No surprise to see LVR rules relaxed a little further

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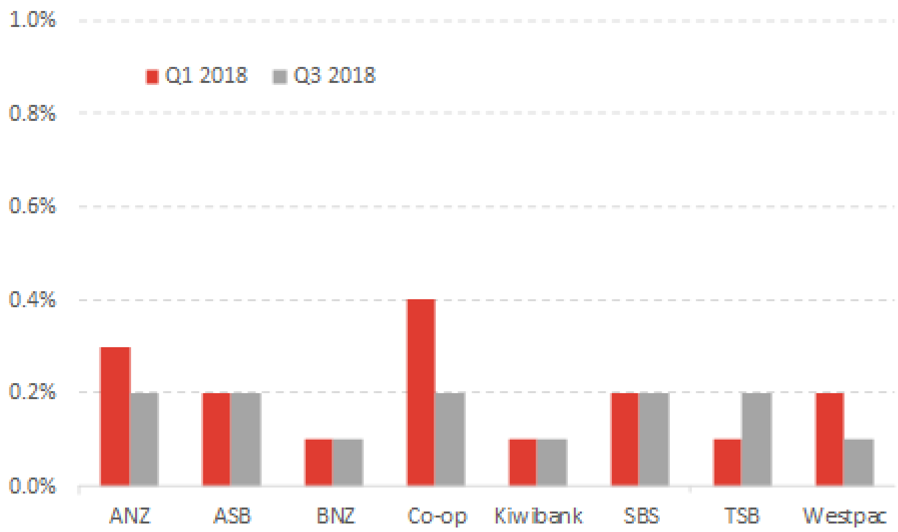
New lending data released this week highlights low non-performing loan ratios and a still-cautious approach by the banks. As expected, the Reserve Bank of New Zealand also announced a further softening of LVR rules. This may provide a kick-start to sales volumes provided more borrowers can secure loans, but it's not a guaranteed outcome: banks may still remain cautious.

