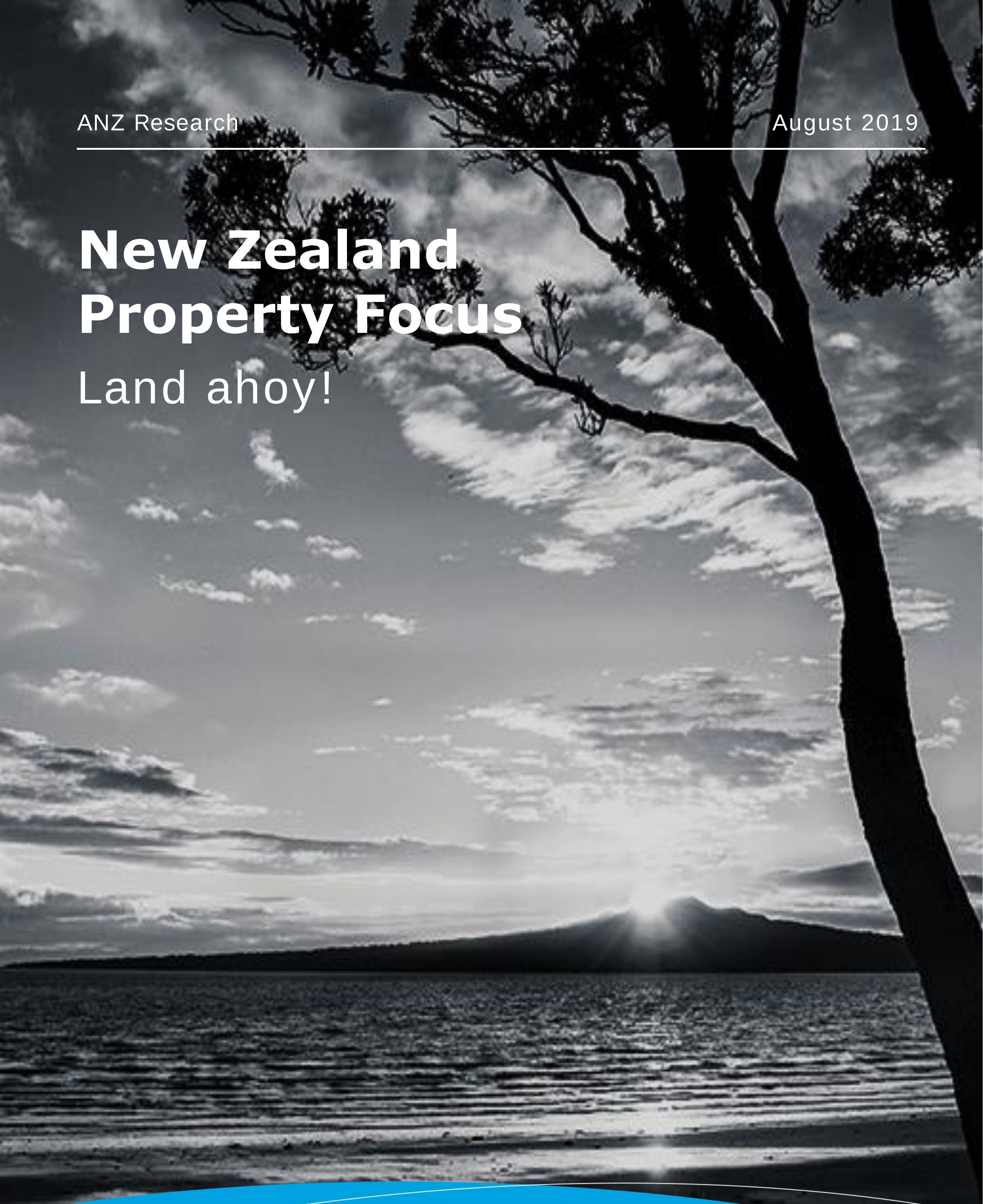

New Zealand Property Focus

Land ahoy!

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INSIDE

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Summary

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

Feature Article: Land ahoy!

Land makes up a pretty hefty chunk of the price of housing, and has made some significant contributions to house price inflation over the years. After taking a drive though the New Zealand countryside, you could be forgiven for thinking that New Zealand has an abundance of land and that a simple way to address housing affordability is simply to extend a few urban boundaries, pop in some roads and get building. But alas, land appropriate for housing might not be as abundant as you think and the stuff we do have, particularly around key urban boundaries, is currently being put to good use. Given the numerous downsides of urban sprawl, increased housing density is definitely going to have to be part of the solution to addressing housing affordability in New Zealand. While the data suggest construction activity is shifting towards multi-unit dwellings, there's still a decent way to go. And with cost pressures eroding profitability in the sector, and construction firms recently becoming increasingly pessimistic about their own outlook, activity risks are skewed to the downside.

Property gauges

The housing market has tentatively stabilised. Nationally, house prices were flat m/m in July (up 1.7% y/y 3mma), but the theme of regional divergence continued. Auckland prices are down 3.3% y/y, while pockets of strength remain in the regions of Manawatu-Whanganui and Southland. Falls in mortgage rates over the past year have not provided a noticeable boost to house prices so far, but the recent pick-up in sales supports our expectation of stabilisation in prices from here. Overall, the outlook for house price inflation is delicately balanced. Lower mortgage rates (reflecting a lower OCR), gradual loosening of the LVR restrictions, and an ongoing supply-demand imbalance are expected to provide ongoing support. However, headwinds in the form of a cautious banking sector, wary investors (particularly given policy changes), a deteriorating labour market outlook and affordability constraints limit the upside.

Economic overview

The global growth outlook remains fragile. Global manufacturing and trade has continued to soften, and while this has not yet manifested into weaker household activity in an observable way, it could be just a matter of time. Global central banks and governments have more to do to lean against the wind, and that's been reflected in global financial markets, with some long-term interest rates touching record lows. Back home, the RBNZ delivered another 50bps of OCR cuts in August in a proactive move that's keeping mortgage rates and the exchange rate under pressure. We expect a follow-up 25bp cut in November, but with the global data-flow deteriorating, September remains live. It's our expectation that slowing economic momentum is finding a floor around about now, but so far the evidence of a rebound is tentative at best. Indeed, risks appear skewed towards the slowdown lasting a little longer than we expect. However, still-elevated (albeit easing) net migration inflows, a little more government spending (albeit short-lived), the still-elevated terms of trade, and accommodative monetary conditions should prevent growth from rolling over.

Feature Article: Land ahoy!

