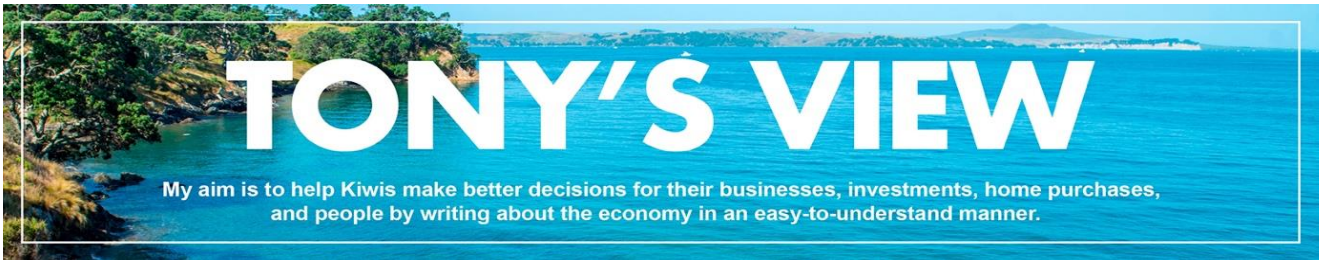

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Changes at the margin

Let's say you and I sat down to design a survey giving insight into what is happening in the housing market or something like that. The way it will go is that you will come up with a list of question which will provide good insight into the nature of the sector at the moment. Maybe things like who owns what, how many, what did they pay, starting mortgage interest rate etc.

The answers will all be interesting – for one month. After that – meh.

As an economist I don't have all that much interest in the structure of the housing market. What I am interested in is how things are changing. My list of questions would focus on how people are feeling about certain things at the moment, what their plans are etc.

The first month I would write up and try to make it sound interesting – but to me it wouldn't be really. My interest would start in the following months when I could see how things were changing. It is those changes in people's plans that are what we need to know if we are to pick where the housing market is headed. Static cross-sectional insights give no directional guides.

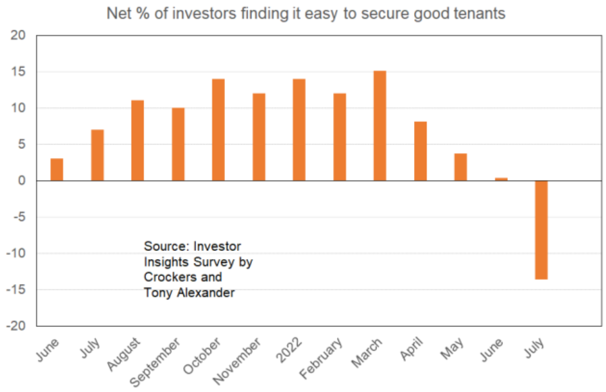
If you look through my monthly surveys, you might be able to pick the questions which can yield good insights on a month to month or quarter to quarter basis – they'll be the ones I suggested. The other ones giving insight into structures which hardly ever change – ever – may have been inserted by the organisation sponsoring the survey.

So, what are some of the interesting things which I am gleaning from my monthly surveys at the moment? Or, to put it another way, what is changing at the margin? These things are.

The rental market is moving in favour of tenants

You will get good insight into this next week when the results of my monthly survey of residential property investors with Crockers Property Management are released. I'm not going to give it all away but let's just say that this graph sums things up fairly well.

It shows a strong shift in the net proportion of investors saying that they are finding it easy to get good tenants. The net proportion is now firmly negative. Landlords are less able to pick and choose amongst many good tenants now.