CoreLogic research analyst Kelvin Davidson writes:

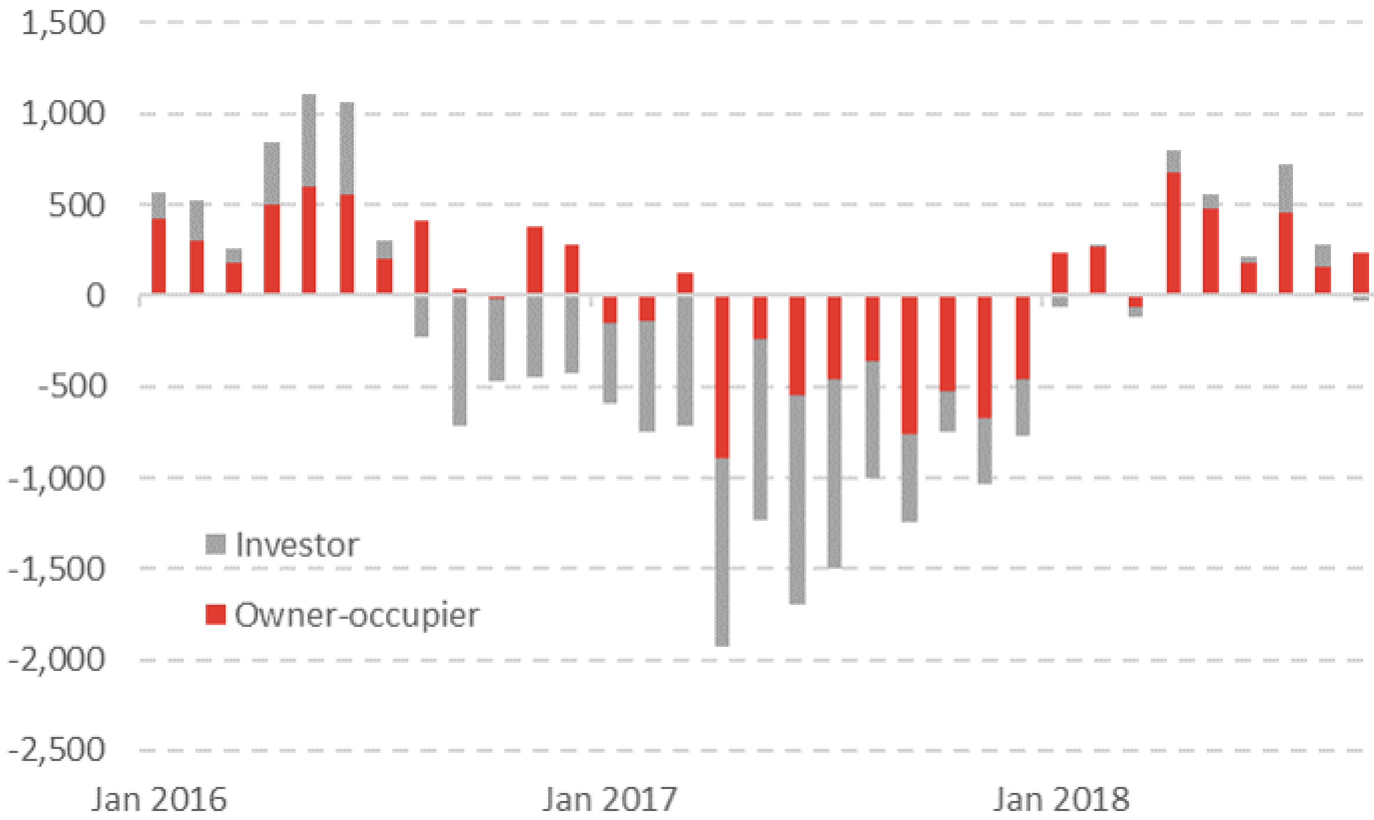
The first three days of this week have been very busy for Reserve Bank of New Zealand (RBNZ) data releases related to the housing market. This Pulse wraps up the most notable aspects from the latest releases: the key message is that residential property lending is well-controlled, hence the RBNZ's comfort in loosening the LVR restrictions earlier today.