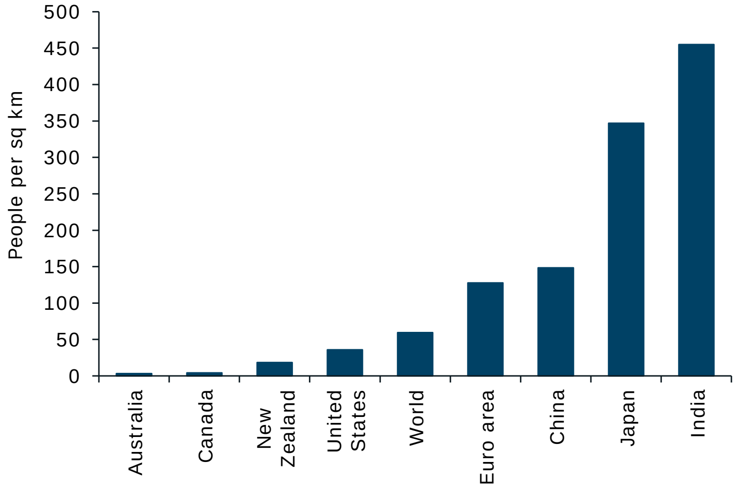
Summary

Land makes up a pretty hefty chunk of the price of housing, and has made some significant contributions to house price inflation over the years. After taking a drive though the New Zealand countryside, you could be forgiven for thinking that New Zealand has an abundance of land and that a simple way to address housing affordability is simply to extend a few urban boundaries, pop in some roads and get building. But alas, land appropriate for housing might not be as abundant as you think and the stuff we do have, particularly around key urban boundaries, is currently being put to good use. Given the numerous downsides of urban sprawl, increased housing density is definitely going to have to be part of the solution to addressing housing affordability in New Zealand. While the data suggest construction activity is shifting towards multi-unit dwellings, there's still a decent way to go. And with cost pressures eroding profitability in the sector, and construction firms recently becoming increasingly pessimistic about their own outlook, activity risks are skewed to the downside.

Land ahoy!

Land! With around 19 people per square km of land in New Zealand, we don't appear short of the stuff by international standards (Figure 1).

Figure 1. Population density (people per square km of land)



Source: World Bank

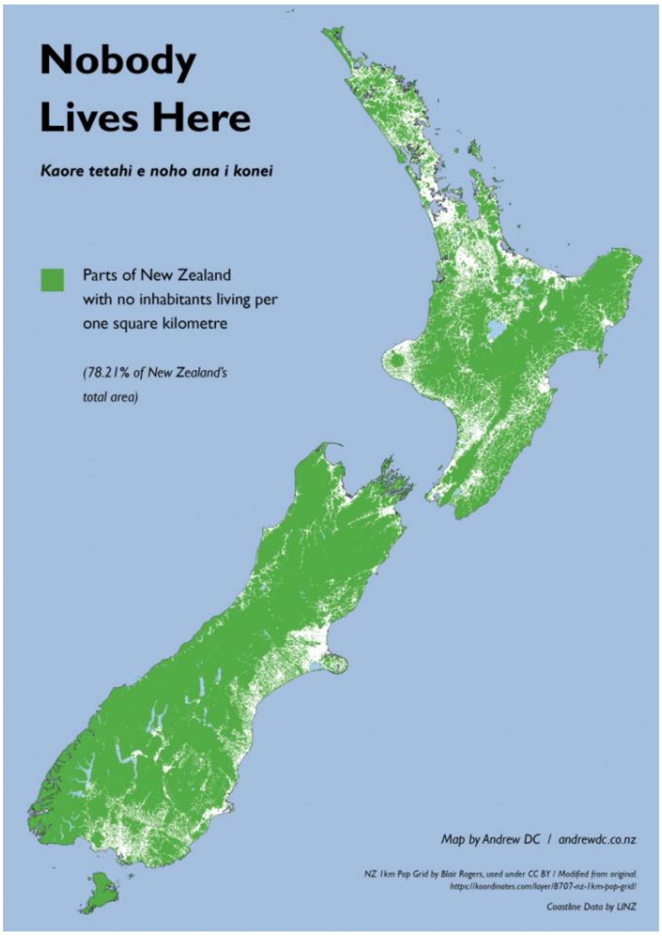
That said, population growth has seen this number more than double since the 1960s. And when you consider the fact we're not making more of it, and that the land we do have is needed to feed not only our population (which is still growing at an annual pace of around 1.6%) but also countries with a higher dependency on food imports, providing the backbone of our economy, we need to be careful about how we use it.

In Māori tradition, land (Papatūānuku) is so much more than a commodity to be traded. She is the mother who gives birth to all things (including Tāne-mahuta), and like all mothers, she deserves to be looked after and treated with respect.

Time for a quick reality check on the chart above, or statistics that get bandied about such as "only 2% of New Zealand's land mass is being used for housing". Much of the South Island, in particular, is completely uninhabitable mountains. More than 78% of New Zealand's land mass has no one living on it (defined as zero population in a given square kilometre), and that's mostly for pretty good geological reasons. (Similar arguments can of course be made about Australian population density).

Feature Article: Land ahoy!

Figure 2. Nobody lives here….



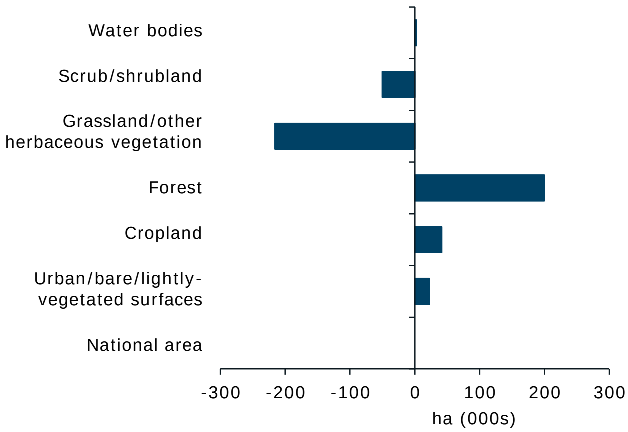
Source: andrewdc.co.nz

… for mostly very good reasons

Source: Albedo39

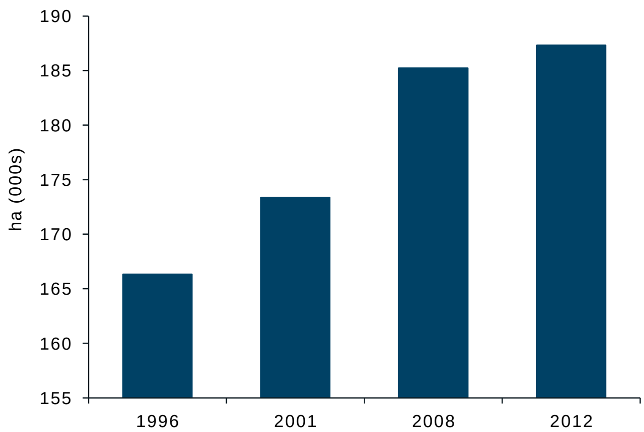
According to satellite imagery data, land use in New Zealand has undergone some significant change over the past few decades. Grassland has made way for forestry to a degree that makes growth in urban land appear relatively small (figure 3). However, that's not to say the increase in urban land hasn't been significant. Between 1996 and 2012, built-up (settlement) land has increased by almost 21,000 hectares (or 210 km^2) to a little over 187k hectares (1,870 km^2). And given the latest data point is now seven years old, and the population has grown by almost half a million people over this period, it's almost certain the amount of built-up land has continued to rise since then.