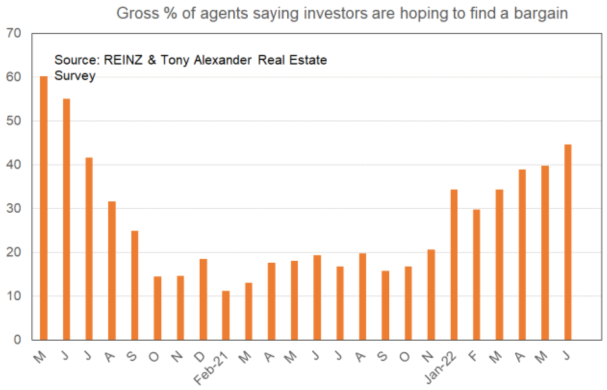


That has implications for rent rises and that is something you will see for yourself next week. The rent implications are one of the early things which will soon start feeding into a scaling back of inflation forecasts in coming months and solidify a view of mortgage rates for most fixed terms being at or near their cyclical peaks.

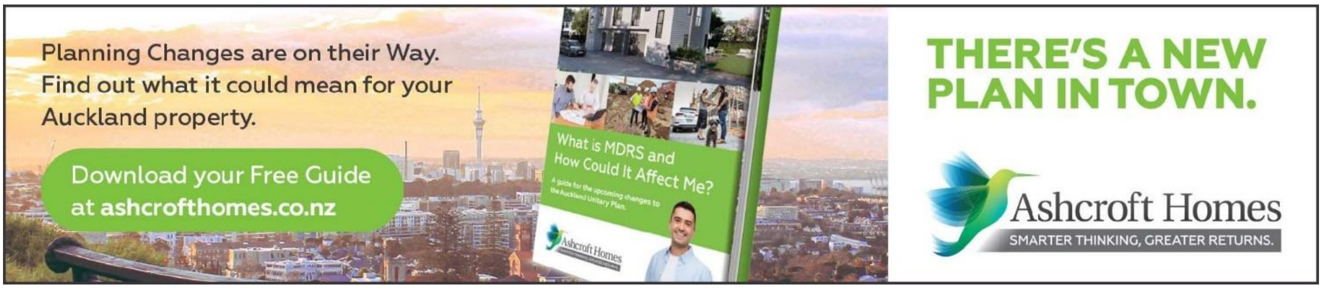
We're not quite there yet. People are fixating on the level of the cost of living annual change now – not where it is headed. Their views and their emotions are backward looking, not forward.

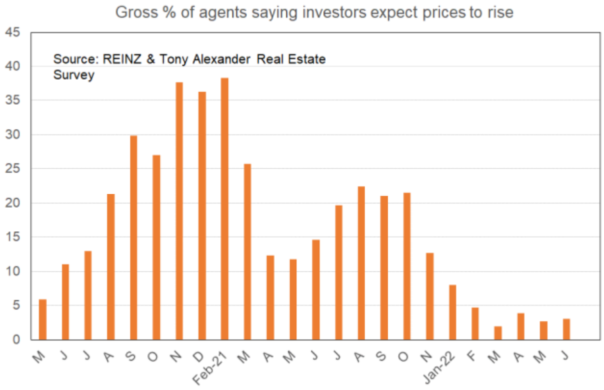
Investors are sniffing around

At the margin we are seeing some investors showing increased interest in purchasing properties. One source of evidence for this comes from my monthly survey of real estate agents alongside REINZ. The gross percent of agents saying that investors looking to buy are doing so because they hope to get a bargain has risen to a two year high of 45% from 40% in June and 34% at the start of the year.



Note that this is not the same thing as saying these investors expect prices to rise. The graph here shows that there is no upward trend in this measure.





And it is definitely not a widespread trend yet of investors coming out of the woodwork. But from my monthly survey of mortgage advisers alongside mortgages.co.nz we have received anecdotes of some investors making tentative enquiries for finance, especially ahead of next year's general election.

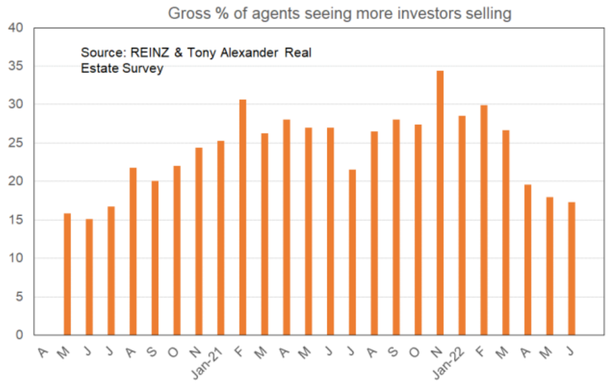
There are signs that some are willing to buy in the next few months while the market is firmly in their favour if the political polls suggest a good chance of National winning next year.

