Massey University

NZ Residential Rental Market

March 2007

Quarterly Survey Volume 10, Number 1

A Plan to Ease Rents and House Prices

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DATA SOURCE The private sector rental data is supplied by the Department of Building and Housing (Bond Centre). Information on wage rates, demographics and the structure of the rental housing stock is drawn from Statistics NZ data. House price information has been extracted from Real Estate Institute and Quotable Value NZ statistics.

The Supply Side

The recent debate about the lack of affordable housing in New Zealand has begun to focus more attention on the supply side of the housing equation. Advocates of a market driven solution argue that relaxing planning restrictions will encourage more greenfields subdivision and lower the price of residential sections. However, the idea of unleashing market forces on the city boundaries does have its drawbacks. There are the usual NIMBY (not in my back yard) problems associated with existing owners located next to proposed low cost housing. More importantly in an era of increasing public concern about global warming and carbon taxes questions about the financial and environmental sustainability of uncontrolled urban sprawl cannot be ignored.

Traditionally residential developers concentrated on building new housing on the city fringe because large tracts of land were available and land costs were lower than the option of infilling existing suburbs. But there were hidden subsidies with greenfields developments as Councils (existing ratepayers) picked up the tab for extending infrastructure to connect with new developments. In the current climate of more transparent and user pays driven local government, greenfields subsidies are not a popular option with existing ratepayers and most of the costs associated with extending infrastructure will have to be paid for by developers and then passed on to section buyers.

Of course housing decisions are not just about land costs. Commuting from the fringe has both direct hard costs (running a car) and indirect costs. Aucklanders will be very familiar with the time delays (reported in the Herald in 2004 at costing around $1 billion annually) resulting from an already overloaded roading system. Extending sprawl is almost certain to add to overall commuting time and hardest hit will be the people living in low cost housing on the fringe.

Density Considerations

So what are the alternatives? One possible solution would be for central government to take a lead role in increasing the supply of affordable housing within the confines of our existing cities. By international standards New Zealand towns and cities have a very low density of population per square kilometre (km^2). In 2001 statistics New Zealand reported the population density in our main urban areas averaged 522/km^2. At this time Auckland was at 989/km^2, Wellington 765/km^2 and Christchurch 549/km^2. Wikipedia shows these densities are generally less than half those found in Australian capital cities and a quarter of many North American and European cities. Vancouver in British Columbia rates as one of the most livable cities in the world and has a density of 5250/km^2. The "little boxes on the hillsides" in San Francisco achieve a density of 6420/km^2. Even sprawling Los Angeles with all its freeways is relatively densely settled (3114/km^2) compared with New Zealand cities.

The Plan

This win-win plan simply involves increasing the supply of housing at no cost to the taxpayer. Does it sounds too good to be true? Well here is how it works. Housing New Zealand (HNZ) currently has around 66,000 State Houses rented. Using conservative values let's assume these houses are worth on average $200,000 each giving a total value of $13.2 billion. Let's say for each year over the next 5 years the government sells 10% of its rental houses at market value. Naturally first option to buy would be given to the existing HNZ tenants and second option to other qualifying first home buyers. The sale proceeds to HNZ would come either directly from the tenants deposits and private sector mortgages or the HNZ could offer vendor financing and then securitize the debt. Sale proceeds of $1.32 billion per annum would then be applied to building 6600 new medium density rental units in the areas of greatest need. This would mostly likely mean building more medium density units (up to 3 stories) in Auckland and having a wider range of bedroom types to cater for the increasing number of small families. The land costs for each new rental unit would be minimised by clever infill, re arrangement of existing state owned houses on land already owned by the Crown and some comprehensive redevelopment of prime sites. The net result might be that instead of adding say 1500 units to the housing stock per year HNZ could add around 8000 units.

The key points with this plan are first it will cost the taxpayer nothing, second it adds 6600 units to the housing stock each year and third increasing supply is likely to apply significant downward pressure on house prices and rents at the lower end of the market.

Win-Win

There is a win for the 6600 tenants who become home owners in well built houses, they don't have to move and without the need for real estate agents transaction costs would be minimised. There is a win for other would be first time buyers because 6600 additional houses are being added each year to the housing stock. People on the HNZ waiting lists also win because the construction of new rental units would target localities in greatest need. The taxpayer wins because income from property sales would balance expenditure on building new units. Furthermore if rents can be kept down there is more chance of rental subsidies ($1 billion + per year) being moderated.