Figure 3. Change in land types 1996 - 2012



Source: Land Air Water Aotearoa

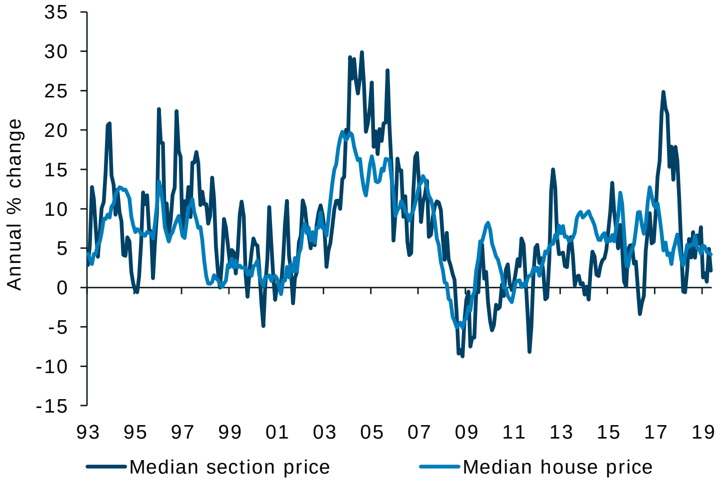
Figure 4. Built-up (settlement) land cover



Feature Article: Land ahoy!

With land a finite, non-renewable resource, it's little wonder that the cost of land has made a significant contribution to house price inflation over the years. But admittedly, it's a bit of a chicken and egg story, as higher demand for housing lifts the price of houses while also lifting the price of "potential houses" (ie sections). So it's hardly a surprise that median house sales prices and section prices move together (figure 5).

Figure 5. Median house and section price growth

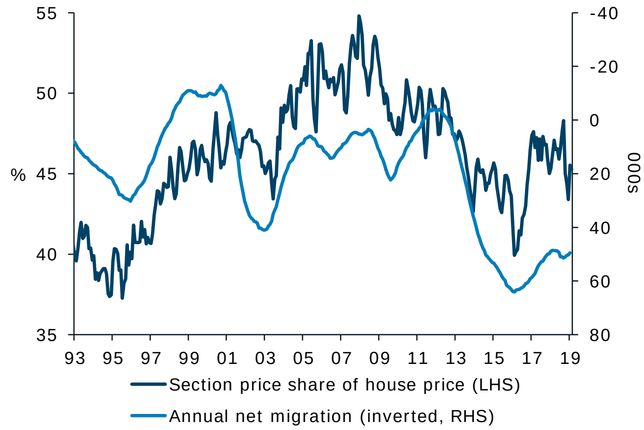


Source: REINZ, ANZ Research

On average, however, growth in median section prices has outpaced that of houses over the past two and a half decades. And using section prices as a proxy for land costs when buying a house (location, section size, and other features mean we're not exactly comparing apples with apples here), this suggests the cost of land has risen from around 39% of the median house price 25 years ago to a little over 45% currently. However, it hasn't been a straight line, with this share peaking at around 55% in May 2008 following a period of strong growth in section prices (figures 6 and 7). Over history, and in broad terms, the median section price share of house prices has had an inverse relationship with net migration flows, suggesting the existing stock of housing (captured in the denominator in figure 6) receives more of the initial impetus to housing demand from a population shock. Thereafter, as housing supply looks to catch up, it makes sense for land prices to follow suit.

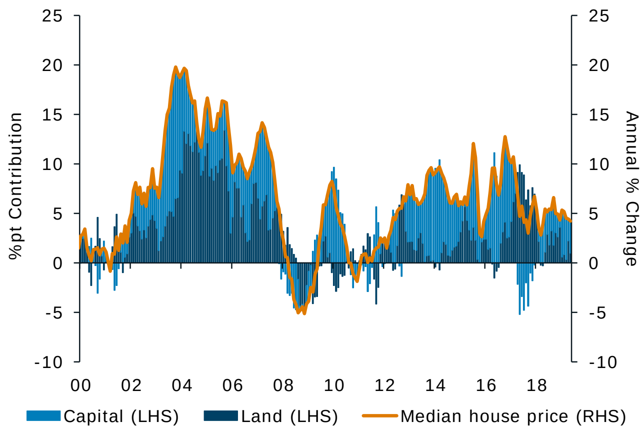
Looking through the noise, there are a number of reasons why land prices might outperform general house prices on average. Supply constraints (which for larger towns and cities are generally a function of urban boundaries) are one, while changes in the rules that allow for greater intensification and therefore a higher potential capital value (ie more or taller dwellings on a given piece of land) are another. The latter will be true for individual plots of land that are rezoned for higher density, but of course will be a dampening impact on land prices in an aggregate sense. In addition, land costs become less relevant for an individual dwelling when construction shifts towards vertical multi-unit dwellings.

Figure 6. Median section price share of median house price



Source: Stats NZ, REINZ, ANZ Research

Figure 7. Land cost contribution to house prices



Feature Article: Land ahoy!

So with land prices such a significant component of house prices, could the Government make housing more affordable by simply freeing up more land? The short answer is yes, it probably could, and there are plenty of people advocating exactly this solution. However, there are real costs to this type of growth that make it far from a no-brainer that is the best avenue to pursue.

- From an environmental point of view, more urban sprawl means **a larger carbon footprint**, all else equal. Ironic as it may be, a lifestyle block is a far less environmentally friendly lifestyle choice than an inner-city apartment. Longer travel distances to and from work and other human activities mean more emissions, and while one may argue technology has a role to play in fixing that problem (which it does) purely green transportation is a little while away. New Zealand has adopted ambitious emissions targets, and the transport sector already comprises 19% of our emissions.
- It is also an **extremely expensive** form of adding housing, given the infrastructure requirements (roads and 3 waters etc), which means it may not be the most effective way to improve housing affordability.
- There are also **productivity implications**. More cars on the road mean longer traffic waits for the likes of courier drivers and cement truck drivers, implying fewer goods shipped per day and less concrete poured than otherwise. The Government could of course just invest in more and better roads to help reduce traffic congestion (and to a large extent it is already doing this), but that would do little to encourage lower carbon emissions. And given the incentive to invest in new and better public transportation networks is a function of population density, increased urban sprawl will likely lead to less efficient public transport than otherwise. For example, you need a certain population (or revenue) base to justify the cost of building a new underground rail service.
- From a **food security** point of view, expanding urban boundaries at the cost of diminished productive land could see New Zealanders relying more heavily on imported food such as fruits and vegetables. In April last year, a joint report by the Ministry for the Environment and Statistics New Zealand noted that there is limited information about how quickly our most versatile land is shifting to urban use, but that between 1990 and 2008 29% of new urban areas were on high-class land, with the greatest areas of conversion from high-class land to urban use in Canterbury and Auckland.[1] The report identified expanding urban areas and the change of land use towards more lifestyle blocks as the main pressures facing highly productive land on the edge of towns and cities. The Government has recently announced its plan to protect productive land from urban sprawl, and this has attracted a great deal of attention. The draft National Policy Statement for Highly Productive Land (which is open for submission until October) proposes that councils be required to consider the availability of highly productive land within their region or district for primary production now and for future generations.

So given all the above, it would seem that addressing housing affordability by simply extending urban boundaries isn't a slam-dunk solution.

In any case, whether you view land-use constraints as an environmental or liveable cities no-brainer or merely the landed gentry protecting the value of their assets, the fact remains, with constraints on the degree to which land can be freed up for urban use, land prices appear set to remain a significant share of overall housing costs. In order to mitigate this, higher density housing (building closer and higher) is going to remain a very important part of meeting New Zealand's housing needs.

