ECONOMIC BULLETIN

House price update.

25 Jun 2024 | **Kelly Eckhold**, Chief Economist | +64 21 786 758 | kelly.eckhold@westpac.co.nz | X: @kellyenz

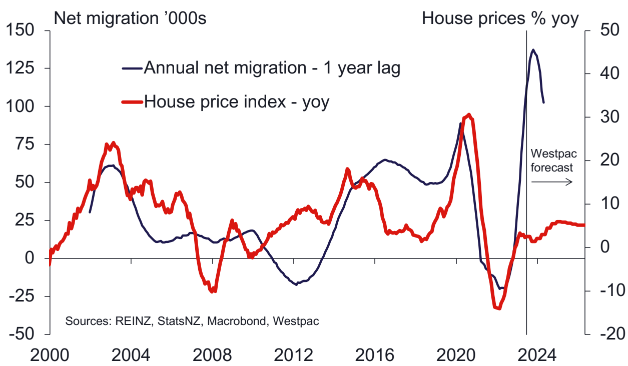
Housing market in hibernation

- **We are revising down our forecast for house price growth for 2024 but have revised down our 2025 forecast more modestly.**
- **We now expect 2.1% house price growth in 2024 – down from the previous 5.8% forecast.**
- **Slow momentum in the housing market since the 2023 election combined with the RBNZ's "tough love" message of keeping interest rates high for longer are the key drivers.**
- **Prices are expected to rise 6% in 2025.**
- **House prices will benefit from lower interest rates in 2025 and ongoing housing shortages as construction remains weak and population growth continues.**

Time for the forecast to reflect recent trends.

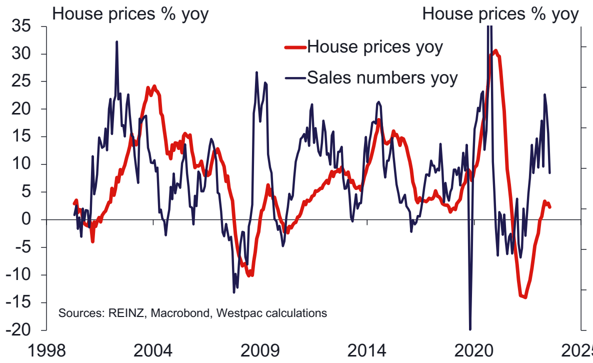
Since August 2023 we have had a relatively positive view of the house price cycle, in that we have expected house prices to outperform inflation more generally. The key driver of this view has been the historically strong population growth seen since early 2023. This population growth, which has coincided with a slowdown in the construction sector, has led to pressure on rental markets that we expected would ultimately push house prices higher with the usual lag.

Annual net migration (12-month lag) vs house prices - yoy



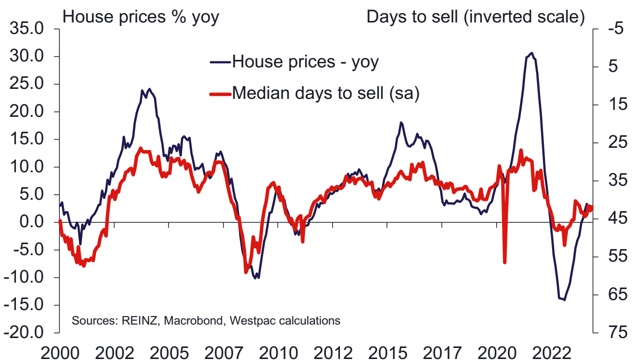
House prices did pick up slightly from around May 2023 until the General Election and we did see some modest house price growth in the first quarter of 2024 that was close to expectations. However, momentum in the housing market has decidedly slowed since around the middle of last year. Indeed, growth in house sales has been flagging in recent months, just as we would have expected some resilience in market activity based on our previous house price forecast.

