BNZ Weekly Overview

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Mission Statement

To help Kiwi businesspeople and householders make informed financial decisions by discussing the economy and its implications in a language they can understand.

Close Enough

Back in March 2014 we ran our final BNZ-REINZ Residential Market Survey asking licensed real estate agents the question about the proportion of their dwelling sales made to people located offshore. (See page 5 in the link below) The estimated proportion was 6.4% with the offshore definition including not just foreigners but Kiwis located offshore as well. Broken down by where the people were located the agents suggested 25% in China, 20% in Australia, 11% in the UK, and a big mixture beyond that.
http://tonyalexander.co.nz/wp-content/uploads/2014/03/BNZ-REINZ-Survey-March-2014B.pdf

I mention this because on Tuesday afternoon this week Land Information New Zealand released data on land title transfers between January and March this year regarding the proportion of the 45,114 registered transfers being made to people with offshore tax residency. Their estimate was 3% - well off Labour's 39% but probably with a downward bias caused by Chinese buyers finding it harder to get funds offshore since a year or so ago, time taken for offshore buyers to get around to getting an NZ IRD number, people on student and work visas not being correctly coded, and some people having brought forward their purchases to before the October 1 commencement date for the rules.

Allowing for that bias and 10% of transfers reflecting sales before October 1 then our 6.4% estimate seems pretty good especially when you consider this. There were 45,114 land title transfers but only 21,866 dwelling sales which we can round up to 22,000 at least to allow for the small number of sales not through members of the REINZ.

That means half the land transfers were not sales, and it is possible that few of those transfers would have involved foreigners. (Or not, who knows?) So one can run a case for saying that not 3% but 6% of sales went to people offshore.

Regarding where the offshore tax residency buyers were located LINZ reported 28% in China, 27% in Australia, 9% in the UK, and a big mixture beyond that.

Our March 2014 survey produced an estimate that 12% of sales in Auckland were to people offshore. The estimate using LINZ data is 4%+ or 8% removing transfers unrelated to sales, so our survey was more accurate nationwide than at the regional level where naturally statistical sampling errors are always higher.

The 3% estimate from LINZ (even 6%) is low enough that we can kick into touch any likelihood of restrictions on foreign buyers appearing in the near future including a land tax or stamp duty, though there would still seem plenty of electoral support for some rules. I still support adoption of Australia's long-standing rules whereby Kiwis and Aussies can buy what they want in Australia but all other foreigners can only build new houses and not buy existing ones. I support such a rule because of an expectation that sales offshore will grow in coming years and become more of an issue as more people look to get their assets off the Chinese mainland, and because having restrictions in place will refocus attention on the true cause of Auckland's soaring prices – a shortage of supply. And that is the key point we have been making since the middle of 2009 and to some extent also late-2008.

Migration

Following on from the very good jobs growth numbers released last week there were a few articles in the media along the lines of too many foreigners coming into the country and that if they were not coming in Kiwis would be able to get jobs so the unemployment rate would be lower than it is. The impression given is that we are being swamped with migrants. This is not correct though it is correct to say the unemployment rate would be lower with fewer migrants.

In the year to March 2012 NZ suffered a net migration loss of 3,383 people. The unemployment rate was 6.8%. Ahh the good old days eh? Now the net migration gain is 67,619 and the unemployment rate is 5.7%. Shocking. The horror.

The change in the total flow is 71,002. Of that change 31,317 is fewer people leaving. So the flood of migrants is reduced to a boost of 39,685. Of that number 10,176 were Aussies and Kiwis who have a legal right to come here just as we have a legal right to hop over to Australia when things get too boring, claustrophobic, and small minded in NZ. The foreigner surge now reduces to 27,699.

Of that 27,699 change from 2012 to 2016 11,553 is accounted for by more students coming to study long-term in New Zealand. This is an important source of foreign currency earnings. The net migrant boost compared with 2012 now falls to an extra 17,523 people.

Can we calculate the proportion of the 204,000 increase in jobs since 2012 taken up by migrants? This is unfortunately not possible. You will get a big upward bias to your estimate because if you add up work visas over the period you'll count people who stayed only just over a year, and if they were replaced by another working migrant then you'll get two people but just the one position and an over-estimation of the proportion of extra jobs going to migrants.