In Auckland, the Council anticipates that by 2047 capacity for up to 400,000 new dwellings will be needed, and anticipates that up to 70% of new dwellings will be built within the existing urban area. The estimated required dwellings is of course a wild guess dependent heavily on successive central governments' immigration policy, but the upshot is that they estimate with a bit of squishing up there's still ample room within existing boundaries to accommodate future demand. But for this to work, a cultural shift among residents has to happen. That is, residents need to warm to the idea of living in smaller dwellings and in closer proximity as the norm, opposed to the multi-bedroom, standalone house with a nice veggie patch and just 20 minutes from the CBD.

All else equal, rules that favour higher-density building and keep urban boundaries contained will put upwards pressure on land prices, with the "potential development value" of land increasing as future supply restrictions become more certain. However, it's possible that other policy tweaks provide at least a partial offset. For example, imposing a tax on vacant land (as recommended by the Tax Working Group (TWG) in February, and

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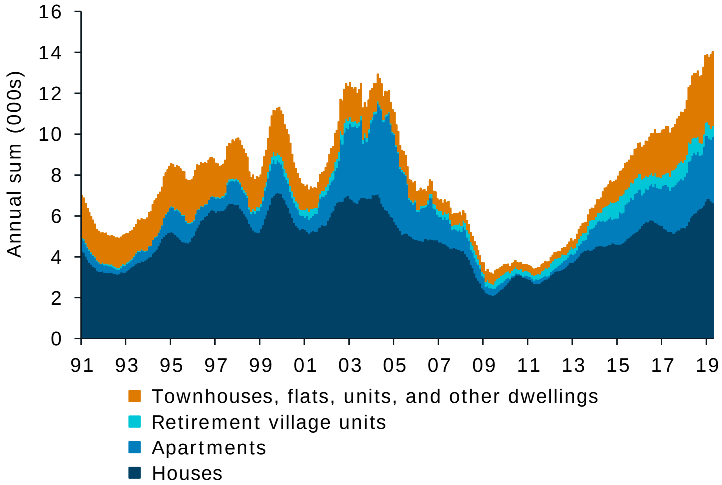
[1] Based on the Land Use Capability (LUC) system grade 1-2. See: https://www.mfe.govt.nz/sites/default/files/media/RMA/Our-land-201-final.pdf

later classified as a high priority for further investigation by the Government), is one way to limit the expected return from land banking. However, information released by the TWG suggests that the design, implementation and efficacy of vacant land taxes are complex.[2] But regardless of future policy settings, higher land prices don't necessarily imply higher dwelling prices on a per unit basis, as generally speaking, higher-density building (particularly vertical) reduces the land cost per unit, making it less relevant overall.

So if the future is higher density dwellings, is that what's actually being delivered? Dwelling consents data suggest progress on this front is indeed being made. Figure 8 shows that while annual consents for houses has remained at a high level over the past year or so, the trend higher has been driven largely by townhouses, flats, units and apartments.

Figure 8. Composition of new dwelling consents



Source: Stats NZ, ANZ Research

Auckland has been leading the pack in the multi-unit dwelling consent space, accounting for almost 80% of national total apartment consents in the year to June 2019 and more than 50% of townhouse, flats and units consents (figures 9 and 10). While recent strength in apartments doesn't look out of kilter compared to the mid-2000s cycle, the recent strength in townhouses, flats and units is unprecedented.

Figure 9. Annual apartment consents

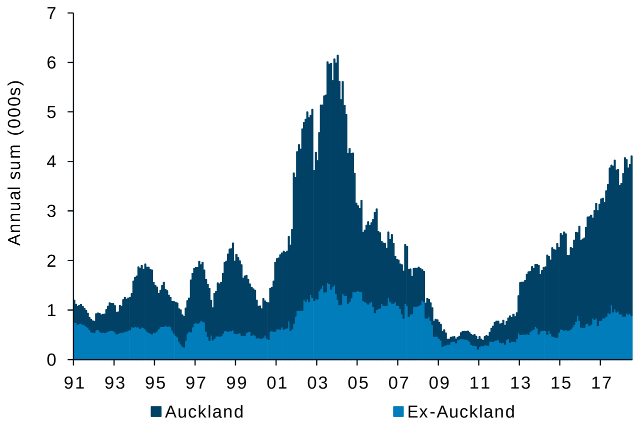
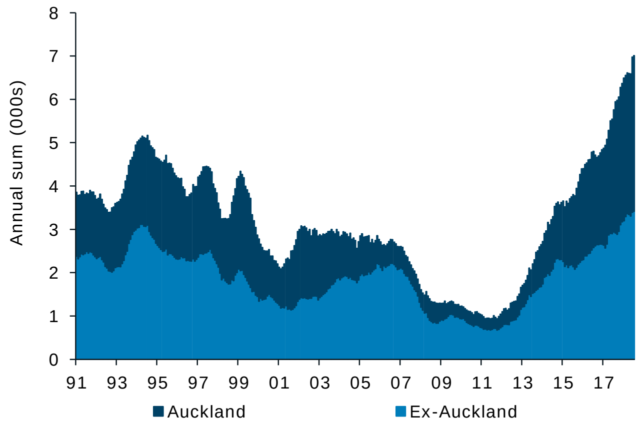


Figure 10. Annual townhouse, flats and units consents



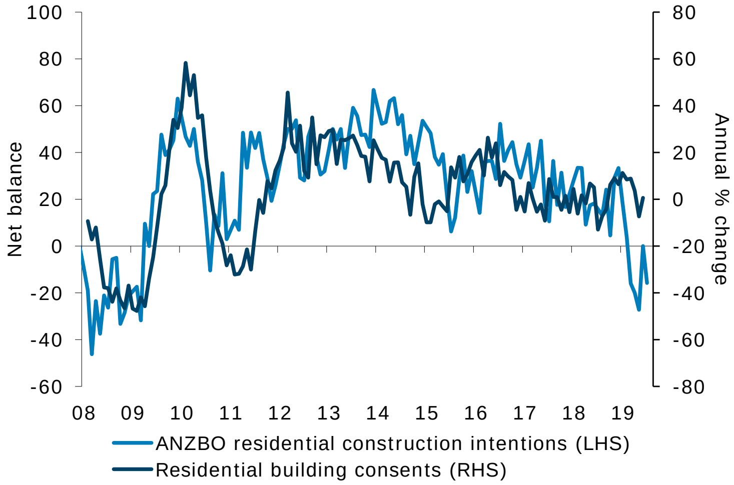
Source: Stats NZ, ANZ Research

It's difficult to work out from the regional consents data just how much of the strength in Auckland is owing to housing supply catch-up following years of strong population growth, and how much can be put down to the Auckland council changing the rules to allow for higher-density housing. Regardless, it seems progress is indeed being made towards a larger share of higher-density housing.

[2] https://taxworkinggroup.govt.nz/sites/default/files/2019-02/twg-bg-4037441-taxing-vacant-property.pdf

However, the signal from our ANZ Business Outlook Survey suggests construction may struggle to maintain recent activity levels. For a while now the construction sector has been reporting softening profitability with costs on the rise (including for labour) and difficulty increasing prices. Now, it appears that difficulties in the sector are coming to a head, with a net third of construction firms expecting lower activity (figure 11) and the same proportion expecting to reduce headcount. While the sample size within this survey isn't large enough to call this signal 'robust', it has correlated well with activity in the past.

