

# Home Truths

10 December 2014

## What does oil have to do with the price of houses?

Today the Home Truths team has upgraded its New Zealand house price inflation forecast for 2015 to 7% (previously 3.5%). We would expect Auckland to outperform that national average, while other centres may underperform.

We have long been arguing that the housing market would respond vigorously to falling mortgage rates and booming population growth once the election had passed. Today we are further upgrading that already-bullish view.

The reasoning for this further upgrade may seem oblique at first – global oil prices have plunged to their lowest level in five years. But the chain of reasoning is actually quite simple.

Cheaper oil is sure to suppress inflation in New Zealand. We now expect that inflation will drop below one percent, and stay below one percent, until September 2015. As a result it now looks unlikely that the Reserve Bank will increase the OCR in 2015 at all. If anything, financial markets will probably start speculating on the possibility of OCR reductions. The Reserve Bank is unlikely to oblige for reasons that will become obvious in the next paragraph. But if financial markets do get the idea of OCR reductions in their minds, wholesale fixed interest rates will fall. And that will drag fixed mortgage rates down. We are forecasting a quarter-percentage point reduction in two-year fixed mortgage rates over the coming few months.

For the housing market, a further reduction in fixed mortgage rates would be like spiking the punch at a party – things will get raucous, or even a little out of hand. Population growth is booming. The economy is strong. The election has passed. Interest rates are low. Everything points to a housing market resurgence.

Rising house prices will worry the Reserve Bank from a financial stability perspective. With the OCR pinned down at 3.5%, the RBNZ will have only one remaining option for dealing with errant house prices – macroprudential tools. We now expect that at some point over the coming year the Reserve Bank will either tighten its limits on high-LVR mortgage lending, or to enact some other form of macroprudential restriction with a similar effect.

## Proof in the pudding

The latest data on the housing market has more than vindicated our view that the market would take off at the tail end of 2014. Real Estate Institute data registered a 14.2% increase in seasonally adjusted house sales for the month of November. That was the biggest monthly increase in house sales since 2008. The REINZ house price index lifted 2.4% in the month, which was the biggest increase in a single month since 2005.

Unsurprisingly, Auckland has experienced the biggest lift in house sales. However, most other regions also saw activity levels lift strongly, with Waikato and Otago the most notable standouts.

The REINZ housing market activity data is corroborated by other evidence, such as mortgage approvals data and listings on realestate.co.nz, all of which have surged in the past month or two. On the price front, the the QV measure house price inflation (which is generally the most accurate) is actually still subdued, having registered only a 0.7% increase in house prices over the three months to November. We think it is only a matter of time before the QV measure catches up with the other data, and registers an acceleration in house price inflation.

### REINZ housing data, November 2014

	Nov-14	Oct-14	Oct-13
<b>House sales, number, s.a.</b>	7176	6286	6631
Mth % chg	14.2	4.3	-6.2
Ann % chg	6.5	-2.5	2.1
<b>Days to sell, sa</b>	37.6	37.8	34.5
<b>House Price Index (s.a.)</b>	4062.3	3965.7	3818.6
Mth % chg	2.4	0.7	1.0
Ann % chg	6.0	3.9	9.9

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