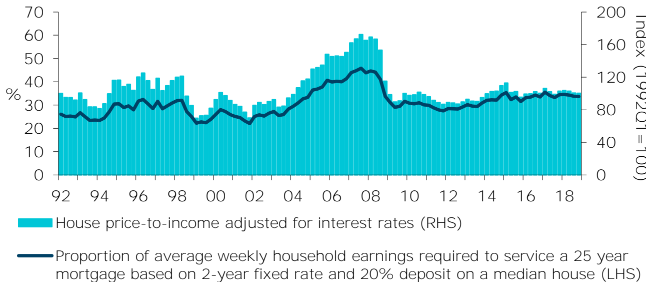


Figure 2: Household debt to disposable income

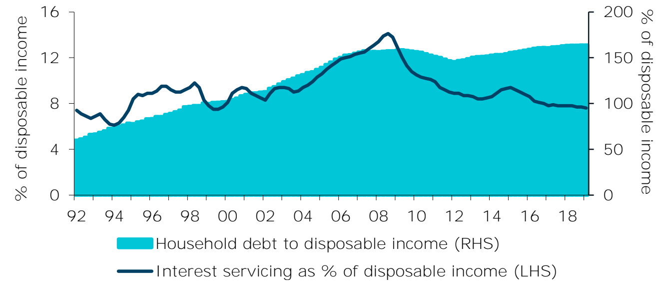


Figure 3: New customer average residential mortgage rate (<80% LVR)