National have said that they will fully restore deductibility of interest expenses and take the brightline test back to two years.

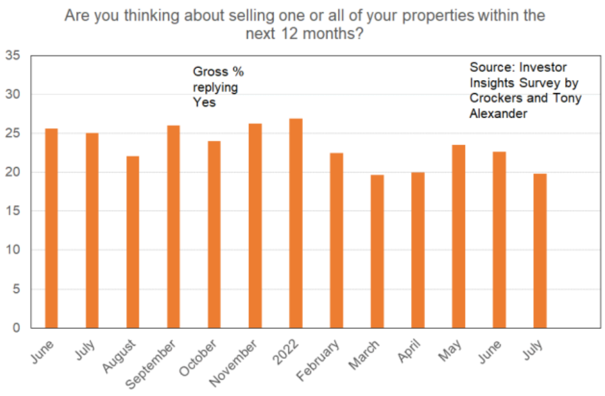
There is no wave of investors selling

I've been making this point for over a year. Since the tax announcement of March 23 last year investors have stepped back from their buying. But they have not stepped forward to sell in any identifiable numbers.

Over the past three months there has been a noticeable decline in the proportion of agents saying that they are seeing investors looking to sell.



This next graph from my survey of residential property investors with Crockers Property Management suggests the reduction in willingness to sell started in about February and maybe the graph above of real estate agents about shows the same thing.



The results of my latest survey of portfolio investors undertaken in conjunction with Sharesies will be released at the end of the month. They also show a mild downward trend in the proportion of people looking to sell their residential property.

Given that consumer confidence is already slammed, mortgage rates have about peaked, and house prices on average have probably completed over half their likely declines, the factors which would encourage investors to sell are not strengthening. Soon they will be easing.

I look at these very early indications of changes at the margin then add in a few other things. Before the end of this year there is a good chance that the Reserve Bank will ease up LVR rules. Plus mortgage rates will probably be assessed to have started falling as evidence accrues of inflation pulling back.

But I won't be calling an end to the period of falling prices and potential for some average gains until some other things happen. One of those is evidence of vendors capitulating to the new pricing reality and accepting first-up offers from buyers rather than continuing to hold off in case they can get the price they could have got late last year.

If I were a first home buyer would I look to buy at the moment? Yes. I would have a wide range to choose from, the vendors will be getting more willing to negotiate as each day goes by and the media scare them more and more with stories of woe about virtually everything in New Zealand.

I'd be confident of keeping my job or getting a new one easily if laid off.

However, opting to buy and being able to get the finance are two very different things. For many young buyers making a purchase is not going to be an option for a while now that some bank test interest rates are almost at 8%, getting a loan with less than a 20% deposit is very hard, and the changes to the CCCFA rules are not good enough.

If I were a borrower, what would I do?

Nothing I write here or anywhere else in this publication is intended to be personal advice. You should discuss your financing options with a professional.

Rates up and curve inverts

Wholesale borrowing costs which banks must pay to lend to borrowers at fixed interest rates rose this week largely in response to the June quarter inflation number coming in slightly higher than expected. Some analysts have lifted their predictions for the official cash rate and the markets are increasingly of the view that having stuffed up monetary policy last year by keeping things too loose the Reserve Bank is set to muck things up again by now making things too tight. Nice work if you can get it I guess. Economic competence doesn't seem to be a requirement any longer to work high up in our central bank.