In summary all we can say is this. The annual migration change since 2012 has been 71,000 of which 31,000 is fewer people leaving so extra inflows are 40,000 of which 10,000 are Kiwis and Aussies and 12,000 are students, leaving an actual foreign migrant "boom" of only an extra 18,000 people compared with 2012. They account for just 25% of the migration surge and if you wanted to cut the current net migration gain back to the long-term average of 10,000 you would need to stop 58,000 people from migrating here in the past year. Given that excluding Kiwis, Aussies, and students the gross migrant inflow left is 60,010 you would have to have prevented all non-student foreigners from coming in. That seems fairly unrealistic.

Uncertainty

One of the key themes we have been pushing for six years now has been that forecasting has become extremely difficult post-GFC. We have now and then tried to flesh out some factors behind the surge in inaccurate forecasts including changes in consumer behaviour, the availability of new technologies, changes in institutional arrangements and so on. On top of all these "special" factors we currently have one of the biggest gatherings of specific uncertain events we have seen for a number of years. To whit...

The US Presidential election. Will Donald Trump win? What will his policies be? How will other countries react? What will it do to US consumer and business sentiment, the US sharemarket etc.?

Tightening US monetary policy. How will the housing market, consumer spending, business investment react? How much tightening will occur?

UK June 23 referendum on EU membership. Will people vote to leave? What will the economic impact be over what period of time? By how much are forecasts of the costs of Brexit overblown?

China's economy. The old drivers of surging exports, cheap labour, and construction have weakened but household spending and services are not rising strongly enough to deliver confidence that employment growth will remain strong. How slow really is growth now? How bad is the debt situation? What extra stimulatory measures will be taken? When will over-production of many subsidised products cease?

Australia's general election on July 2. Will Labour win and how quickly will tax rates then be put up with what impact on business sentiment, migration flows across the Tasman etc.? What impact will removing negative gearing for new purchases have on the Aussie and NZ housing markets? Will the budget deficit track in Australia lead to the government's credit rating being cut?

Europe's growth rate has improved recently but to what extent does this simply reflect the short-term impact of a fall in oil prices, weaker Euro, and unsustainable money printing? Can growth really consolidate higher without economic reforms which EU members are unwilling to implement? Will the ECB extend money printing?

Greek debt problems are in the headlines again with new debt relief being sought amidst renewed riots against laws reining in excess social spending in Greece.

Then one can add some of the longer term sources of uncertainty such as where the new equilibrium oil price really sits, will a currency war officially break out etc.?

None of this means we economists won't give you a set of forecasts. We will. But we will more strongly than ever emphasise the uncertainty attached to our numbers and the need to focus a lot more deeply on industry and firm-specific factors which can be monitored and influenced. The need for getting close to one's customers is much more than in the past and the need to be able to react quickly to the many shocks sure to come along has grown.

Housing

The Reserve Bank released their six monthly Financial Stability Report on Wednesday morning and repeated that they are keeping an eye on three risks – global financial weakness, the dairy sector, and the housing sector. While noting that they feel the NZ banking sector is in good shape they feel that risks have increased over the past six months. Noting that they have seen some rebound in the Auckland housing market and strength elsewhere, they say that as yet they are not announcing any new restraining measures. "The Reserve Bank is closely monitoring developments to assess whether further financial policy measures would be appropriate."

Such measures probably will appear because the REINZ monthly data released later in the day showed a market rising firmly. In Auckland average prices rose by another 1.8% in March after rising 4.3% in February and 5.5% in January. Prices are up 11% since December but ahead a more reasonable 2.4% since the previous peak in October last year.

In Wellington average prices have risen by 5.9% in the March quarter compared with the December quarter (Auckland 6.6% by this measure) with Christchurch up only 0.6%, the rest of the South Island 5% and the rest of the North Island 5.8%.

So outside over-supplied Christchurch prices are rising strongly and nationwide the average number of days taken to sell a dwelling at 32 days was 4.8 days faster than average.

Will the pace of price rises be slowed if the Reserve Bank introduces debt to income rules perhaps limiting borrowers to getting just 4.5 times their household income, as is the case for most loans in the UK? Yes, but if the rule is only applied in Auckland it will accelerate the pace of price rises in the rest of the country. Yet from an affordability point of view it is hard to justify applying the rule outside Auckland and effectively removing any hope for most young people of buying a house unless prices fell sharply.