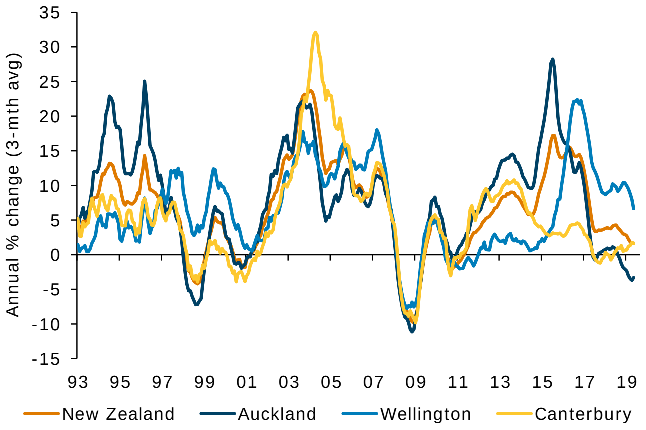
Figure 11. Construction intentions and consents



Source: Stats NZ, ANZ Research

All up, despite the fact that land costs have made a significant contribution to house price inflation over the years, the downsides associated with simply freeing up more of it for urban use suggest a careful and considered approach is required. Indeed, there are some major economic and environmental benefits associated with higher-density housing, which, in an economy where productivity growth is all but non-existent and carbon emissions reduction a priority, shouldn't be overlooked. And while consents data show we're on the right track, survey data suggests a cyclical downturn in building activity may not be far away.

Figure 1. Regional house price inflation

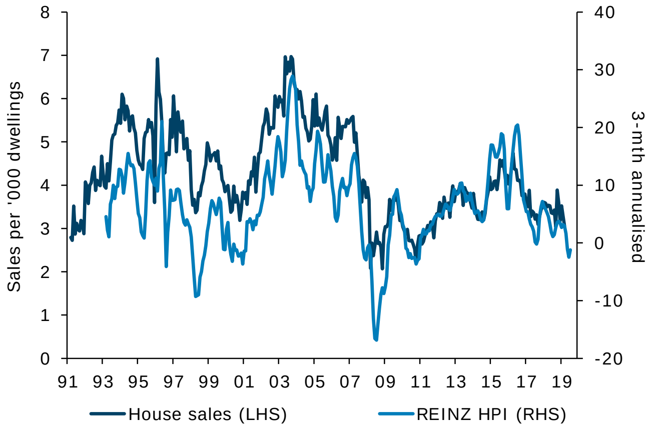


Source: ANZ Research, REINZ

House prices were flat m/m in July at the national level, with annual house price inflation tracking broadly sideways at 1.7% y/y (3mma) – well down on double-digit growth a little more than two years ago. We had expected the firming in prices in late 2018 would prove short-lived and that headwinds weighing on the market would keep price growth contained, and this has proven to be the case.

Regional divergence remains a key theme. Auckland house price inflation is negative, contracting 3.3% y/y. Growth in Wellington prices has slowed to 6.7% y/y while prices in Canterbury are lifting modestly at 1.6% y/y.

Figure 2. REINZ house prices and sales

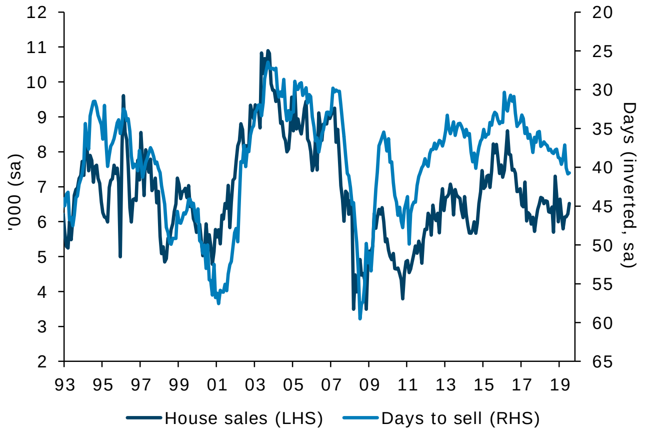


Source: ANZ Research, REINZ

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

Seasonally adjusted house sales rebounded 4.8% m/m in July and have been much less volatile in recent months compared to late 2018 and early 2019. That said, house sales remain at a low level relative to total dwellings, which is consistent with low house price inflation. On an annual basis, sales are down 1.2% at the national level (3-month average) and are down 4.5% in Auckland. Outside of Auckland, sales were up 0.8% y/y.

Figure 3. Sales and median days to sell

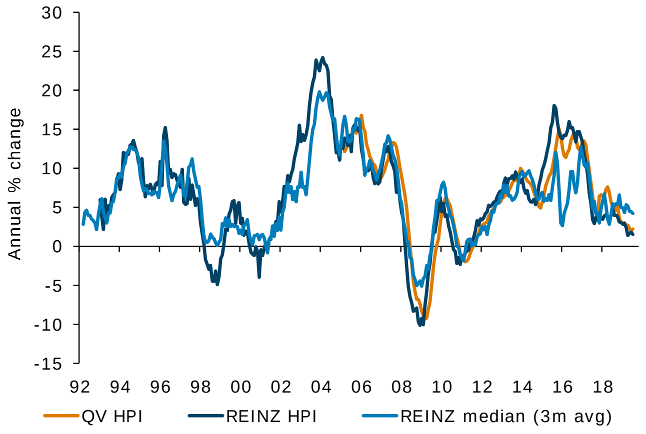


Source: ANZ Research, REINZ

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.

Seasonally adjusted days to sell in July were steady at 41 days in aggregate, above its historical average of 39.5 and suggesting there is some slack in the market. However, regional divergences are evident, with days to sell in Auckland in particular showing significant signs of slack at 46 (historical average: 36). Slack around this level suggests that weakness in prices may continue for a while yet.

Figure 4. REINZ and QV house prices

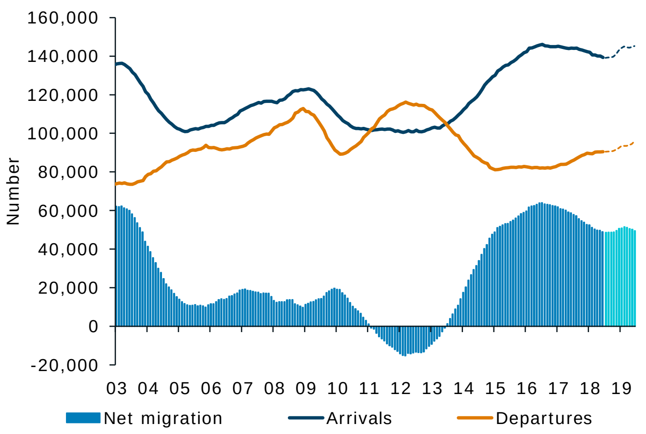


Source: ANZ Research, REINZ, QVNZ

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 1.7% y/y (3mma) in July. The QVNZ measure has moderated even further and is sitting at 2.2% y/y. The REINZ median remained within recent ranges, with annual growth of 4.2%. 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

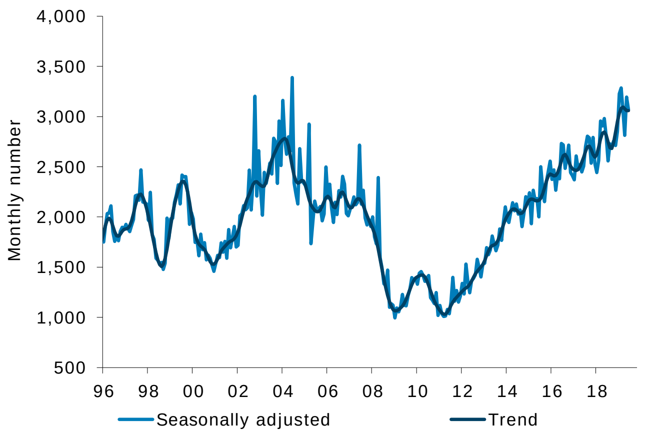
*Dotted lines show the last nine months of data, which we look through because they are subject to substantial revisions. The data prior to June 2014 is back-casted using Stats NZ's discontinued experimental data.

