

16 February 2012

Inquiry into Housing Affordability
New Zealand Productivity Commission
PO Box 8036
The Terrace
WELLINGTON 6143

Dear Sir/Madam

PRODUCTIVITY COMMISSION HOUSING AFFORDABILITY INQUIRY – DRAFT REPORT

1.0 INTRODUCTION

- 1.1 Hamilton City Council (HCC) welcomes the opportunity to make a submission to the New Zealand Productivity Commission's draft report on Housing Affordability (referred to throughout this submission the draft report).
- 1.2 The extensive research and analysis undertaken by the Productivity Commission in developing the draft report is acknowledged.
- 1.3 HCC would also like to support Local Government New Zealand's submission to the draft report, particularly their comments around the Productivity Commission's 'push' for the release of significant tracts of Greenfield and Brownfield land to the market.
- 1.4 HCC's submission focuses on a number of the draft report's recommendations and is structured under the following headings:

1.0 INTRODUCTION

2.0 SUMMARY OF HCC'S KEY POINTS

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- B. Housing Affordability – an 'Auckland' Problem
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5.0 CONCLUDING COMMENTS

2.0 SUMMARY OF HCC'S KEY POINTS

A. Release of Greenfield and Brownfield Land

- Releasing significant tracts of Greenfield and Brownfield land to the market is not seen as a 'magic bullet' solution to the country's housing affordability issue.
- Implementation of this solution would have significant cost implications for councils, particularly around the provision and ongoing maintenance of infrastructure required to service new Greenfield and Brownfield developments.
- In Hamilton's case, servicing of land must be paid from debt, at huge cost, and with HCC's cost and debt reduction commitment, its capacity and appetite to borrow to facilitate such expansion does not exist.
- Estimates of Hamilton's Greenfield sections shows the city has a potential supply surplus estimated at 6 years of demand currently; 9 years by 2022, and a similar number estimated / available out into the long-term. **Clearly then, release of further Greenfield sections in Hamilton would not materially improve the city's housing affordability.**
- More than ever, councils need to be fiscally responsible in regards to expenditure, particularly in light of the current worldwide financial recession and the planning/development currently taking place around 2012-22 Long-Term Plans.
- The issues involved in today's housing situation are clearly far more complex than looking at one solution in isolation and pin-pointing it as the key to addressing housing affordability.

B. Housing Affordability - an 'Auckland' Problem

- New Zealand's housing affordability is, to a large extent, an 'Auckland' problem. This will only get worse, with Auckland forecast to be home to almost half of the country's new households created over the next 20 years.
- Given the ongoing population pressure and premium prices being paid for Auckland houses, solutions/recommendations from the Productivity Commission to the 'Auckland' problem may not necessarily be the most appropriate ones to address housing affordability issues in other parts of the country.

C. Development Contributions

- Qualified support is provided for a set of Best Practice Development Contributions Guidelines.

D. Aim of Reducing House Values

- Decreases in house values will benefit first time buyers but will disadvantage existing home owners i.e. any such reduction would impact negatively on a homeowner's personal financial position and net worth. Flow-on effects include affecting the amount that a homeowner may be able to borrow when applying for a loan (e.g. for house renovations) and using their home as security.
- The last thing the country needs is the situation where house values fall to such an extent that a segment of homeowners end up with a mortgage that is higher than the value of their house.

E. Building Consent Processes and Reforms

- Government needs to seriously consider joint and several liability with respect to the

ability for local authorities to manage the likes of leaky building claims.

- Government changes pending to the building consenting regime factor in a risk approach based on the person who does the work bearing major responsibility if something goes wrong.
- Agree that monitoring of reforms by the Department of Building and Housing is an important means of establishing that the reforms are working as proposed.
- There are alternatives to the multi-proof building consent process such as the Hamilton City Council partnership programme and department staff should work with HCC staff to explore some of the philosophies and how they can be applied to a wide range of building consenting.