First, on Monday the RBNZ published the latest (Q3) update to the Bank Financial Strength Dashboard, which covers a huge range of information relevant to each bank's financial resilience. From a property perspective, one of the key highlights was that the 'non-performing housing loans' ratio is very low for all main banks (see the first chart). This measures the total value of loans that are either impaired (where the bank may not get all of the agreed principal and interest repayments) or 90 days past due but not yet impaired, as a percentage of all housing loans. This figure for all main banks came in at 0.2% or less, which reflects careful lending practices, the LVR speed limits, and the strong economy (e.g. low unemployment).



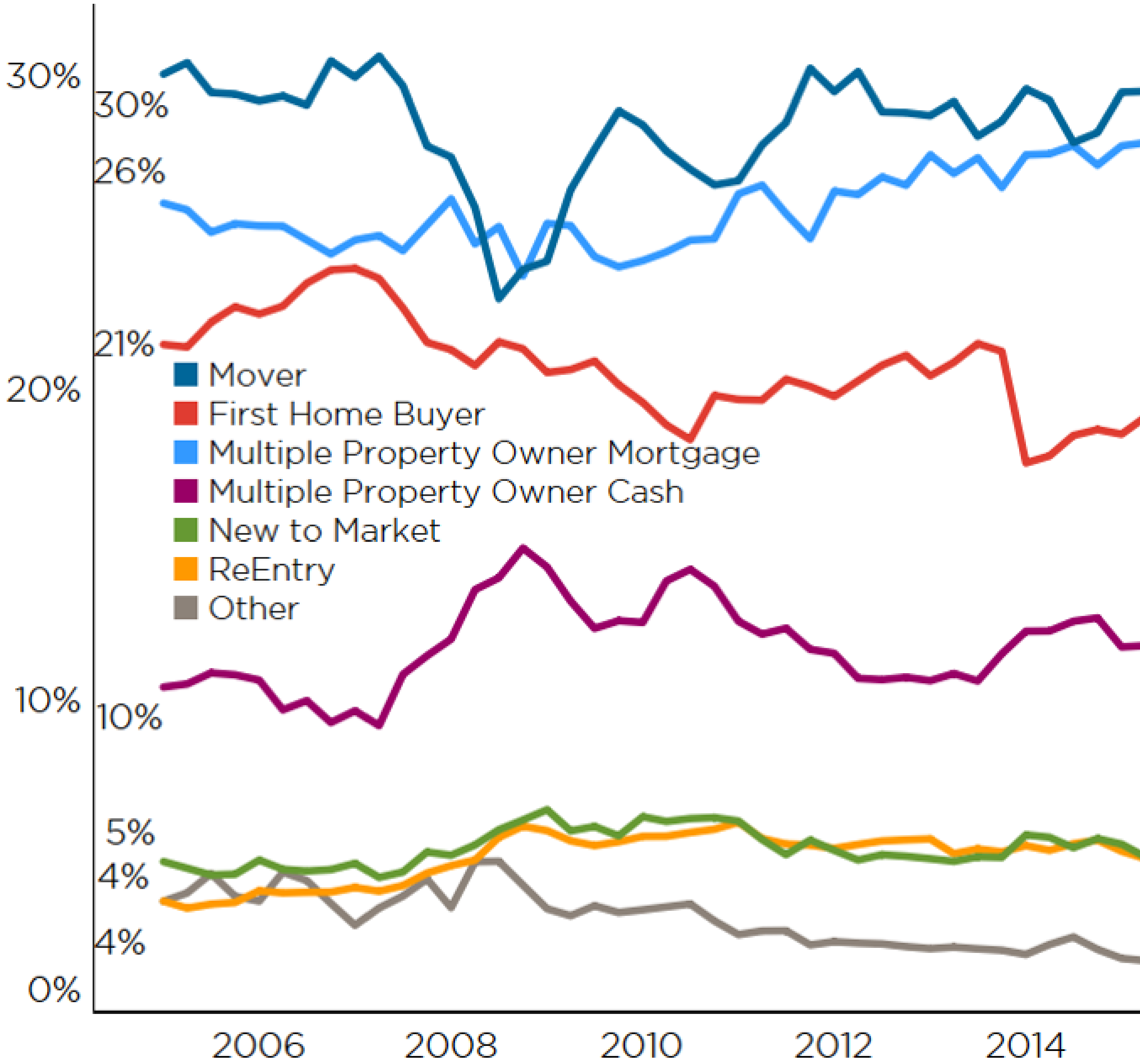
Non-performing housing loans ratio (Source: RBNZ)

Then on Tuesday the lending statistics for October were published, covering lending by LVR, borrower type, and loan type. There were two key points - first, lending flows in October were higher than a year ago, the seventh consecutive rise (see the second chart). Second, that rise came despite lenders still staying well away from the LVR limits as they were at the time, with only 10.3% of loans going to owner-occupiers without a 20% deposit, and only 0.4% of loans going to investors without a 35% deposit. The RBNZ also reported a further rise in lending to first home buyers, which is consistent with the upward trend shown in our CoreLogic Buyer Classification series (as shown in the third chart).



