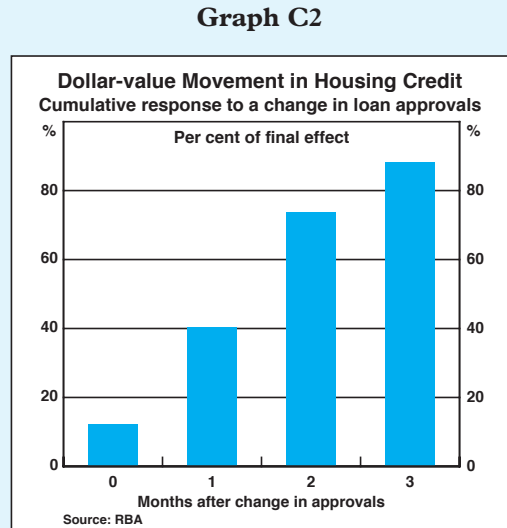


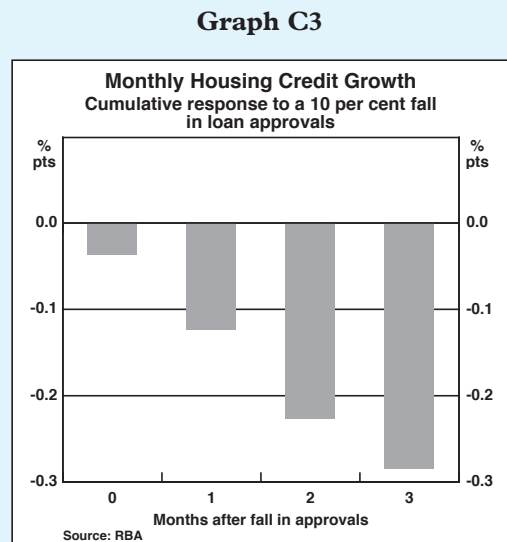
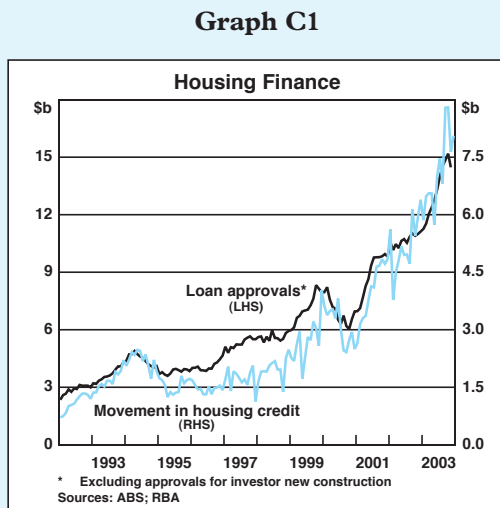
Box C: Housing Loan Approvals and Housing Credit Growth

The value of housing loan approvals and movements in housing credit outstanding track one another closely (Graph C1), although the value of approvals is typically at least double the dollar value of the movement in credit, due to repayments of principal and drawdowns of existing facilities.¹ Typically there is a 6–10 week delay between when a loan approval is recorded and property settlement takes place, so movements in credit lag the level of approvals. Indeed, empirical work suggests that it can take up to four months for the effect of a change in the level of approvals to fully flow through into a change in the movement in credit, with around 40 per cent of the effect occurring within one month, and 75 per cent within two months (Graph C2).

Given the relationship between the level of housing loan approvals and the dollar-value movement in housing credit, it is possible to derive a relationship between the *percentage change* in approvals and the *growth*



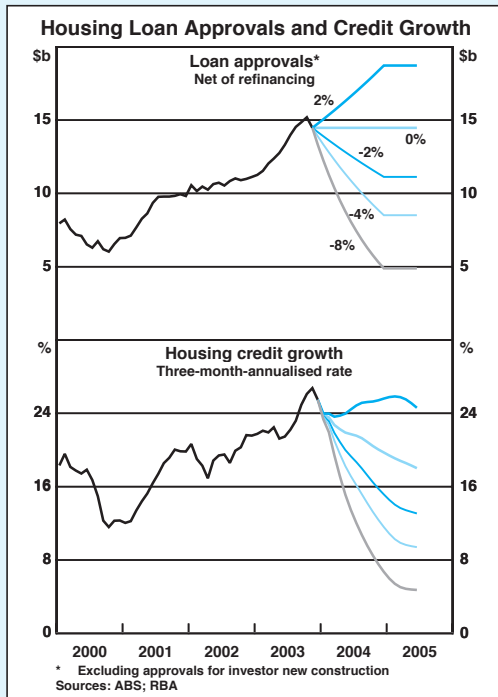
rate of credit. Again, empirical work suggests that, at current levels of approvals and credit growth, a once-only 10 per cent decline in approvals would reduce the monthly rate of credit growth by around 0.3 of a percentage point after about three months (Graph C3).²



1. Including redraws of excess repayments and drawdowns of home-equity loans.
2. The growth rate of credit would, however, continue falling over time due to the base effect from the rising level of the outstanding stock of credit. For any given growth rate of credit to be maintained, the level of approvals needs to increase over time to offset this effect.

To put these numbers into perspective it is useful to consider the likely impact on credit growth of the 5 per cent decline in the value of housing loan approvals recorded in November 2003. Assuming that approvals remain at their new lower level, housing credit growth would be expected to slow from a three-month-annualised rate of 25 per cent to a still rapid rate of around 18 per cent by mid 2005 (Graph C4).

Graph C4



It is also useful to look at the effect on credit growth of a number of other scenarios for loan approvals. If, for example, approvals were to fall by 2 per cent each month until the end of 2004, and remain constant thereafter, the rate of housing credit growth would be expected to slow to a three-month-annualised rate of 13 per cent by mid 2005. Under this scenario, approvals would fall by a cumulative 27 per cent from their October 2003 peak, to around the level recorded in early 2003.

If instead approvals were to fall by 4 per cent per month, housing credit growth would be expected to slow to a three-month-annualised rate of 9 per cent by mid 2005. Under this scenario, the cumulative decline in approvals would be 44 per cent, which, while large, would not be inconsistent with declines in previous cycles. If instead, however, approvals were to fall by 8 per cent per month until end 2004, housing credit growth would be expected to slow to around 5 per cent by mid 2005. Such a large decline in approvals is clearly outside the range of previous experience.

Finally, rather than falling, if the value of loan approvals was to grow by 2 per cent per month from the November 2003 level until the end of 2004, housing credit growth would be expected to remain at around its current rate of close to 25 per cent. ↗