F. The Quality of Housing Stock

- HCC supports the recommendation that Statistics New Zealand collect more information about the quality of New Zealand's housing stock and consumer satisfaction with the residential construction industry. A number of variables need to be considered - in particular the age of the country's housing stock as this has a key bearing on determining such aspects as insulation levels.

G. Cost of New House Construction

- Building firms in some areas of the country are already more efficient and competitive in the construction of new houses than others. These existing efficiency and competitive elements need to be identified and promoted throughout the sector.

H. The Financial Sector's Impact on Housing Affordability

- There is a gap in the draft report around the significant impact that the financial sector has on housing affordability e.g. the extremely high costs of breaking fixed rate mortgages in order to obtain lower interest rates and ease regular mortgage payments. This is one aspect that the Productivity Commission may wish to follow up on.
- At the extreme end of the scale, those no longer able afford to pay a mortgage are reflected in mortgagee sales, which increased from 591 in the July-September 2010 quarter to 652 in the July-September 2011 quarter (**compared to just 89 in the same period in 2007 – pre-recession**). A large proportion of these sales are now 'Mum and Dad' property owners.

3.0 COMMENTS IN RESPONSE TO SPECIFIC RECOMMENDATIONS

3.1 Recommendation 7.1

- 3.1.1 *Auckland Council show in its final Auckland Plan how it has considered and reconciled affordable housing alongside its other priorities.*

HCC's Response

- 3.1.2 HCC supports the intent of this recommendation. The Productivity Commission note in their draft report that the issues around housing affordability are very much an Auckland centred issue. Given Auckland's likely future growth, this issue will only continue to compound, with the city forecast to be home to almost half of the country's new households created over the next 20 years.

3.2 Recommendation 7.2

3.2.1 *Bring significant tracts of Greenfield and Brownfield land to the market in Auckland – identify and assemble land that could be quickly released and identify significant tracts of land with the potential for (say) 50 years development, with at least 20 years' worth under preparation for development.*

HCC's Response

- 3.2.2 HCC does not believe that this recommendation is a 'magic bullet' solution. The issues involved in today's housing situation are clearly far more complex than looking at this specific recommendation in isolation and pin-pointing it as the key to reducing housing costs.
- 3.2.3 Implementation of this recommendation is likely to have significant cost implications for the Auckland Council (and for that matter all councils if this were to be implemented throughout the country), particularly around provision and ongoing maintenance of infrastructure required to service new Greenfield and Brownfield developments.
- 3.2.4 This in turn would have significant implications for residential rates – another major cost component of the home ownership/affordability equation.
- 3.2.5 More than ever, councils need to be fiscally responsible in regards to expenditure, particularly in light of the current worldwide financial recession and the planning/development currently taking place around 2012-22 Long-Term Plans.
- 3.2.6 In addition, councils are also cognisant of recent comments from the new Minister of Local Government. The Hon Dr Nick Smith has stated that current rates rises across New Zealand are "unsustainable". His main concern is council spending and the financial burden on households and businesses - councils must focus on getting better value for ratepayers¹.
- 3.2.7 The Minister has also warned that the Government may reintroduce debt limits on councils.

3.3 Recommendation 7.4

3.3.1 *Territorial authorities:*

- *Take a less constrained approach to the identification, consenting, release, and development of land for housing in the inner city, suburbs, and city edge.*
- *Adopt a strategy that allows for both intensification within existing urban boundaries and orderly expansion beyond them.*
- *Develop strategies that promote adequate competition between developers for the right to develop land.*

HCC's Response

- 3.3.2 HCC does not support this recommendation.
- 3.3.3 While this presents with theoretical benefits for housing affordability, supply, and availability, there are circumstances and financial realities that would prevent broad

¹ 'Smith hits out at 'unsustainable' rates rises and debt'. The Press (26/1/2012).

release and development of land for development, including that:

