

House prices: Three factors, that keep them climbing and three that might not

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Despite seven months of COVID-19 including four weeks in full lockdown, the New Zealand property market has defied expectations and continues to reach new highs compared with the previous five years.^[1] In fact, in August 2020, the number of residential properties sold in New Zealand was 24.8% higher than August 2019.^[2] This article analyses possible reasons behind the steady climb of New Zealand property prices and speculates possible future trends in the property market.

Ever since New Zealand's first COVID-19 case on 28 February 2020, the virus has continued to impact the lives of New Zealanders socially and economically. The increase of positive coronavirus cases throughout March and April saw New Zealand close its borders to foreigners and New Zealand go into its first lockdown under alert level 4 on 23 March. Due to the bubble restrictions imposed by the different alert levels and diminishing economic activities, one would have expected to see economic declines in many markets, including the property market.

Reserve Bank lowers interest rates

The Reserve Bank of New Zealand (RBNZ) projected negative economic implications of COVID-19 on New Zealand markets and in anticipation they lowered the Official Cash Rate (OCR) to 0.25% on 16 March 2020.^[3] This is the lowest the OCR has been since its inception in March 1999. The OCR is adjusted as part of the RBNZ's monetary policy to maintain price stability in the market and support maximum sustainable employment. Correspondingly, the reduction in OCR has caused market interest rates to fall, including mortgage interest rates.^[4]

Loan to value restrictions removed

Low mortgage rates as low as 2.49%^[5] combined with the removal of loan-to-value ratio (LVR) restrictions at the start of May 2020 for at least 12^[6] months produced a lower barrier for entry into the property market for many households and investors. Investors are especially motivated to move their investments elsewhere as term deposit rates fall as a result of the lower interest rate. Investment in the property market presents more promising returns during this period of uncertainty. This increase in demand due to cheaper borrowing costs likely is one of the factors driving the continuous growth in the property market.

Net migration gain drives demand

Over the past three quarters, the world witnessed New Zealand's ability to effectively combat community transmission of COVID-19. With relatively lower COVID-19 cases and only a small number of COVID-19 related deaths compared to the rest of the world, New Zealand is increasingly seen internationally as a safe haven. While New Zealand closed its borders to most international visitors in March, the borders remain open for returning New Zealanders. Whether it was due to uncertainties in the overseas job market or the newfound perception of safety in New Zealand, Statistics New Zealand found a net migration gain of approximately 16,000 New Zealand citizens for the year ended June 2020^[7]. This is a record amount of net New Zealand citizen migration compared to previous years, where New Zealand continuously experienced net citizen migration losses. Overall, for the year ended June 2020 the population of New Zealand experienced a gain of 2.1%^[8]. This increase in population likely also contributed to the demand for property in New Zealand. Faced with a sudden shock in demand and not enough supply of properties to meet the needs in time, prices in the property market were likely to be driven higher.

End of the wage subsidy

Despite the seemingly upward-facing trend in house prices in recent months, we may not have seen all of the effects of the coronavirus on the property market yet. The 12-week wage subsidy scheme introduced by the Government on March 17 has since been extended for another 8 weeks. Further, a 2-week resurgence wage subsidy was implemented for the period from 21 August to 3 September. The multiple weeks of various wage subsidies have supported at least 350,000 jobs as at 28 August 2020^[9]. One of the conditions before businesses can receive any of the wage subsidies is that the business must retain the employees in the application for the period of each subsidy. If no further wage subsidy policies are introduced, the New Zealand economy may soon face the brunt of the impact from COVID-19. Some businesses that were previously able to maintain the employment of their staff due to the wage subsidies may no longer be able to keep all of their staff employed. A higher level of

unemployment is likely to occur across industries, especially tourism and travel. Higher levels of unemployment is likely to dampen the current high demand for properties in the market as households face increasing financial instability.

Mortgage deferral programme finishes

Another policy which may have direct impacts on the property market is the regulatory guidance for the mortgage deferral programme, which from 27 March has helped lenders support customers that are financially affected by COVID-19. Although the guidance was due to expire on 27 September, the RBNZ has extended the scheme until 31 March 2021^[10]. After the scheme expires, Banks will no longer apply the same concessionary regulatory treatment to customers wanting to defer, and customers will have to go through the usual rigorous application process. Coupled with increased unemployment, more households may find that they are no longer able to meet their mortgage repayments, resulting in increased numbers of foreclosures and correspondingly greater supplies of properties in New Zealand.

Overseas Investment Act changes

In the predicted economic downturn, overseas investment will be vital to contribute to economic growth. As part of a suite of changes to the Overseas Investment Act made in June, there is now more flexibility for the trading of loans and related security arrangements. The changes also included confirmation that loan origination, by itself, does not raise overseas investment issues. Those changes reflected the importance of lending to New Zealand's economy, and to the recovery from the impacts of the COVID-19 pandemic.

Further, a series of "standing consents" for certain listed issuers, managed investment schemes, and for transactions involving certain types of land that is sensitive only because it adjoins other land (eg, a small local Council reserve) will reduce the regulatory burden for investors. Those standing consents effectively brought forward permanent changes contemplated by the Overseas Investment Bill (No. 3), which had not completed the legislative process before the last parliamentary term ended.

That said, the changes mentioned above are unlikely, in our view, to materially impact on the residential property market, given that the acquisition of residential property by overseas persons remains squarely within the scope of the regime.

With the No. 3 Bill expected to proceed through the legislative process once a new government is formed, it remains to be seen whether the perceived risks-versus-benefit assessment of foreign investment (including in residential property) will remain the same in light of a significantly different outlook for the New Zealand economy.

Watch this space

As we all know past performance is no guarantee of future returns. With COVID-19 continuing to disrupt the economy there is definitely no guarantee that the gravity defying performance of New Zealand house prices will continue. Then again it just might.

This article was written by [Terence Ng](#) (Partner), [Susie Kilty](#) (Partner) and [Sunny Yu](#) (Law Clerk).

[1] <https://www.interest.co.nz/charts/real-estate/median-price-reinz>

[2] <https://reinz.co.nz/Media/Default/Statistic%20Documents/2020/August/REINZ%20Monthly%20Property%20Report%20-%20August%202020.pdf>

[3] <https://www.rbnz.govt.nz/monetary-policy/official-cash-rate-decisions>

[4] <https://www.asb.co.nz/content/dam/asb/documents/reports/home-loan-rate-report/home-loan-rate-report-26August-2020.pdf>

[5] https://www.nzherald.co.nz/property/news/article.cfm?c_id=8&objectid=12357309

[6] <https://www.rbnz.govt.nz/news/2020/04/reserve-bank-removes-lvr-restrictions-for-12-months>

[7] <https://www.stats.govt.nz/news/international-travel-and-migration-patterns-shift-due-to-covid-19-pandemic>

[8] <https://www.stats.govt.nz/information-releases/national-population-estimates-at-30-june-2020>

[9] <https://www.msd.govt.nz/documents/about-msd-and-our-work/publications-resources/statistics/benefit/2020/monthly-public-update/data-file-monthly-benefits-update-july-2020.xlsx>

[10] <https://www.rbnz.govt.nz/news/2020/08/reserve-bank-extending-mortgage-deferral-scheme>

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