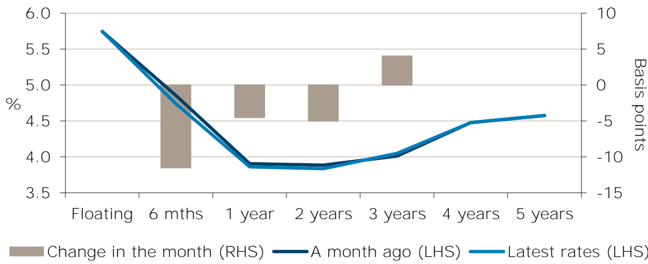


Figure 4: Annual migration*

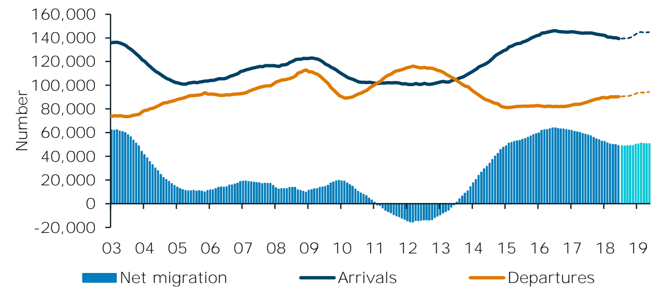


Figure 5: Housing supply-demand balance

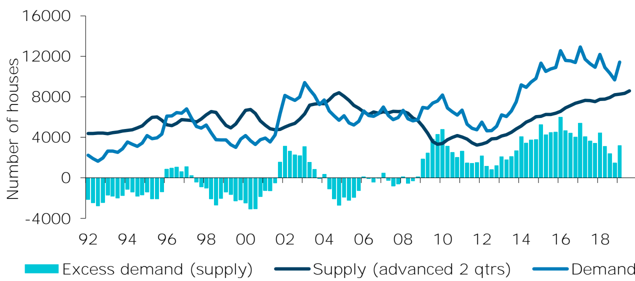


Figure 6: Building consents and house sales

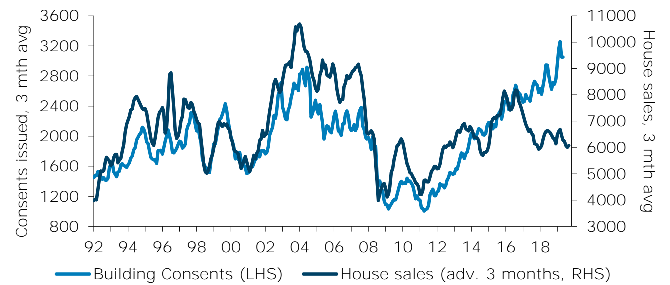


Figure 7: Liquidity and house prices

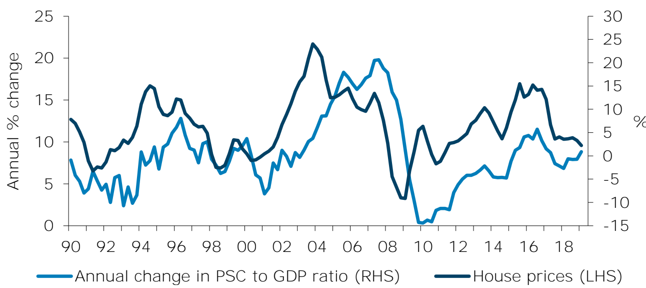


Figure 8: House price inflation comparison

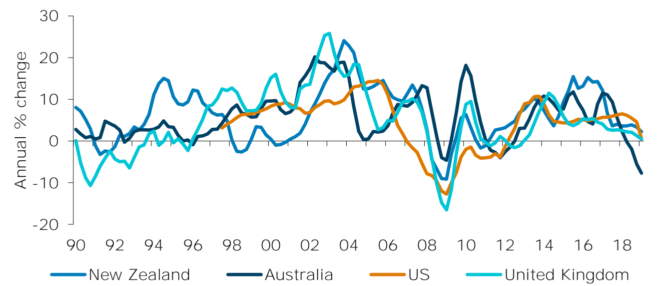


Figure 9: Housing supply

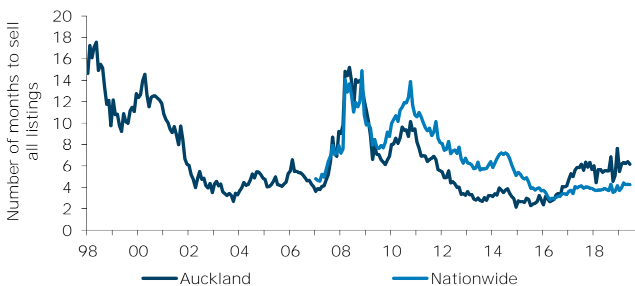
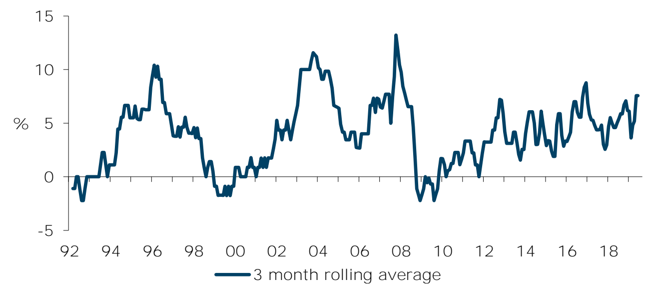


Figure 10: Median rental, annual growth



Source: ANZ Research, Statistics NZ, REINZ, RBNZ, QVNZ, Nationwide, Bloomberg, Barfoot & Thompson, MBIE

* Dotted lines show the last nine months of data, which we look through because they are subject to substantial revisions. The data prior to June 2014 is back-casted using Stats NZ's discontinued experimental data.

Economic overview

Summary

The synchronised slowdown in global growth has become more pronounced, against a backdrop of below-target inflation in many economies. Major central banks are to set to ease policy rates further, but many have little monetary policy ammunition to spare. Back home, the direct impacts of slower global growth on the New Zealand economy have so far been muted. But confidence effects are likely weighing on business sentiment, employment and investment intentions. Domestic growth looks set to trough at 2% in Q2, but the outlook from there is murky. Fiscal and monetary stimulus should provide a bit of a boost, which we expect will support a gradual acceleration in growth. But downside risks are heightened. The inflation outlook is troubling – we've likely seen the peak in domestic inflation pressures, and more is needed from the RBNZ to help met their employment and inflation objectives. We think cuts in August and November, taking the OCR to 1%, should do the trick.