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 49,400 in June from 50,300 in May, but Statistics NZ's data is subject to substantial revision and is relatively untested, so we would caution against reading too much into it. 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

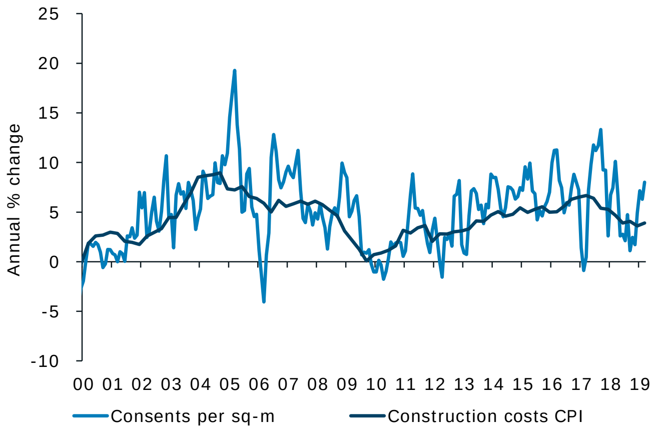


Source: ANZ Research, Statistics NZ

Residential building consents fell 3.9% m/m in June to be down 0.6% on a quarterly basis. These data are volatile, particularly for multi-unit dwellings, and overall consents remain at a high level. However, given construction firms' activity expectations have turned sour of late, we'll be watching this one very closely. Reflecting strength in earlier in the year, annual consent issuance pushed higher in June, running at 34,942, above the previous mid-2000s peak (33,200). Growth in Auckland consents has been driving strength over the past year.

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.

Figure 7. Construction cost inflation

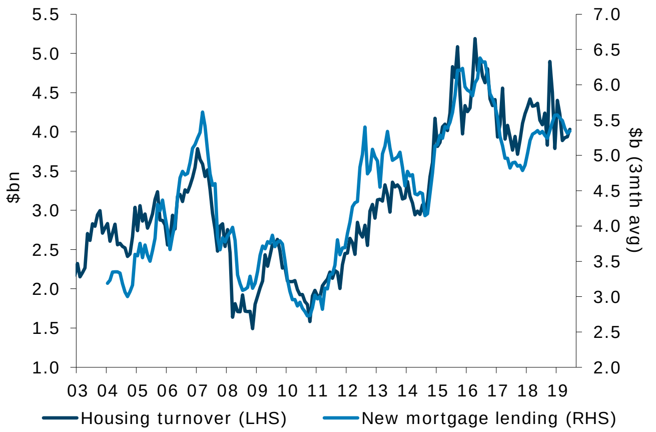


Source: ANZ Research, Statistics NZ

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 lift 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 moves closely with new house sales. New lending fell 0.8% m/m (sa) in June, but remains broadly flat on an annual basis (3mma). 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.

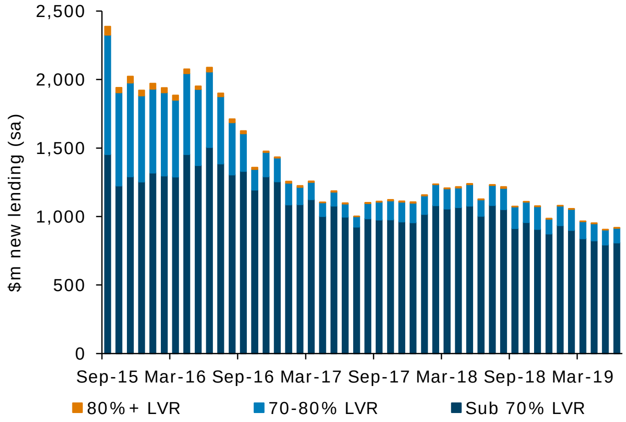
Figure 9. New mortgage lending and housing credit

Source: ANZ Research, REINZ, RBNZ

Household credit has been growing at a relatively steady pace for the past year or so. In seasonally adjusted terms, household lending lifted 0.5% m/m to be up 5.9% y/y in June.

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, and the outlook for the labour market is darkening. On the whole, we expect credit growth will continue to grow modestly from here.

Figure 10. Investor lending by LVR

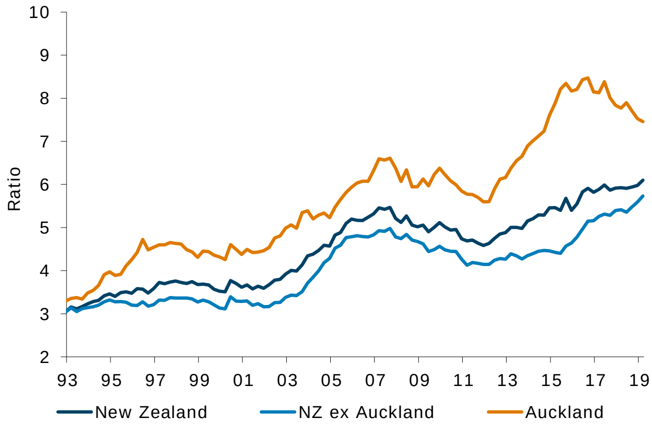


Source: ANZ Research, RBNZ

On a seasonally adjusted basis, new lending to investors rebounded 4% in June, partially retracing May's 4.4% decline. New lending to investors has been relatively soft over 2019 to date, with June's read down 19% on 2018 average levels. Underlying this, investors remain wary, which is weighing on the housing market. About 18% of new loans were to investors in June, down from an average of 22% over 2018 and well below 2016 peaks of almost 35%. It will be interesting to see the impact of the new record low in the OCR.