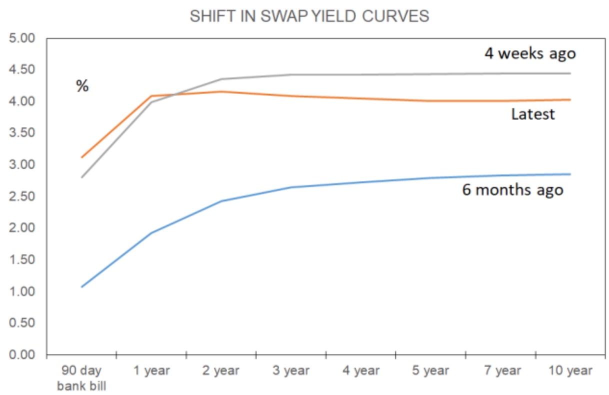
The markets are pricing in the official cash rate going from the current 2.5% to just over 4%. My view remains that the peak will be 3.5% based on inflation easing from here on out assisted by the likes of

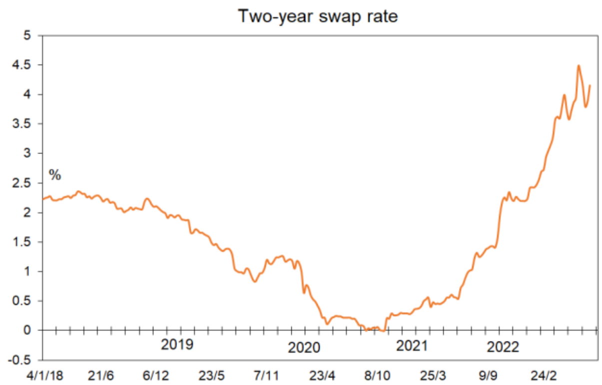
- slowing world growth,
- falls in commodity prices which have already been recorded,
- recent falls in fuel prices, and
- weakening spending by Kiwi consumers reducing the ability of businesses to recoup higher input costs.

But these days we can't really pick what our central bank will do given their focus is diverted

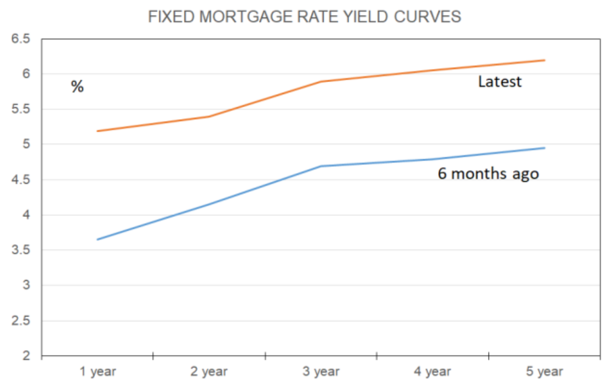
towards other things, the personalities involved are not suited to the job, and competence is low. So, anything's possible over the remainder of the year.

Because the markets believe the Reserve Bank will go too far then have to quickly pull back, the wholesale yield curve is now inversely sloped – negative. The two-year swap rate now sits near 4.16% from 3.9% last week while the five year rate is near 4% from 3.75% last week.





There have been no changes in fixed mortgage rates over the past week.



My current expectation for the one-year fixed mortgage rate in July each year is shown in the first column of the table below. I focus on that rate because there are many people who have fixed one-year repeatedly since 2009 and the strategy has worked very well.

The second column shows what the one-year rate will average over the next 2-, 3-, 4-, and 5-year periods. The last column shows the current best 2 – 5 year fixed rates charged by the lenders I track.

	Forecast 1 year rate	Rolling average rates	Current fixed averages	
2022	5.19		5.19	1 yr
2023	5.75	5.47	5.39	2 yr
2024	5.00	5.31	5.89	3 yr
2025	4.25	5.05	6.05	4 yr
2026	4.00	4.84	6.19	5 yr

If these forecasts prove correct (I'd give that a 10% probability), rolling one-year fixed will deliver an average rate for the next two years of 5.47%, three years 5.31%, four years 5.05%, and five years 4.84%.

If I were a borrower, what would I do?

I'd probably just fix one year largely with a small amount only fixed for two years.

To see the interest rates currently charged by major lenders go to www.mortgages.co.nz

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