Our view

The synchronised slowdown in global growth has become more pronounced, with business activity indicators weakening further in recent months. Businesses are deferring investment and industrial production activity has slowed. Uncertainties persist regarding trade, Brexit, and global growth and this is now spilling over to a broader slowdown. This comes against a backdrop of inflation that is still subdued and below target in many economies, despite tight labour markets and gradually rising wages. Additional policy stimulus is needed to support growth and inflation, with the risks to the outlook remaining to the downside.

Slowing global growth has come at a time when many central banks have little monetary policy ammunition to spare. Policy rates in some regions are now negative and central bank balance sheets are still bloated from previous rounds of quantitative easing. In addition, inflation expectations in many economies are near the bottom of historical ranges, with a key risk that expectations become unanchored and reinforce low inflation.

The Reserve Bank of Australia has already delivered two rate cuts this easing cycle, and we expect another by year-end, to take the Cash Rate to 1%. The Federal Reserve looks set to cut the federal funds rate this month, and we expect that another will be needed by year-end. With the growth outlook deteriorating in the euro area and inflation still far short of where it needs to be, we expect the European Central Bank will also ease further, cutting the deposit rate 10bp to a cool -0.5%.

Back home, the direct impacts of slower global growth on the New Zealand economy have so far been muted. Commodity prices and tourist numbers are down a little, but a lower NZD is providing an offset. The indirect impact of the global backdrop – anxiety over the outlook dampening investment and employment – appears more significant. Business activity measures have been subdued for some time and the growth slowdown is evidence that this has influenced decision making.

Growth in the New Zealand economy looks set to trough in the second quarter of this year, with annual growth falling to 2%. Leading indicators, including our consumer confidence composite and Truckometer, suggest stabilisation in the growth rate from there. It's too early to tell whether growth will gradually pick up from the second half of this year. But we expect the extra stimulus from a lower NZD and lower interest rates – along with a bit more government spending – will be enough to see growth slowly increase.

On the prices side, the outlook is bleak. Recent weakness in growth has seen more spare capacity open up in the economy, which will put downward pressure on inflation from here. In the second quarter, headline CPI inflation picked up from 1.5% y/y to 1.7%, but the bounce higher was driven by strength in petrol prices. Digging into the details, price pressures appear to have stalled. The second quarter of this year likely marked the peak in domestic (non-tradable) inflation for now. Non-tradable inflation was unchanged at 2.8% y/y in the quarter – a respectable 5-year high – but core inflation continued to track broadly sideways.

We expect non-tradable inflation will fall from here as spare capacity in the economy eases price pressure. Annual non-tradable inflation is expected to trough at 2.4% by the end of the year. From there, a recovery in domestic growth should see inflation move higher again. But we don't expect headline inflation to be sustainability back at 2% until 2021, and the risks are skewed to the downside, with inflation expectations starting to slide recently.

All up, the slower economy and fading inflationary pressures suggest that the RBNZ need to do more to support the economy and to ensure that their employment and inflation objectives are met. While there are tentative indications that economic growth is stabilising at a low level, more accommodative monetary conditions are an important driver of our expected gradual acceleration in growth from mid-2019. Hence, we expect the RBNZ to cut the OCR further in August and November, taking the OCR to 1%.