- In Hamilton's case, the servicing of land must be paid from debt, at huge cost, and with HCC's cost and debt reduction commitment, its capacity and appetite to borrow to facilitate such expansion does not exist.
- The cost of installing and extending services is incurred over the short term. However, development contributions recover this debt for funding the servicing of land over decades, creating a huge short-term cost funded by long-term debt that, as above, HCC has no capacity or appetite to take on.
- There are already many hundreds of hectares of land in Hamilton zoned residential in the Greenfield areas that are undeveloped because there is no private or local authority funding to do so. In regard to demand, the number of vacant sections, land-banked legacy consents, the credit-tightened construction industry, and economic conditions would cast serious doubt on the potential uptake if significant blocks of new land were developed and sold.
- HCC is proposing through its Draft 2012-22 Long-Term Plan to act as part funder of infrastructure in selected parts of the city. This is primarily due to funding constraints faced by HCC. The areas where funding of strategic infrastructure for development is planned, have all been long-standing plans and well communicated with the community through various landuse and strategic planning processes. However, HCC also recognises that there may be other areas of the city where different developers may wish to speed up development and fund the full cost of this. HCC is exploring the necessary planning instruments and funding mechanisms to enable this to occur at the timing desired by the funding developer. The focus of HCC in such situations will be to ensure that any large scale and 'out of sequence' development is done in an integrated way and does not have negative outcomes for the existing community and built environment.
- In regard to the recommendation "Adopt a strategy that allows for both intensification within existing urban boundaries and orderly expansion beyond them", HCC currently operates with a strategy of this nature, and will continue to do so.
- HCC is not clear what the recommendation "Develop strategies that promote adequate competition between developers for the right to develop land" would involve. Further detail is required before establishing a view.

3.3.4 The following table outlines the gross potential Greenfield section supply in Hamilton.

Current and Projected Gross Greenfield Section Supply in Hamilton

| Greenfield Section Supply | Approximate # Sections | Date Serviced By | Cumulative Supply of Sections | Potential Supply Surplus |
|---------------------------|------------------------|---------------------|-------------------------------|--------------------------|
| Consented not Titled | 2,000 | Currently available | 3,000 | 6 years (currently) |
| Vacant Titled | 1,000 | | | |
| HCC Serviced | 5,000 | 2022 | 9,500 | 9 years (by 2022) |
| Developer Serviced | 1,500 | | | |
| For Future Development | 15,000 | Post 2022 | 24,500 | 9 years (by about 2040) |

3.3.5 The section numbers above refer to a gross total potential section supply converted to years, if all vacant sections, and legacy sections consented but not titled, were immediately available.

3.3.6 These potential section supply numbers are derived from current supply and land-use information, projected supply for HCC’s 10-year plan to 2022, and projected section numbers post 2022 for future development land zoned residential but with service provision currently unfunded.

3.3.7 The actual anticipated supply of sections is lower after taking account of land-banking, high density development, legacy uptake, and vacant section uptake.

3.3.8 Demand is projected to average about 500 sections per year over the next 10 years, with lower growth in the three years to 2015, reflecting slow projected economic and population growth.

3.3.9 Based on these demand and supply assumptions, there exists a potential supply surplus estimated at 6 years of demand currently; 9 years by 2022, and a similar number estimated / available out into the long-term.

3.3.10 These are impediments of fluid release and sale of some land due to strategic developers ‘land-banking’, and long-term uncertainty around the nature of service provision.

3.3.11 This table is presented to illustrate that releasing and servicing new Greenfield areas would be unlikely to lead to significant new sections for housing in Hamilton, when considering the number of sections of potential development that currently exist but do not get developed due to market conditions and other reasons, but that do exist in terms of an ideal potential supply.

3.3.12 However, these projections provide evidence to support HCC’s assertion that Hamilton does not face a shortage of Greenfield section supply that would support expansion of Greenfield boundaries.

3.3.13 Taking the above into account, release of further Greenfield sections in Hamilton would not materially improve the city’s housing affordability.

