

# Home Truths

14 November 2018



## Here we go

Back in August Home Truths predicted a short, sharp lift in the housing market around New Year. Previously, we had been sounding warnings that various tax policies and the foreign buyer ban would cause house prices to flatten or decline over the long term. But then the Reserve Bank changed its stance and wholesale interest rates fell sharply. We predicted an imminent drop in fixed mortgage rates, which in turn would cause a short, sharp boost to house prices. This was a short-term prediction, not a change to our long-run view on house prices, which remained fairly negative.

Three months on, mortgage rates have fallen and there are clear signs that the short-term housing market boost is upon us. October REINZ data registered a large 9.3% lift in house sales (seasonally adjusted by Westpac). Remember, REINZ tends to understate sales when it first releases its data, so the true extent of the lift in sales is probably even larger than that. The lift in sales was most heavily concentrated in Auckland. Corroborating the idea that the market has perked up, the number of days taken to sell a house fell from 38.2 to 37.2, which is about the level it was at back in April (all figures seasonally adjusted).

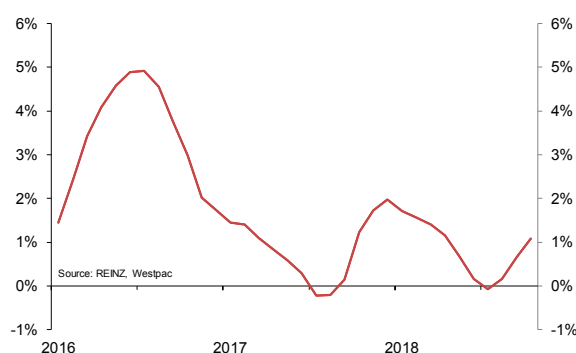
Price data for the month was fairly subdued – nationwide house prices rose 0.4% in the month of October, which is 5.4% annualised. But looking at the three month averages, it is clear that the rate of house price inflation has lifted recently. The acceleration is coming from Auckland and Canterbury, which have shifted from slightly falling to slightly rising house prices, and from Otago and Southland, where house prices are rising fast and accelerating. Meanwhile, the rate of house price inflation in Wellington and a few nearby regions has eased a little.

House sales are a fairly reliable guide as to the short-term outlook for prices. A lift in market turnover like we have

## REINZ housing data, Westpac seasonal adjustment

	Oct-18	Sep-18	Oct-17
House sales, number, s.a.	6802	6225	6061
Mth % chg	9.3	-0.5	2.8
Ann % chg	15.5	-0.6	-13.0
Days to sell, sa	37.2	38.2	36.2
House Price Index (s.a.)			
Mth % chg	0.4	0.6	0.6
Ann % chg	3.8	4.0	3.4

Figure 1: REINZ house price index, three month average versus previous three months



seen this month is a fairly good indicator that house price inflation is set to accelerate further. We remain comfortable forecasting roughly one and a half percent house price inflation in the March quarter of 2019.

Once again, we are seeing clear evidence that the most important driver of house prices is interest rates. But mortgage rates will not keep falling forever. Actually, wholesale fixed interest rates have risen quite sharply over

the past week or two. That should at least arrest the decline in fixed mortgage rates, if not reverse it. This is why we think the current housing market upturn will be short-lived.

We remain convinced that mortgage rates will eventually rise significantly. At that point, we expect the housing market to be severely impacted. But with the Reserve Bank looking very keen to keep the OCR low for some time, this is more a story for the 2020s than the current decade. We are forecasting falling house prices in the early 2020s.

The other reason to be circumspect on the long-run outlook for house prices is government policy. We were surprised that today's data showed no evidence that the foreign buyer ban, which came into force in late October, is affecting the market. However, we do believe that the ban will have a bearing on house prices eventually. Next year the market will be impacted by changes to the rules around tax deductions for property investors. And if a capital gains tax is introduced, the impact on house prices will be large.

Even though the short-term outlook for house prices is positive, the long-term outlook remains negative.

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