Key forecasts

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

Mortgage Size ($'000)	Mortgage Rate (%)													
	3.50	3.75	4.00	4.25	4.50	4.75	5.00	5.25	5.50	5.75	6.00	6.25	6.50	6.75
200	231	237	243	250	256	263	270	276	283	290	297	304	311	319
250	289	296	304	312	320	329	337	345	354	363	371	380	389	398
300	346	356	365	375	385	394	404	415	425	435	446	456	467	478
350	404	415	426	437	449	460	472	484	496	508	520	532	545	558
400	462	474	487	500	513	526	539	553	566	580	594	608	623	637
450	520	534	548	562	577	592	607	622	637	653	669	684	701	717
500	577	593	609	625	641	657	674	691	708	725	743	761	778	797
550	635	652	669	687	705	723	741	760	779	798	817	837	856	876
600	693	711	730	750	769	789	809	829	850	870	891	913	934	956
650	750	771	791	812	833	854	876	898	920	943	966	989	1,012	1,036
700	808	830	852	874	897	920	944	967	991	1,015	1,040	1,065	1,090	1,115
750	866	889	913	937	961	986	1,011	1,036	1,062	1,088	1,114	1,141	1,168	1,195
800	924	948	974	999	1,025	1,052	1,078	1,105	1,133	1,160	1,188	1,217	1,246	1,274
850	981	1,008	1,035	1,062	1,089	1,117	1,146	1,174	1,204	1,233	1,263	1,293	1,323	1,354
900	1,039	1,067	1,095	1,124	1,154	1,183	1,213	1,244	1,274	1,306	1,337	1,369	1,401	1,434
950	1,097	1,126	1,156	1,187	1,218	1,249	1,281	1,313	1,345	1,378	1,411	1,445	1,479	1,513
1000	1,154	1,186	1,217	1,249	1,282	1,315	1,348	1,382	1,416	1,451	1,486	1,521	1,557	1,593

Housing market indicators for June 2019 (based on REINZ data)

	Median house prices		No of sales (sa)	Mthly % chg	Avg days to sell (sa)
	Ann % chg	3mth % chg			
Northland	6.0	-3.4	197	-2%	59
Auckland	-0.1	0.6	1,720	+8%	45
Waikato	0.0	-0.4	636	-6%	40
Bay of Plenty	3.7	0.5	449	0%	48
Gisborne	1.8	5.3	55	-7%	31
Hawke's Bay	10.5	3.8	217	-13%	35
Manawatu-Whanganui	23.1	4.3	367	+2%	28
Taranaki	10.2	-0.2	139	-26%	34
Wellington	1.2	-1.4	675	-8%	34
Tasman, Nelson and Marlborough	6.7	-3.6	221	-22%	37
Canterbury	3.0	-0.4	834	0%	45
Otago	8.1	-2.7	387	-2%	28
West Coast	0.1	7.7	34	-12%	74
Southland	14.4	1.3	154	-12%	26
New Zealand	**4.4**	**-0.3**	**6,023**	**-1%**	**41**

Key forecasts

	Actual				Forecasts					
Economic indicators	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20
GDP (Ann % Chg)	2.7	2.5	2.5	2.0	2.2	2.2	2.2	2.5	2.5	2.6
CPI Inflation (Annual % Chg)	1.9	1.9	1.5	1.7(a)	1.2	1.2	1.8	1.6	1.7	1.8
Unemployment Rate (%)	4.0	4.3	4.2	4.3	4.3	4.4	4.4	4.3	4.3	4.3
House Prices (Annual % Chg)	4.3	3.3	2.7	1.6	2.1	2.1	2.3	3.4	3.2	3.0
Interest rates (RBNZ)	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20
Official Cash Rate	1.75	1.75	1.75	1.50	1.25	1.00	1.00	1.00	1.00	1.00
90-Day Bank Bill Rate	1.9	2.0	1.9	1.6	1.3	1.2	1.2	1.2	1.2	1.2
Floating Mortgage Rate	5.8	5.8	5.8	5.5	5.3	5.0	5.0	5.0	5.0	5.0
1-Yr Fixed Mortgage Rate	4.8	4.8	4.7	4.4	4.2	4.2	4.2	4.2	4.2	4.2
2-Yr Fixed Mortgage Rate	4.9	4.9	4.8	4.5	4.3	4.2	4.2	4.3	4.3	4.3
5-Yr Fixed Mortgage Rate	5.6	5.6	5.4	4.8	4.6	4.6	4.5	4.5	4.5	4.5

Source: ANZ Research, Statistics NZ, RBNZ, REINZ

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