3.4 Recommendation 8.1

- 3.4.1 *That the Government update the Best Practice Guidelines to Development Contributions, based on a process that takes account of the experience of both councils and the industry.*
- 3.4.2 *The principles in the guidelines might be given statutory status by being incorporated into Schedule 13 of the LGA.*

HCC's Response

- 3.4.3 HCC would provide qualified support for a set of Best Practice Guidelines to Development Contributions, following disclosure and after due consideration of any proposal, including any potential statutory implications.

3.5 Recommendation 8.2

- 3.5.1 *That the Government leads training to enable councils to enhance their skills in implementing the proposed Best Practice Guidelines for Development Contributions.*

HCC's Response

- 3.5.2 HCC would agree in principle to be involved in training and implementation of any new guidelines.

3.6 Recommendation 8.3

- 3.6.1 *That as part of the process of updating the Best Practice Guidelines to Development Contributions, the Government:*
- *Identify information that councils would need to provide in regular reports to demonstrate compliance with the Guidelines*
 - *Develop a process for regular auditing of councils to assess their adherence to the Guidelines.*

HCC's Response

- 3.6.2 HCC would offer qualified support for the development of guidelines, but with full input into the process.
- 3.6.3 HCC is not clear what this would involve, and would need to see the detail before establishing a view.

3.7 Recommendation 9.2

- 3.7.1 *The Law Commission gives regard in its review of the application of joint and several liability on the incentives faced by regulators.*

HCC's Response

- 3.7.2 HCC supports the view that the Government needs to seriously consider joint and several liability with respect to the ability for local authorities to manage the likes of leaky building claims.
- 3.7.3 Government changes pending to the building consenting regime factor in a risk

approach based on the person who does the work bearing major responsibility if something goes wrong. For example, a builder as a Licensed Building Practitioner (LBP) takes responsibility for his work and provides some form of guarantee. If the building leaked under the new regime it is likely that the builder as an LBP will bear the brunt of repair costs or repair the building at his own cost.

- 3.7.4 This approach differs under joint and several liability whereby local authorities are often 'the last man standing' and therefore are caught up in paying for 100% of the repairs, whereas the builder can walk away from the issue.

3.8 Recommendation 9.3

- 3.8.1 *The Department of Building and Housing report on its ongoing evaluation of the reforms on the allocation of risks between parties to building work five years after introduction.*

HCC's Response

- 3.8.2 HCC supports the view that monitoring of the reforms is an important means of establishing that the reforms are working as proposed.

3.9 Recommendation 9.4

- 3.9.1 *The Department of Building and Housing should provide more specific guidance for Building Consent Authorities about what is required for an alternative solution to comply with the Building Code.*

HCC's Response

- 3.9.2 HCC supports the recommendation as implied.

3.10 Recommendation 9.5

- 3.10.1 *The Department of Building and Housing should review the Multi-proof building consent process with a focus on identifying barriers to its application, and suggesting ways to overcome these barriers.*

HCC's Response

- 3.10.2 HCC suggests there are alternatives to the multi-proof building consent process such as the Hamilton City Council partnership programme and department staff should work with HCC staff to explore some of the philosophies and how they can be applied to a wide range of building consenting.

3.11 Recommendation 9.6

- 3.11.1 *Statistics New Zealand consider collecting more information about the quality of New Zealand's housing stock and consumer satisfaction with the residential construction industry.*

HCC's Response

- 3.11.2 HCC supports this recommendation. There would obviously need to be some

standardised measures developed to ensure that a consistent approach to measurement is undertaken throughout the country.

- 3.11.3 A number of variables need to be considered, and in particular the age of the country's housing stock as this has a key bearing on determining such aspects as insulation levels.

4.0 ADDITIONAL COMMENTS

4.1 Report Recommendations and Subsequent Flow-on Implications

- 4.1.1 The report does not seem to clearly identify the subsequent flow-on implications that implementation of the various recommendations may have. It also does not identify key interrelationships between the various recommendations.
- 4.1.2 For example, as identified in Recommendation 7.2, the Productivity Commission recommends bringing significant tracts of Greenfield and Brownfield land to the market in Auckland. Implementation of this recommendation would have significant cost implications for the Auckland Council (and for that matter all councils if this were to be implemented throughout the country) around provision and ongoing maintenance of new infrastructure required to service new Greenfield and Brownfield developments. This in turn has significant implications for residential rates – another major cost component of the home ownership equation.