That is not something likely to happen because of all the other factors in play supporting and still pushing prices higher including not just the lack of supply in Auckland, but conservative investors seeking returns better than 3.5% in a bank account and putting their existing funds to use in the property market.

Too often people have neglected to add into their housing market analysis the effect of these non-speculative investors reacting to low, falling, and expected to stay low interest rates. For these investors it is not the cost of borrowing money which is most important to them, as it is for speculators, but the return on simple bank deposits. And considering that these people have for quarter of a century endured publically funded and private enterprise advertising campaigns and warnings about the need to have more savings for their retirement, they are either cashed up having reacted to those messages, or they feel an increasingly dire need to put funds to better use.

Is it likely that debt to income rules will be introduced? No. They will disproportionately hit first home buyers and because many of these buyers are already locked out of the housing market anyway this double hit will not have the sort of price restraining impact the Reserve Bank would like. Many investors would definitely be affected. But if they have to go to a secondary source for funding 1.5% above the rate which a bank will charge them for a first mortgage they will probably do so and pay an interest rate which their historical experience tells them is still good.

The chances are that rather than introduce an entirely new rule requiring a new set of bank regulation changes the existing investor-focussed deposit requirement of 30% will be spread to the rest of the country and in Auckland raised to 50%. That seems the cleanest way of doing something.

NZ Dollar

Nothing insightful to add here this week beyond noting that huge uncertainties exist offshore and in such times the NZ economy and currency stand out as good places to park funds for a while to see how things eventually settle down.

You will find current spot rates here. http://www.xe.com/currency/nzd-new-zealand-dollar

If I Were A Borrower What Would I Do?

Opps. Last week I wrote about fixing two years at 2.39%. Actually I meant 4.39%.

If I Were An Investor ...I'd see a BNZ Private Banker
The text at this link explains why I do not include a section discussing what I would do if I were an investor.
http://tonyalexander.co.nz/regular-publications/bnz-weekly-overview/if-i-were-an-investor/

For over quarter of a century now Kiwis have been told by governments, doom-mongers, and literally tens of thousands of people working in the financial services sector that they need to save more for retirement because

-the fiscal outlook is so bad the super payment will disappear or be radically slashed
-superannuation payments will have to be abated to reflect other income and assets
-you will probably need to put a reverse mortgage in place on your house and these are very expensive
-the age of eligibility for superannuation will have to be raised
-medical costs will go through the roof amidst a shortage of health professionals and hospital beds

and so on.

In the public minds there is almost certainly now a bias toward slowly preparing for retirement by building up some assets, but without making too great a level of short-term spending sacrifice. That latter sentiment is seen in the ongoing negative household savings rate in spite of the shock of the global financial crisis, which calls into question the success of the retirement savings campaigns. In fact with the scare stories still proliferating one would have to conclude that so far the quarter of a century effort has not been successful.

Then again, they probably have in one way which has come at the cost of the current generation of young people looking to buy their first home.

We are in the midst of a shift in the housing market toward a higher proportion of this income and capital gain yielding asset being held by people preparing for their retirement. The reduction in the availability and affordability of home ownership for young people is the logical consequence of this structural ownership shift engineered by the past two and a half decades of savings propaganda encouraging people to invest in assets.

Just a quick final point made here before, but rarely made elsewhere, and with no intention of sounding clever or morbid – just factual. Saving for your retirement is a very good idea but it pays to give thought to how long you think you will be dependent upon your savings and superannuation. If you smoke, drink a lot, take drugs, are obese, engage in dangerous activities, or have one of thousands of certain ailments, then research suggests you will not live as long as people not doing/having these things. (In the United States life expectancy of white people is currently falling.) Your incentive is to save less than people pursuing healthy lifestyles and without unfortunate ailments. You can in fact "afford" to spend more on smokes, booze, burgers etc., but it would seem silly to do so.

The Weekly Overview is written by Tony Alexander, Chief Economist at the Bank of New Zealand. The views expressed are my own and do not purport to represent the views of the BNZ. To receive the Weekly Overview each Thursday night please sign up at www.tonyalexander.co.nz
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