House prices versus number of sales



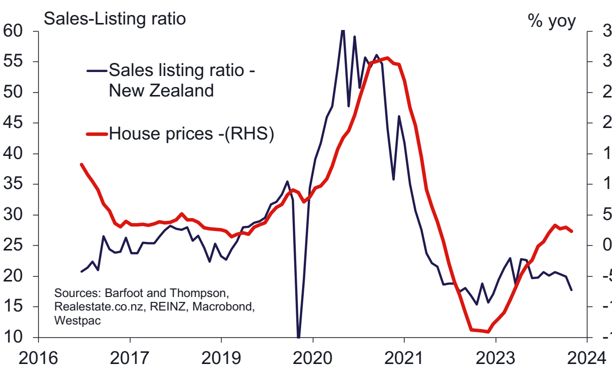
Median days to sell have stabilized at modest levels at around 42 days (seasonally adjusted). This pace of activity is generally associated with house prices growing close to the rate of inflation and somewhat lower than the average rate of house price growth seen post-GFC and pre-Covid (6.5% per annum from 2010-2020).

House prices vs median days to sell



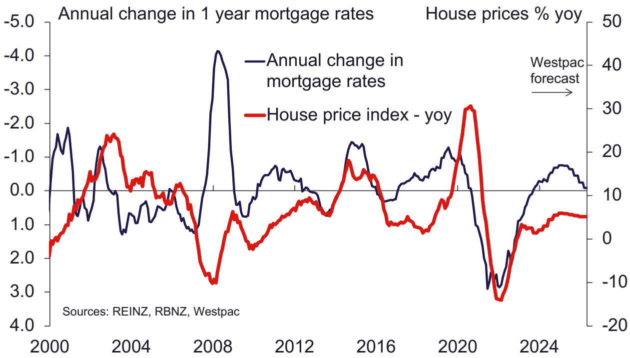
The ratio of sales to listings peaked in mid-2023 and has not been recovering in recent months. As sales volumes have remained modest, listings have tended to increase – consistent with the market turning into a "buyers' market" in recent months.

Nationwide sales-listings versus house price growth



One key factor that has been leaning against house price growth and activity has been the RBNZ's policy stance. There is a reasonable relationship between changes in short-term mortgage rates and house price growth. We had seen the prospect of OCR reductions from early next year as a factor that would increasingly provide support to the housing market (and the economy more generally) as 2024 went on.

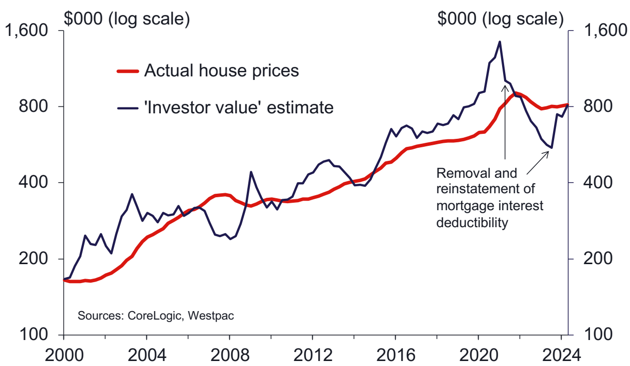
Annual change in house prices vs change in mortgage rates



However, the RBNZ's stance has hardened in recent months reflecting the still uncomfortably high inflation outlook. In contrast to our own expectation of a lower OCR from February 2025, the RBNZ has indicated a longer period before lower interest rates become a realistic prospect. We think this more pessimistic view has been reflected in the downturn of many economic growth and confidence indicators in recent months – the housing market included. While this pessimism persists, it seems hard to see a significant pick-up in house prices in 2024.

Finally, our long-running 'investor value' model suggests that the housing market is roughly fairly valued now. While the 'investor value' is not a forecast, we find that house prices tend to gravitate towards it over time. Rising mortgage rates and the removal of interest deductibility for investors in 2021 meant that the housing market had turned overvalued since early 2022; the new Government's commitment to restore interest deductibility has removed this downward pressure on prices, rather than providing a substantive boost.

Westpac 'investor value' model of house prices



Hence, we have scaled back our expectations to reflect close to 2% house price growth in 2024, and a more modest downgrade to 6% growth in 2025. We continue to take a more optimistic view of house prices in 2025, as this will be a year when the OCR falls (and likely a bit earlier in the year than the RBNZ is currently indicating). The ongoing mismatch between housing demand and supply remains. The impact of that mismatch (and ongoing above general inflation rent increases, plus improvements in investor tax treatment) points to higher house price inflation in 2025.

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