

Hi John,

Confidence is back but where's the money?

*Money, get back.
I'm all right jack keep your hands off of my stack.*

To see Pink Floyd's Money video [click here](#).

Residential recovery

In my last issue of GLOBAL VIEW I discussed differing views of whether the housing market was recovering or not, and its importance in leading economic recovery generally. To read this issue [click here](#).

Well since then events have been encouraging. Barfoot & Thompson reports Auckland has been experiencing a "golden autumn" of sales continuing through June, "with sales up 5.8 per cent from the month before, and 54.9 per cent on the same month last year." Managing director Peter Thompson said the biggest challenge facing the company was obtaining new listings which had fallen to the lowest level for the past 20 months. To read the Herald article [click here](#).

This trend is supported by BNZ economist Tony Alexander in his latest Weekly Overview. In this there are headings such as "House Construction Stabilising", "Householders Gain Enough Confidence To Borrow More", and "Housing Market Continues To Firm".

Under the last heading he says "The monthly NZ Property Report compiled by the website www.realestate.co.nz shows even more clearly why those people still predicting NZ house prices will collapse have forgotten their basic economics." The report "backs up the conclusion that the availability of residential real estate stock is diminishing quite quickly."

Tony's key forecasts are:

- Dwelling consent numbers to slowly recover from the middle of this year.
- Real estate sales have bottomed for this cycle. Activity is likely to fluctuate and begin a drift upward before year end with potentially firm activity over 2010.
- House prices stabilising, rising slightly over 2010.

To read his Weekly Overview [click here](#).

Now I don't think that means you should rush out and buy a house in case you miss out on the ridiculous prices rises we saw between 2002 and 2007.

I went to Gareth Morgan's excellent Investment Adventurer seminar in Auckland a few weeks ago and bought his latest book "After the Panic". It's an excellent read and gets into what went wrong with the economy and who was to blame. There's a chapter in it called "Our economy and the Kiwi obsession with property". His view is house prices have a way to go to get back to the trend line.

So if you're buying a house, buy it as a place to live in, or get a rental return. Don't expect the massive capital gains of the past era.

Housing leads the way

But as I've said before "A major driver of New Zealanders' investment sentiment is the state of the residential property market, and this is now starting to show signs of increased activity."

Well people are starting to feel better. The recent Westpac McDermott Miller Consumer Confidence survey moved back into optimistic territory to reach its highest level in 18 months.

I think the Westpac report summed it up pretty well when they said "Since March, the weight of evidence suggests that the worst of the global downturn has passed. Sure, the global economy is still in recession and the hurdles for future growth remain large, but the fear of something much worse (think the 1930's Depression) has diminished. *It seems consumers are responding not so much to what has happened, but to what hasn't happened.*" Italics are mine. To read the report [click here](#).

Tony Alexander's survey of BNZ Weekly Overview readers last Friday reveals that a net 15% expect the NZ economy will improve over the coming year. This is down slightly from a net 18% positive in June and record 27% in May but Tony says "the minor pullback is consistent with our interpretation of recent results being a "sigh of relief" at the avoidance of an especially deep recession scenario".

Lower dairy prices affect dairy farmers

If you read the confidence report above you'll see all regions recorded an improvement in confidence with the exception of Waikato. You'd not be blamed if you thought that was a reaction to the negative news about dairy prices. Well it would be if you're a dairy farmer or a supplier to that industry.

But if you think dairy prices rule housing prices in the Waikato, or the whole New Zealand economy – as many commentators are inclined to do – I suggest you read Rodney Dickens Ravings which came out last May when one of the first of the cuts in the dairy payout by Fonterra was announced.

In this article Rodney says the facts show "that the negative impact [on housing prices in the area] would be limited compared to the stimulus in the pipeline from super-low interest rates and rising net migration". He says "the outlook for the housing market and the domestic economy more generally are drive much more by interest rates and net migration than by export prices but this hasn't brought an end to the urban legend that the agricultural/export sector is the heart of the NZ economy." To read the Ravings [click here](#).

Don't rely on the dollar going down

One last word on the New Zealand economy. If things were as bad as some people make out then the New Zealand dollar would not be getting the support it is.

There are some good articles on the prospects for the exchange rate by Rodney Dickens and Tony Alexander. Both say we cannot expect the dollar to sink to the lows some people expect in the short to medium term. In essence it comes back to how small we are in the scheme of things and where we are perceived in relation to the larger economies.

If you're in business as an exporter or an importer I suggest you read them. For Rodney's articles [click here](#) and [here](#) and for Tony's read pages 3, 4, 15 and 16 of his Weekly Overview mentioned above [click here](#).

Where's the money - and what's it going to cost?

There's no trouble in finding a residential mortgage. You just have to qualify. Sure it's harder than before but not unreasonable. It means going back to the normal days when you went to a lender with a reasonable deposit and proof you could meet the debt servicing requirements.

As far as residential interest rates are concerned the Reserve Bank has said they expect to keep the official cash rate low for the next year or so. Fixed interest rates have risen since their low point in March in response to rising offshore rates. It's a 50/50 call whether to fix or float right now.

But there's no question it's much harder to find money for commercial ventures including property and business. This is largely a result of there being far fewer lenders out there since the demise of most of the finance companies and the gradual winding up of mortgage trusts (and others which didn't qualify for the Crown Retail Deposit Guarantee Scheme hastily drawn up at the height of the global credit crisis).

Many of the non-bank lenders remaining have been hoarding funds to ensure loans that cannot be repaid or re-financed - due to the economic conditions prevailing - can be renewed. And for non-performing loans there is no point in going to mortgagee sale if there are no buyers around for that particular asset.

Lenders are also conscious reduced asset values can mean lending ratios are breached. This can force lenders to re-capitalise their own balance sheets. The recent \$40 million cash Allan Hubbard pumped into South Canterbury Finance is an example of this.

Banks are concentrating on supporting existing clients and have little to lend to new ones.

Another factor affecting non-bank lending in particular, is the Crown Retail Deposit Guarantee Scheme mentioned above. Designed to stop panic investor withdrawals, this government guarantee was put in place for two years. This means as 12 October 2010 draws closer - and with no news from government yet as to what will happen then - it makes it difficult for those institutions qualifying for the scheme to commit to loans maturing later than that date.

But the great thing about capitalism is someone always fills the hole. There are lenders out there from residential lenders requiring all the conditions mentioned earlier, through to private lenders who take a mezzanine risk for a comparable return. And some are realising in a time of low asset values a part loan part equity position can give an excellent return.

There's also the opportunity for private investors to participate in equity and quasi equity positions in property and business ventures.

The cost of money reflects the wide risk profile between low ratio loans with proven debt servicing, and loans given at a time of uncertainty about asset values, and the ability to realise them in the event of default.

If you're interested in any of the above give me a call.

Cheers

JP



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