Banks started to utilise their new LVR leeway in January

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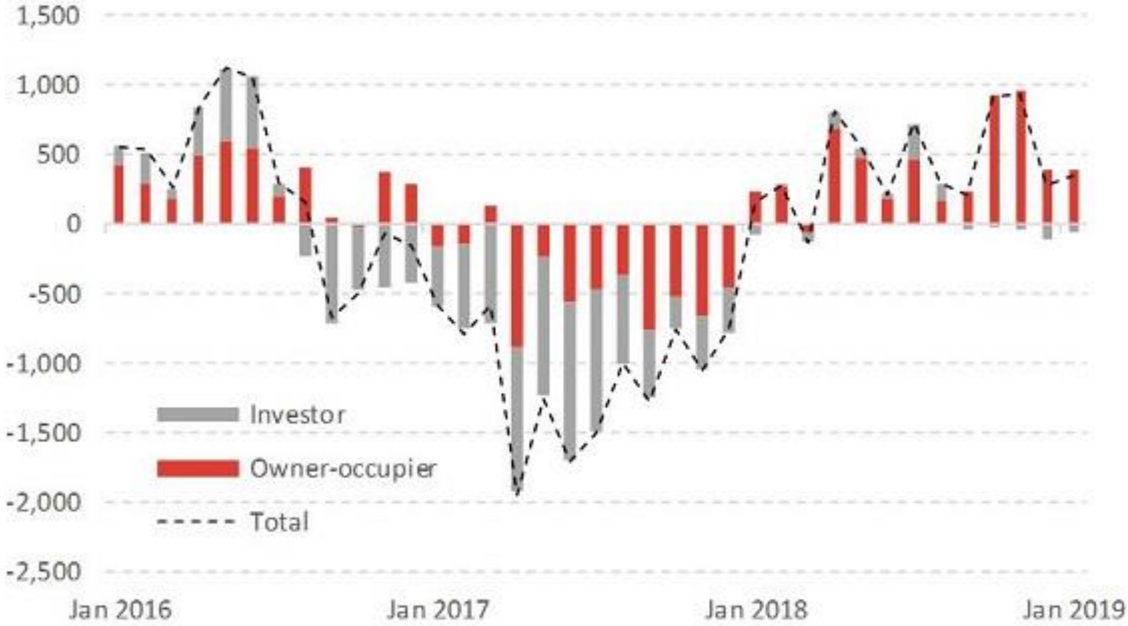
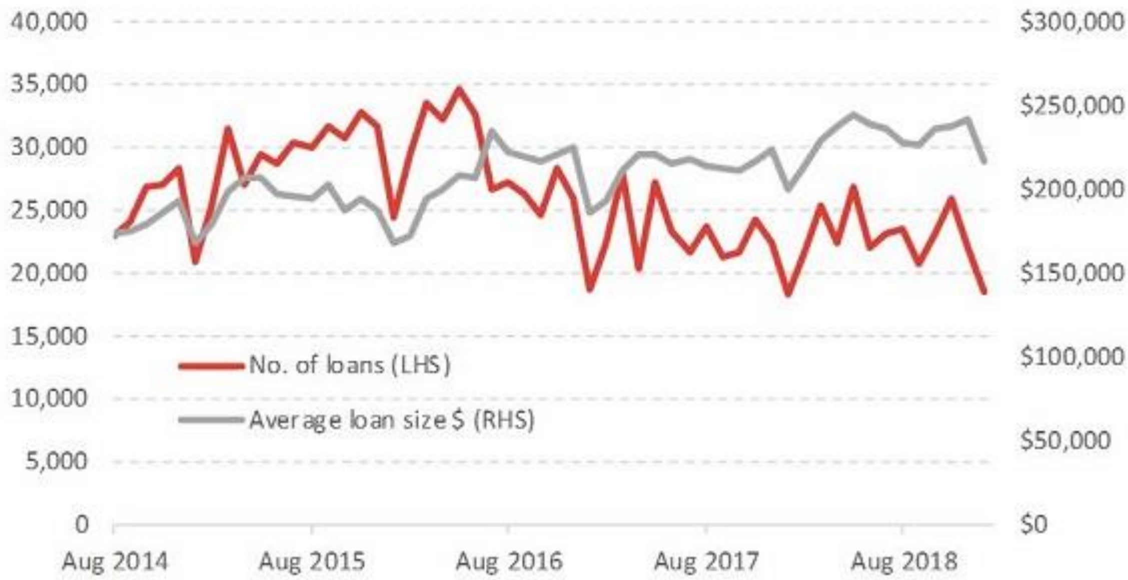
Today's figures from the Reserve Bank cover lending activity in January, so are the first available after the latest easing of the LVR rules. They provide interesting insights: showing that the banks started to use their new freedom last month, raising the share of high LVR lending to owner-occupiers from 9.8% in December to 12.1%. That is of course still well below the new speed limit of 20%, and the general air of caution amongst the banks suggests that this impetus may soon fade again.

CoreLogic Senior Property Economist Kelvin Davidson writes:

The Reserve Bank of New Zealand (RBNZ) has reported that mortgage lending activity rose again in January, the tenth consecutive monthly increase and the 12th in the past 13 months (**see the first chart**). The figure for January was $4.1bn, up by around $360m from the same month last year.

