



## **Submission to Housing Affordability Inquiry in Response to Draft Report dated December 2011**

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### **1. Overview**

The report represents the most extensive study of the New Zealand housing sector ever undertaken. There are no serious omissions in the extent of the inquiry with the exception that the issue of the availability of finance for development is not discussed.

I find it puzzling that there are no findings and recommendations from the first five chapters of the report which include many of the demand side issues. My submissions below cover the matters I consider to be important.

The issue of what represents an adequate affordable entry level house remains unclear both for those in need of social housing and for independent first home purchasers. Particularly for the second group there is an implication that the first home should be a new detached home on its own section. Whilst has been the New Zealand experience in the past, in the UK and Europe first home buyers often buy either second hand homes in need of modernisation or units in multi-unit developments. If such accommodation is accepted as being suitable for first home buyers, then policy should be focussed on ensuring the total stock of housing slightly exceeds demand rather than on the specific needs of first home buyers.

### **2. Chapter 2: The New Zealand housing scene**

#### **Chapter 3: Macroeconomic factors**

#### **Chapter 5: Population and demographic change.**

Box 4 on p14 sets out an excellent summary of what drove the surge in New Zealand house prices in the 2000s except it does not mention supply side inflexibility. The issues summarised are demand side issues and highlight the significance of both finance industry policies and actions, and net migration. These two issues represent the significant differences between the market in the 2000s and in the 1990s but are not followed through on in the findings and recommendations.

Given Australasian Banks were reasonably prudent during this period and that the volatility in net migration is substantially driven by volatility in outward migration it is hard to know what recommendations the Commission can make. However in terms of understanding the problem we are dealing with it is important that the findings highlight the influence on house prices of these two issues. In effect the price surge in the 2000s was driven by a combination of an asset price bubble and a surge in real demand. The surge is then exacerbated by the stickiness in the supply side that the report identifies. It is important that we understand this otherwise there is the danger we believe the problem can be solved by addressing only supply side issues.

### **3. Chapter 7: Urban planning and housing affordability**

I essentially agree with the findings and recommendations from this chapter. However I suggest:

- 1) The findings and recommendations should more clearly stress the need for planning authorities to over provide for both greenfield and brownfield land in order to ensure competition. The current paradigm being one of adequate provision.
- 2) That development and similar levies should as far as possible recover the costs of all externalities including infrastructure etc. If this is done there is no need for the planning authority to decide on the merits of greenfield vs brownfield development as the market will be able to use price mechanisms to resolve each case.

### **4. Chapter 10: The performance of the building industry**

The report provides an excellent profile of the industry and the structural issues that underpin its inefficiencies. However recommendation R10.1 is weak and optimistic. The productivity partnership is a useful but under funded initiative that spans the whole construction sector and within which the housing industry is weakly represented. It appears to have only limited support from government ministers. If the government wishes to see an improvement in productivity in housing construction it will need to take a much more proactive stance than it is currently providing.

In saying this it is also important to emphasise that the industry of the future needs to be significantly focussed on efficiently producing medium density housing rather than stand alone housing.

### **5. Finance for development**

The report does not tackle the issue of finance for development. During the 2000 – 2010 period finance for development was provided in three ways. The developers own equity, trading bank finance and finance from finance companies, the latter being referred to as mezzanine finance. Typically the developers provided minimal equity and the trading banks lent prudently. Mezzanine finance was readily available secured by mortgages and debentures that ranked behind the trading banks' interest. This enabled developers to fund developments almost completely by debt. Whilst this practice facilitated developments there was clearly a lack of prudence on the part of both finance companies and developers as a

result of which both finance companies and developers became insolvent and generally no longer exist.

The demise of the mezzanine financiers and the continued prudence of the trading banks means that currently developers need to provide significant amounts of equity in order to finance the medium and large scale developments that the Draft Inquiry Report identifies as enabling efficient construction. There are very few potential developers who are both willing and able to provide such equity and hence little development activity of this nature. Whilst in the short term this relieves competitive pressure for the purchase of development land and helps to ease land prices, in the longer run it will lead to undersupply of houses and a less competitive housing sector.

This is a significant structural issue to which the writer can offer no solution.

## **6. Further involvement**

The writer would be pleased to be involved in any further discussion on these issues.

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