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

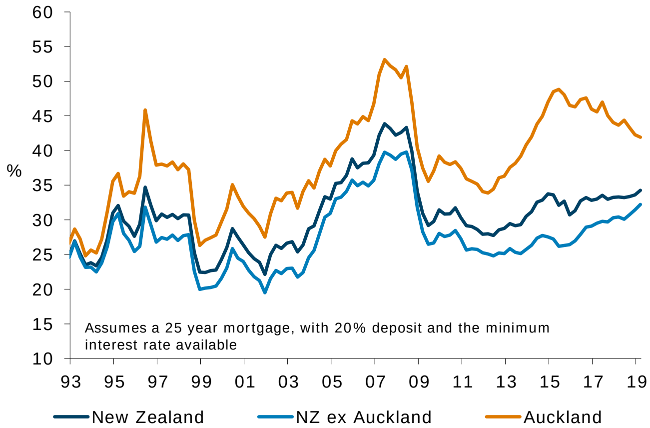


Source: ANZ Research, REINZ, Statistics NZ

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 broadly stable at 6 times income since early 2017, as ongoing moderation from high levels in Auckland and catch-up from elsewhere around the country offset. 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

The housing market has tentatively stabilised. Nationally, house prices were flat m/m in July (up 1.7% y/y 3mma), but the theme of regional divergence continued. Auckland prices are down 3.3% y/y, while pockets of strength remain in the regions of Manawatu-Whanganui and Southland. Falls in mortgage rates over the past year have not provided a noticeable boost to house prices so far, but the recent pick-up in sales supports our expectation of stabilisation in prices from here. Overall, the outlook for house price inflation is delicately balanced. Lower mortgage rates (reflecting a lower OCR), gradual loosening of the LVR restrictions, and an ongoing supply-demand imbalance are expected to provide ongoing support. However, headwinds in the form of a cautious banking sector, wary investors (particularly given policy changes), a deteriorating labour market outlook and affordability constraints limit the upside.

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; several other regions have joined the party.
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 November, but the impact on retail rates is unclear. Short-term mortgage rates have fallen.
Migration	Peaked	↔/↑	Migration remains elevated. Data for June softened from previous estimates. The data remains prone to very large revisions.
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

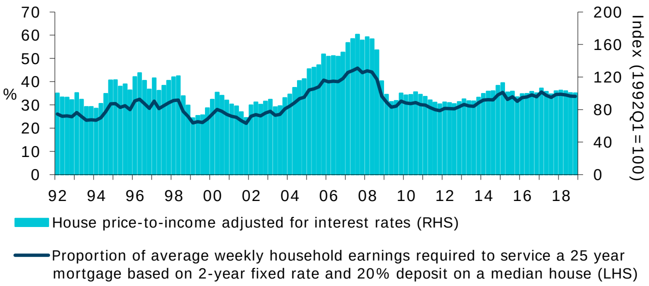


Figure 2: Household debt to disposable income

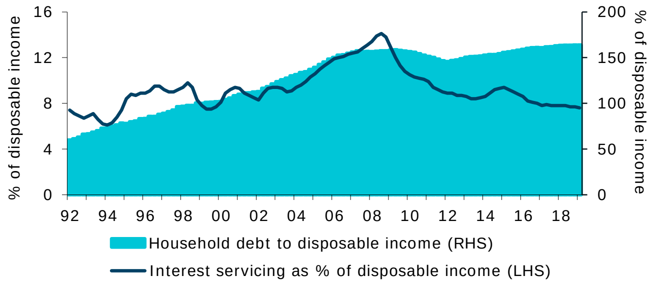


Figure 3: New customer average residential mortgage rate (<80% LVR)

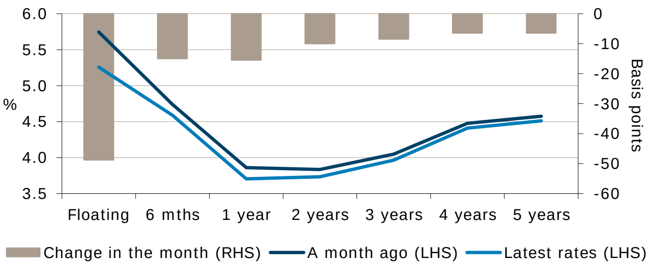


Figure 4: Annual migration*

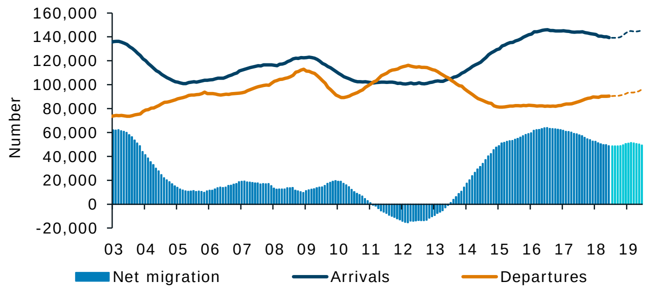


Figure 5: Housing supply-demand balance

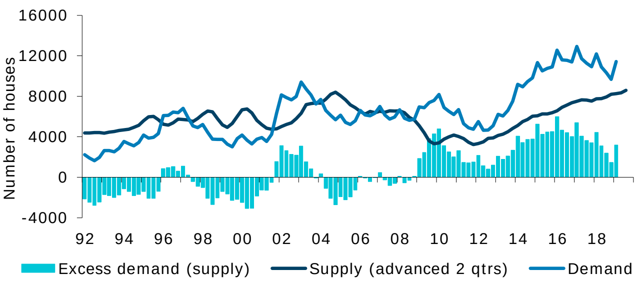


Figure 6: Building consents and house sales

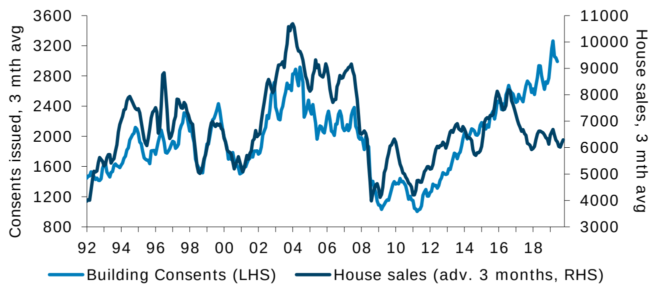


Figure 7: Liquidity and house prices

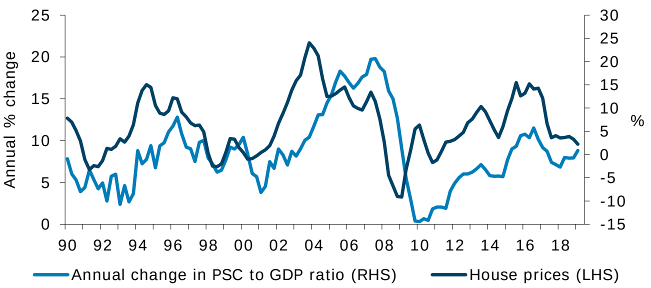


Figure 8: House price inflation comparison

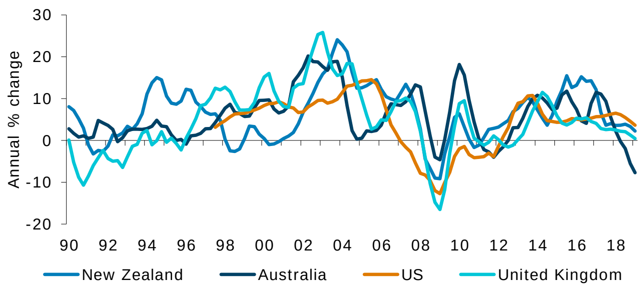


Figure 9: Housing supply

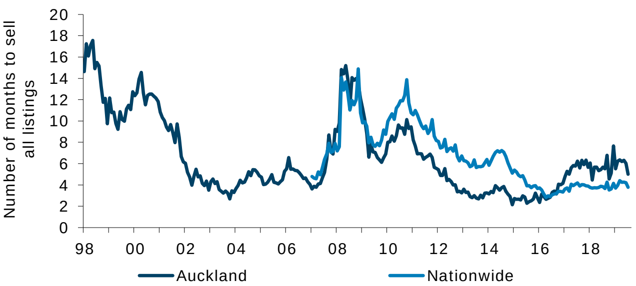
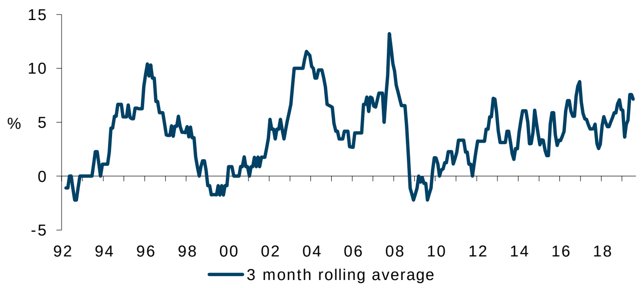