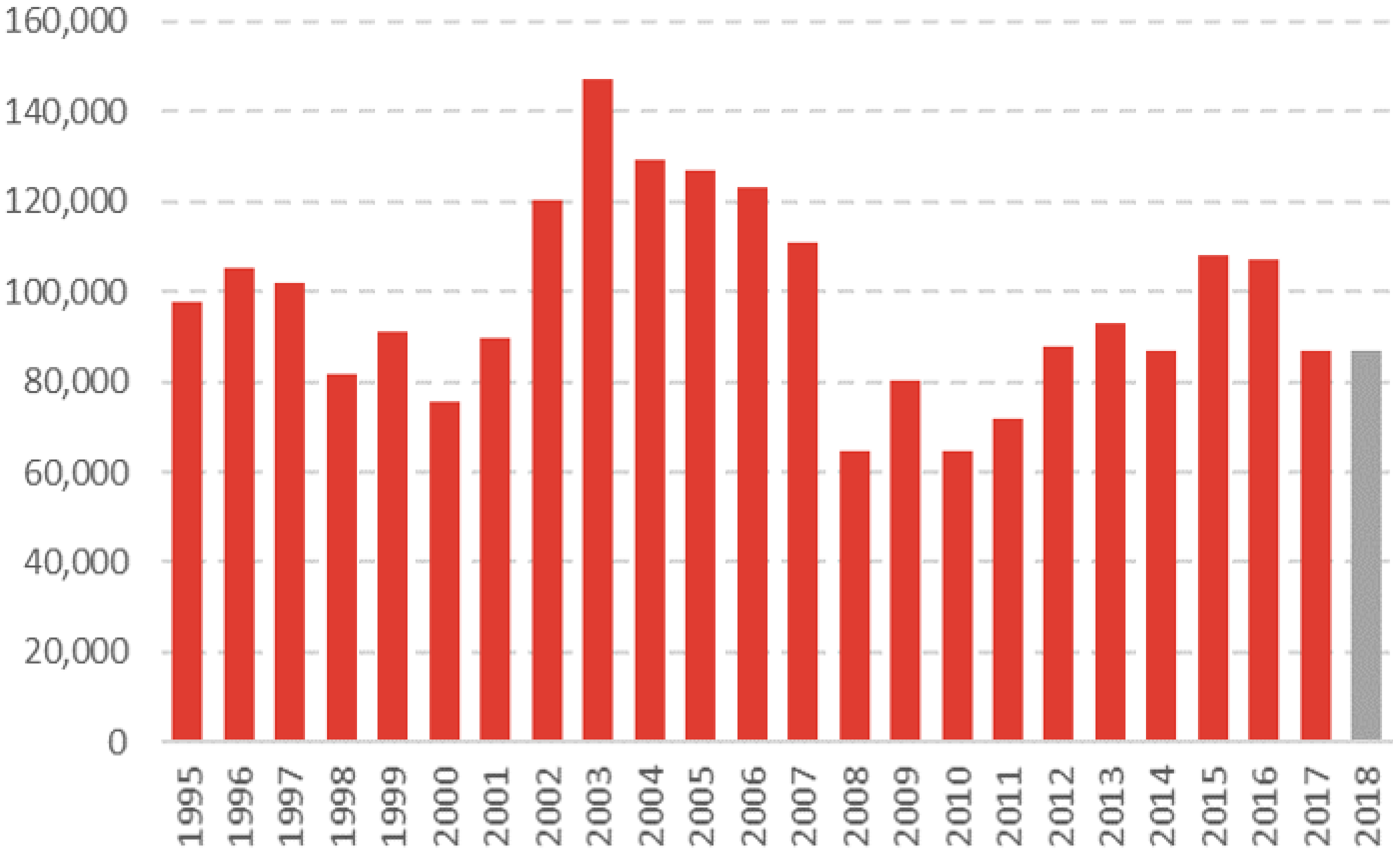
Annual change in lending ($m, Source: RBNZ)

So, how can lending flows be rising whilst banks are still showing a cautious approach to new loan standards? One explanation would be that the share of mortgage applications being approved is rising; because only the best borrowers are coming forward. These higher quality borrowers would have a sufficient deposit, be able to meet more stringent income and expense testing, and could service the debt at a hypothetical mortgage rate of 7% or more.



Share % of property purchases (Source: CoreLogic)

Given all of that, then, it was little surprise that the RBNZ announced a relaxation of the LVR rules this morning. From 1st January 2019, up to 20% (previously 15%) of new lending to owner-occupiers can have deposits of less than 20%, and up to 5% of loans to investors can have deposits of less than 30% (previously 35%). It seems likely that this will welcome in some borrowers who were previously locked out of the market, and could produce a stronger number of future property sales than our purely economic model would suggest (see the fourth chart).



Property sales (Source: CoreLogic)

But even that is not a clear-cut outcome. After all, lenders may choose to continue on their cautious path, especially since today's Financial Stability Report also highlighted the RBNZ's view that "higher capital requirements are necessary, so that the banking system can be sufficiently resilient whilst remaining efficient". In other words, a requirement in future for the banks to hold higher capital buffers would tend to dampen lending flows.

Tags: NZ Property Market , NZ realestate