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The building industry wins since guaranteed HNZ work would help to smooth out market fluctuations. The environment wins because with medium density housing the residents “environmental footprints” are minimised in terms of land usage, energy efficient housing and commuting costs. The convenience of being able to walk to work and shops also offers a health benefit win for residents in higher density areas. Yes, there may be some losers. If the plan works property speculators may not see the sort of increases in rents and prices that we have seen over the last five years.

Lessons From The Past

Some elements of this plan have been used before. For example, New Zealand has a long history of the state building rental housing and at times these houses have been sold to the tenants. Certainly, HNZ has made modest attempts at infilling and redevelopment but so far there is nothing on a scale to impact on rents and house prices. What is different in 2007 is the desired outcome includes the objective of minimising further urban sprawl. Redeveloping existing neighbourhoods to achieve higher density outcomes is difficult for private developers because they have to purchase sufficient land to achieve the economies of scale needed for comprehensive redevelopment and are often faced with hostility from existing residents. Central government has significant advantages because it already owns whole neighbourhoods of rental houses in medium density zoned localities that are ripe for redevelopment. Furthermore many of these neighbourhoods are close to where people work. In addition central government already owns lower density zoned tracts of land where it is possible to relocate surplus state houses.

Questions

Of course it’s easy to think up plans but some important practical questions remain. Could the building industry cope with this additional supply? Would the private sector simply reduce supply in other segments of the market, such as city apartments? Do HNZ and local government have the technical and regulatory expertise to achieve good medium density housing outcomes? Perhaps a public private partnership is called for? The worry is while increasing rents and house prices makes existing home owners feel better off it results in an inter generational transfer of wealth away from young people. These are the very people who are expected to fund the retirement of the older generation. Herein lies the challenge for the policy makers!

Rental Levels Continue To Move Up

The weekly national level of median rent moved from $270 in November 2006 to $280 in February 2007. On an annual basis the national median was up by 5.6% compared with February 2006. On a quarterly basis the national median continued to stay ahead of inflation increasing by 3.7% from November 2006 to February 2007.

A snap shot of rents in the main Territorial Local Authorities (TLAs) over the period February 2006 to February 2007 is shown in the table at the top right. Increases in rents over the last quarter are most likely partially attributable to demand pressure from stronger than anticipated net migration figures. Also home affordability has been steadily deteriorating thus forcing first home buyers to remain in the rental market for longer. There may also be a slowdown occurring in the acquisition of investor housing as landlords are faced with net yields of around 3-4% and a slowing property market. In the larger centres Wellington (9.1%) led median rental quarterly increases , followed by Waitakere (6.6%) and Christchurch (5.7%).

Median Rents	*Feb 06*	*Aug 06*	*Feb 07*
Whangarei	*230*	*240*	*250*
North Shore	*350*	*350*	*360*
Waitakere	*300*	*300*	*320*
Auckland	*320*	*330*	*335*
Manukau	*305*	*300*	*330*
Papakura	*285*	*290*	*300*
Hamilton	*260*	*252*	*270*
Tauranga	*260*	*265*	*280*
Rotorua	*185*	*200*	*210*
Gisborne	*195*	*195*	*230*
Hastings	*220*	*225*	*240*
Napier	*250*	*250*	*250*
New Plymouth	*220*	*240*	*250*
Wanganui	*167*	*170*	*175*
Palmerston North	*220*	*220*	*235*
Kapiti	*230*	*240*	*245*
Porirua	*250*	*270*	*280*
Upper Hutt	*200*	*222*	*222*
Lower Hutt	*250*	*240*	*260*
Wellington	*335*	*320*	*360*
Nelson	*250*	*247*	*250*
Christchurch	*265*	*260*	*275*
Dunedin	*230*	*190*	*250*
Invercargill	*160*	*160*	*160*
All NZ	*265*	*260*	*280*

Massey University Real Estate Analysis Unit

The primary objective of the Massey University Real Estate Analysis Unit (MUREAU) is to provide reliable property information to the property industry, the land related professions and the public.

The Director of MUREAU is Professor RV (Bob) Hargreaves. MUREAU also offers a consulting service for individual clients. MUREAU publications, free on request are:

1. The AMP Banking Home Affordability Report (Quarterly)
2. Rural Real Estate Market Outlook (Quarterly)
3. Auckland Commercial Market Outlook (Quarterly)
4. Christchurch Commercial Market Outlook (Quarterly)
5. Wellington Commercial Market Outlook (Quarterly)
6. Auckland Residential Market Outlook (Quarterly)
7. Christchurch Residential Market Outlook (Quarterly
8. Wellington Residential Market Outlook (Quarterly)

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