Figure 10: Median rental, annual growth



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 global growth outlook remains fragile. Global manufacturing and trade has continued to soften, and while this has not yet manifested into weaker household activity in an observable way, it could be just a matter of time. Global central banks and governments have more to do to lean against the wind, and that's been reflected in global financial markets, with some long-term interest rates touching record lows. Back home, the RBNZ delivered another 50bps of OCR cuts in August in a proactive move that's keeping mortgage rates and the exchange rate under pressure. We expect a follow-up 25bp cut in November, but with the global data-flow deteriorating, September remains live. It's our expectation that slowing economic momentum is finding a floor around about now, but so far the evidence of a rebound is tentative at best. Indeed, risks appear skewed towards the slowdown lasting a little longer than we expect. However, still-elevated (albeit easing) net migration inflows, a little more government spending (albeit short-lived), the still-elevated terms of trade, and accommodative monetary conditions should prevent growth from rolling over.

Our view

Growth among New Zealand's key trading partners has slowed. And while weakness has largely been concentrated in trade and manufacturing, with softer-than-otherwise investment also a feature, things could get rather ugly if global labour markets and household sentiment and spending follow suit.

The starting gun for the race to the bottom for global central banks was fired when the RBNZ cut the OCR in May. Since then the RBA have cut their cash rate to 1.0%, the Federal Reserve have eased 25bps, the ECB has signalled that easing isn't far away, and China has bumped up fiscal stimulus and allowed the yuan to depreciate. And it would seem further global stimulus is just a matter of time.

Turning to the domestic picture, New Zealand's export prices have been relatively robust in the face of slowing global activity. Yes, commodity prices are down a little, as are tourist numbers, but a lower NZD is providing some offset. However, with the global outlook so uncertain we think exporters are going to remain cautious, implying constrained investment spending and possibly a phase of deleveraging.

The domestic side of the New Zealand economy has been losing steam for a while now, with annual growth slowing from around 4% in late 2016 to 2.5% by Q1 2019. We expect Q2 GDP will show this slowdown persisted into Q2 with annual growth expected to trough at 2.0%. Thereafter, we've pencilled in a gradual acceleration in economic activity that will see annual growth lift towards 3% by the end of 2021. However, forward-looking indicators are yet to provide convincing evidence that this is actually occurring.

Households have remained in good stead, evidenced by the modest tick up in wage growth in Q2 and fall in the unemployment rate (from 4.2% to 3.9%), but the labour market generally lags economic activity. And more recently, survey data suggest that both the construction and manufacturing sectors are reducing headcount, which doesn't bode well for employment growth over the second half of the year. Consumer confidence is not looking quite as bullet-proof as it was.

Overall, the risk that slowing economic momentum is a little more persistent than we've pencilled in is intensifying as data flow rolls in (such as the manufacturing PMI). But if this is the case we still think there are enough supports out there to put a floor under things (unless something drastic happens of course – commodity price crunches and drought have been the typical historical catalysts for a New Zealand recession). That said, if the gradual pick-up in growth does occur as we expect, we think it will be hard won as the tailwinds of lower interest rates, recent NZD depreciation, a tight labour market, and a little extra fiscal stimulus will still need to contest with stubbornly low business sentiment (which we suspect is weighing on investment and employment decisions), slowing population growth, anaemic productivity growth and a softer housing market.

All up, the New Zealand economy is doing okay, but risks are certainly heightened. And if risks are skewed to the downside around our expectations for a relatively modest growth recovery, then they are skewed even further south compared to the RBNZ's relatively optimistic-looking August MPS forecasts. By November, we think the evidence will be clear that growth is struggling to accelerate as the RBNZ expects and that they will cut the OCR to a record low of 0.75%. Should the global picture deteriorate further, or domestic data take a marked turn for the worse, the cuts could come earlier and/or deeper than we expect. If things were to really deteriorate, there's plenty of fiscal headroom for government to step up to the plate and lean against the wind with a little extra spending or tax cuts.

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 July 2019 (based on REINZ data)

	Median house prices Ann % chg	Median house prices 3mth % chg	No of sales (sa)	Mthly % chg	Avg days to sell (sa)
Northland	-2.5	-3.3	196	-3%	59
Auckland	0.1	0.4	1,912	+7%	46
Waikato	3.0	-0.2	656	+2%	41
Bay of Plenty	-0.3	-0.9	463	0%	45
Gisborne	16.9	3.7	58	+4%	29
Hawke's Bay	9.3	3.7	257	+16%	30
Manawatu-Whanganui	25.7	5.0	367	-1%	30
Taranaki	-3.8	0.0	186	+28%	43
Wellington	14.8	2.7	716	+1%	33
Tasman, Nelson and Marlborough	0.4	-1.6	228	+1%	36
Canterbury	3.9	-0.2	947	+10%	45
Otago	21.7	2.1	377	-6%	33
West Coast	-25.0	-2.3	36	-3%	80
Southland	19.9	-0.8	162	0%	38
New Zealand	**4.7**	**0.6**	**6,523**	**+5%**	**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	1.5	1.6	1.7
Unemployment Rate (%)	4.0	4.3	4.2	3.9(a)	4.1	4.2	4.2	4.3	4.3	4.3
House Prices (Annual % Chg)	4.3	3.3	2.7	1.6(a)	2.1	2.1	2.3	3.4	3.2	3.0
Interest rates (RBNZ)	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21
Official Cash Rate	1.75	1.75	1.50	1.00	0.75	0.75	0.75	0.75	0.75	0.75
90-Day Bank Bill Rate	2.0	1.9	1.6	1.1	0.9	0.9	0.9	0.9	0.9	0.9
Floating Mortgage Rate	5.8	5.8	5.7	5.2	5.0	5.0	5.0	5.0	5.0	5.0
1-Yr Fixed Mortgage Rate	4.8	4.7	4.6	4.3	4.3	4.3	4.4	4.4	4.4	4.4
2-Yr Fixed Mortgage Rate	4.9	4.8	4.7	4.5	4.5	4.5	4.5	4.5	4.5	4.5
5-Yr Fixed Mortgage Rate	5.6	5.4	5.0	5.0	4.9	4.9	4.9	4.9	4.9	4.9

Source: ANZ Research, Statistics NZ, RBNZ, REINZ

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