4.2 Housing Affordability - an 'Auckland' Problem

- 4.2.1 Following on from this, the housing affordability issue in some ways appears to be very much an 'Auckland' problem, with house prices in this city way out of kilter when compared to house prices in the remainder of the country's cities.
- 4.2.2 As noted in the Productivity Commission's 'Cut to the Chase' summary, *"During the boom, house prices increased strongly across most regions. In Auckland, this continued a well-established trend of strong price increases for houses that were already among the most expensive in the country. So the premium for Auckland housing has continued to increase"*.
- 4.2.3 Given the ongoing population pressure and premium prices being paid for Auckland houses, solutions/recommendations from the Productivity Commission to the 'Auckland' problem may therefore not necessarily be the most appropriate ones to address housing affordability issues in other parts of the country.

4.3 Aim of Reducing Current House Values – Another Perspective

- 4.3.1 One key aspect that does not appear to have been addressed in the Productivity Commission's draft report is that existing home owners (irrespective of how long they have owned their property) are very unlikely to want any reduction occurring in their current house values (either in the short, medium or long-term).
- 4.3.2 Any such reduction would impact negatively on a homeowner's personal financial position and net worth. It would also have other flow-on effects, such as affecting the amount that a homeowner may be able to borrow when applying for a loan (e.g. for house renovations) and using their home as security.
- 4.3.3 In addition, the last thing the country needs is the situation where house values fall to such an extent that a segment of homeowners end up with a mortgage that is higher than the value of their house.

- 4.3.4 As it currently stands, the draft report implies that a reduction in overall house values will be a good thing for all sectors in the country. Given that all homes in New Zealand are owned (irrespective of whether they are for personal use, are rented or used for another purpose), the resulting impact would be significant.
- 4.3.5 In summary, while a decrease in house values will benefit first time buyers, it will disadvantage existing home owners. This is an important aspect and needs to be taken into consideration by the Productivity Commission in its final 16 March 2012 report to the Government.
- 4.4 **Home Ownership Aspirations**
- 4.4.1 Whilst acknowledging that the percentage of people renting has increased and that rents themselves have increased significantly in recent years, the Productivity Commission's draft report appears to assume that most New Zealanders aspire to own their own home.
- 4.4.2 However, the draft report appears to overlook the fact there are many in society who do not share this aspiration, and who have chosen to rent as their first choice of having long-term accommodation. While HCC appreciates that rental charges have increased significantly in recent years, there is still a segment of society that will always choose to rent rather than buy.
- 4.4.3 The Productivity Commission will be aware of the December 2011 Statistics New Zealand report entitled "Progress Report for the 20`09 Review of Housing Statistics" (released on 20 January 2012), with one of the key issues discussed being 'Determinants of Tenure and Location Choices by Young People'. The report notes that in regard to housing demand that "*Information is needed on the non-demographic factors driving the demand for housing, including first-homebuyers and property investors (including New Zealand and foreign property investors*".
- 4.4.4 HCC urges the Productivity Commission to take note of the findings in this report when completing their final report to the Government on 16 March 2012, and to work closely with Statistics New Zealand to address the ongoing work around implementing recommendations from the 2009 Review of Housing Statistics.
- 4.5 **Annual Demographia International Housing Affordability Survey**
- 4.5.1 HCC assumes that the Productivity Commission has analysed the recently released eighth annual Demographia International Housing Affordability Survey, which shows that New Zealand has no affordable markets, and Auckland was the worst. Reserve Bank and Real Estate Institute data were used to measure affordability by taking median house prices and dividing those by gross annual median household income. This gave the house price-income median multiple measure.
- 4.5.2 The report states that housing should not cost more than three times the annual income to be ranked affordable. Housing costing more than five times the annual average income was considered severely unaffordable (the average Auckland house is valued at 6.4 times the city's average household income).
- 4.5.3 HCC is of the view that this approach takes a relatively simplistic view of housing affordability, and that indices such as Massey University's Home Affordability Index (which uses median dwelling prices, average weekly earnings and average monthly interest rates) are more refined and provide a more realistic picture of housing affordability in New Zealand.