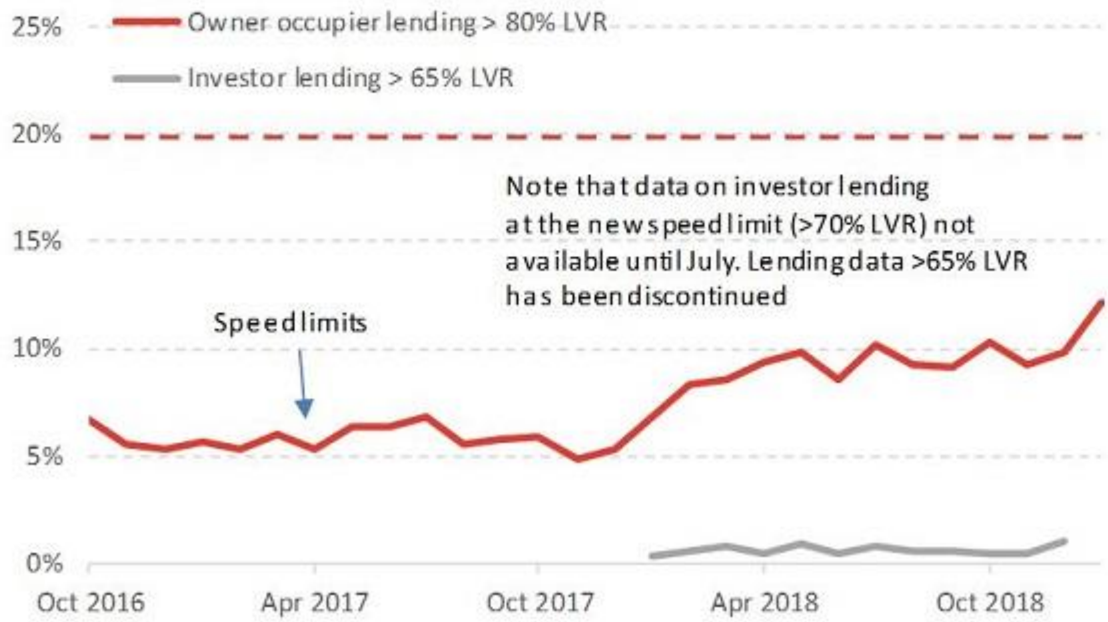


Annual Change in Lending, $m (Source: RBNZ)
Owner-occupiers contributed all of the increase, with investor flows slightly down on last year. Other detail in the RBNZ's release shows that the number of loans remained 'range-bound' in January, staying broadly within the 20,000 - 25,000 per month bracket seen for the past 18-24 months. So the rise in the total value of lending came about because of an increase in the average size of each loan. This was $216,498 in January, up by 8.1% from a year ago (**see the second chart**).



Number of loans and average size (Source: RBNZ)
This data release is of special interest because it's the first set of figures after January 1st's loosening of the LVR rules. And as it turns out, the banks started to utilise their extra leeway for high LVR lending in January. The share of owner-occupier lending at >80% LVR increased from 9.8% in December to 12.1% in

January – still a long way below the new speed limit of 20%, but certainly a step-shift in activity (**see the third chart**). Unfortunately, for investor lending at >70% LVR (loosened from 65% LVR, but still a 5% speed limit), we'll have to wait for July's release before the RBNZ has enough data to produce its stats.



High LVR lending as % of total (Source: RBNZ)
It remains to be seen whether this impetus to lending flows persists in the coming months. After all, notwithstanding January's rise in high LVR activity, the banks themselves still seem to have a pretty cautious attitude, reinforced by the prospect that the RBNZ is going to require them to hold more capital on their balance sheets in future. Then from the demand side, there's not an unlimited pool of borrowers who can actually meet the strict lending criteria currently being enforced (such as stringent expense verification and also stress-testing the ability to pay at a theoretical mortgage rate of 7-8%).

On top of that, we also now have the Tax Working Group's (TWG) recommendation for a capital gains tax on residential rental property (along with other assets too). And although there wasn't anything in the TWG's final report that came as a surprise, this just gets us one step further along the road to a more comprehensive CGT being (possibly) imposed, which will tend to add to a general sense of caution amongst potential investment buyers as 2019 progresses.

Of course, it's also worth bearing in mind that a slow and steady market is often a good thing. For example, it's likely that the LVR rules have played a role in helping to keep the banks' non-performing loans ratios* very low (**see the fourth chart**). In turn, low levels of repayment stress help the market to avoid mortgagee sales, which undermine confidence and values.

Non-performing loans ratio (Source: RBNZ)

Overall, we'd anticipate more increases in mortgage lending in 2019, but the growth is unlikely to be rampant. We wouldn't be surprised to see the share of owner-occupier lending at high LVRs rise to about 15%, then flatten off (i.e. hit the old speed limit, but stay about 5%-points below the new speed limit).

* This is the sum of loans that are impaired (whereby the bank may not receive all of the agreed principal and interest repayments) and those that are 90 days overdue but not yet impaired, divided by the total value of all loans. The figures come from the RBNZ's Bank Financial Strength Dashboard, which is updated this week, at 3pm on Friday 1st March.