Property values showing loss of momentum, but full picture still unclear

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3 Jun 2020

According to the May 2020 QV House Price Index (HPI) results out today, the momentum in the property market prior to the pandemic has since been lost. However, with the number of residential property sales extremely low through April and May, a clear and timely understanding of the housing market performance will take a bit more time to become clear.

The signs of the expected loss of momentum come from the monthly change in average values, which rose by only 0.5% in May, the smallest monthly gain in eight months. Given the HPI methodology includes sales over a rolling three month period, and considering housing market activity went into hibernation through April and most of May, the latest HPI results are heavily skewed towards housing market conditions in March.

Today's HPI release confirms that the market has lost some momentum, however it's likely we won't have a firm view on the trajectory of property values until sales volumes have picked up further over the coming months.

Over the next few months, property values look set for further weakness, as GDP falls and unemployment continues to rise.

We can look to Australia for what to expect as they've been operating at the equivalent of about a lock-down level 2.5 when compared to NZ (according to the University of Oxford stringency index), over the last 2 months. According to the CoreLogic Home Value Index results for May, Australian dwelling values posted their first month-on-month decline since June last year. The national index was down 0.4% over the month, however the fall of less than half a percent in housing values over the month shows the market has remained resilient to a material correction.

Back home, as the country has transitioned down through the lockdown levels over the last month, we have seen early signs of relatively strong demand for property, with would-be-buyers from prior to and during lock-down out in force.

But with lingering uncertainty continuing to dent short term confidence, its unlikely demand will bounce back to pre-COVID levels, especially as we're now into winter which typically sees less turnover. Additionally, we also head into election season which can cause further apprehension for those navigating the property market.

NZ sales volumes were down by almost 80% in April and while activity has increased in May, the market is still a long way from historic average levels of transactions. If low sales volumes persist, we could see additional volatility creeping into pricing measures.

A key constraint on transactions remains a lack of 'for sale' listings. Low inventory levels are also likely to be a factor helping to insulate housing values during a period of less buyer activity. Longer term the market remains vulnerable to downside risk, as the effects of the pandemic and resulting lock-down continue to impact the economy and employment.

As restrictions have eased over the past month, early indicators of real estate agent activity have seen an upswing. Pre-listing activity across CoreLogic’s PropertyGuru and RPNZ platforms remained strong up to the long weekend, however property appraisals generated by agents took a seasonal dip as many people took the opportunity to escape their home town for a mini-break. The first few weeks of winter could prove crucial in whether we get the lift in listings which has been so absent over the last few years.

We will await the Real Estate Institute’s HPI release at the end of next week to get a better feel for how values have performed recently, however we would again stress caution at using median sales prices to assess any market movement, as it can be influenced by a change in the composition of what happens to be selling.

While expectations of a drop in values remain, we can take some comfort from the resilience of the financial system, as reported in the recently released Financial Stability Report from the Reserve Bank (RBNZ). That resilience puts the market in good stead to navigate a short downturn. Indeed, the RBNZ has estimated that even if house prices fell by 15%, which is at the more downbeat end of most forecasts, less than 5% of people would be at risk of negative equity. And it is negative equity, together with forced or urgent sales which could be the cause of greater eventual falls, so this likely limits the downside for now.

While the immediate indicators provide a hazy view of the market, the longer term view is also highly uncertain. As government stimulus and lender leniency policies expire or taper, there is a risk that mortgage arrears could push higher, which could exert downwards pressure on home values. Spring and the post-election period could well be the telling time for the property market; if economic conditions haven’t picked up by then we could see a heightened level of risk for housing markets.

On a more positive note, the likelihood of the country moving to Level 1 sooner rather than later increases with every day that it’s announced there are no new cases (the count is currently 11 days in a row). And level 1 should bring with it further stability for the economy as well as a further reduction in the rate of newly unemployed.

Borrowers who are potentially feeling a little financially strained at present will also be supported by the fresh round of ‘rate wars’ amongst the banks, and there is likely still room for mortgage interest rates to drop further, as the RBNZ continues to put pressure on the retail banks to pass through the lower wholesale rates and support the market.

All in all, the property market is in a holding pattern to some degree at present. As sales volumes continue to increase we’ll start to get a clearer picture of recent value movements. The trajectory of home values and housing market activity will be largely reliant on how well the NZ economy responds to eased restrictions and navigates a path to recovery.