4.6 Cost of New House Construction

4.6.1 Without stating the obvious, the cost of building a new house varies considerably throughout the country. For example, for the year ended November 2011, the average floor area and average building cost for a new house in Hamilton and Wellington are shown below.

New House Construction Cost – Hamilton versus Wellington

| CITY | AVERAGE FLOOR AREA (m ²) | AVERAGE HOUSE COST (\$) |
|------------|--------------------------------------|-------------------------|
| Hamilton | 170.2 | 216,262 |
| Wellington | 170.0 | 274,861 |

4.6.2 Clearly there was a substantial difference in the cost of building a house of similar sized house in Wellington compared to Hamilton i.e. a 27.1% difference.

4.6.3 Interestingly, the average cost of a new Hamilton house in the year 2000 was \$137,693, meaning that the cost has increased by 57% over this 11 year period N.B. these figures take no account of inflation.

4.6.4 The Productivity Commission state that the residential construction industry has the characteristics of a 'cottage industry', dominated by small firms building small numbers of houses.

4.6.5 Despite the increase in the cost of construction materials, HCC agrees that there is scope to improve productivity in the construction sector. However, it would appear that building firms in some areas of the country are already more efficient and competitive in the construction of new houses than others. It is suggested that these existing efficiency and competitive elements be identified and promoted throughout the sector.

4.7 The Financial Sector's Impact on Housing Affordability

4.7.1 While HCC acknowledges the comprehensiveness of the Productivity Commission's draft report, there appears to be a gap around the significant impact that the financial sector has on housing affordability. For instance, there is no mention around the financial burden that many homeowners are currently facing with meeting their ongoing mortgage commitments, particularly in light of continuing increases in everyday living costs in tandem with the current worldwide recession.

4.7.2 As a specific example, the favourable interest rates that have been offered by lending institutions over the past few months means that many who locked themselves into a fixed rate mortgage are now considering 'breaking' this type of mortgage (to either a more favourable fixed rate or a floating rate) to ease their regular mortgage repayments.

4.7.3 However, the cost of breaking such mortgages is usually extremely high, often costing tens of thousand of dollars. In effect, this forces people to continue to pay unrealistically high interest rates on their regular mortgage payments.

4.7.4 It is acknowledged that the banking sector needs to recoup some proportion of costs for clients who break their fixed term mortgage in terms of foregone revenue. They may also have to rearrange funding positions that they have in place in the wholesale interest rate market. However, the break fees currently being charged by

the various banks appear to be excessive and this is one aspect that the Productivity Commission may wish to follow up on.

- 4.7.5 At the extreme end of the scale, those no longer able afford to pay a mortgage are reflected in mortgagee sales. Data from Terralink shows that mortgagee sales in New Zealand increased from 591 in the July-September 2010 quarter to 652 in the July-September 2011 quarter – a 10.3% increase. A large proportion of these mortgagee sales now comprise ‘Mum and Dad’ property owners e.g. in August 2011, 27% of mortgagee sales were for individual property owners who owned only one property.
- 4.7.6 In comparison to the 652 mortgagee sales recorded in the July-September 2011 quarter, there were just 89 in the same period in 2007 – pre-recession.

5.0 CONCLUDING COMMENTS

- 5.1 HCC trusts that the points raised in this submission will be used by the Productivity Commission in developing their final report to the Government on 16 March 2012.
- 5.2 If you require clarification of the points raised in this submission, or additional information, please contact Mark Brougham (phone 07 838 6597 or email mark.brougham@hcc.govt.nz) in the first instance.

Yours faithfully



Barry Harris
CHIEF EXECUTIVE