

Why door is closing on ownership dream

By [Brian Fallow](#) NZ Herald
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Home ownership has many social benefits but remains beyond the reach of many. Photo / Thinkstock

If there is such a thing as the Kiwi dream, living under your own roof is a central part of it.

But home ownership rates have declined, from three in every four households in 1991 to two out of three in the most recent census (2006) and we are now slightly below the OECD average.

We may slip further yet. The housing boom in the last decade drove household debt to a higher multiple of incomes than in Australia, Britain, Canada or the United States.

No wonder, then, that housing affordability is the first inquiry being undertaken by the new Productivity Commission.

The issues paper the commission released last week cites a number of studies linking home ownership to positive social outcomes, ranging from the educational attainments and future income prospects of children to living standards in retirement.

Housing also featured prominently, as you would expect, in a conference last week on New Zealand's macro-economic imbalances.

OECD economist Peter Jarrett said that house prices increased more in New Zealand between 2000 and 2007 than in most OECD countries.

(Spain is an exception but not a reassuring one).

Easy credit and strong net immigration were the major drivers, he said.

Over the five years to the end of 2007 mortgage debt doubled.

Demand for housing was boosted by a surge in the net inflow of migrants in 2002 and 2003.

Overall between 2000 and 2009, New Zealand had one of the fastest rates of population growth in the OECD and the lion's share of it was natural increase - births minus deaths.

OECD research indicates population changes have a much larger impact on house prices in New Zealand than elsewhere, Jarrett said.

But only once prices have risen does the supply of housing react.

And in the latest cycle the increase in construction was short-lived and soon fell below levels needed to keep pace with demand.

Since 2002 the average number of people per household has been going up. Indeed it is a feature of New Zealand housing upturns that the housing stock tends to grow less than OECD norms for a given percentage increase in population.

The Productivity Commission is on to this.

One of the things it will be looking into is why the supply of new housing seems unduly slow to respond to increases in demand.

Is this due to inefficiencies in the building industry, or is it an issue of regulation, to do with the release of land for development or town planning constraints?

The commission's issues paper says that labour productivity in the industry has been flat, at least over the past 15 years, and is low relative to other countries and to other sectors of the New Zealand economy.

The result is inflation in construction costs and upward pressure on house prices generally.

But these supply side factors are only half of the story.

How much has the demand side of the market been stoked by tax policy, or by unrealistic expectation about the returns from housing relative to other investments?

Although expectations eventually adjust to market reality, the commission says, the adjustment can be very disruptive and take a long time, with long-lasting effects.

It has been argued that the surge in house prices in the middle years of the last decade cannot have been driven by population growth. If it had been, there should have been much more pressure on rents than was observed.

During the five years to the end of 2007 when house prices doubled, rents increased by an average 3 per cent a year according to the consumers price index.

Data from tenancy agreements, which cover new rental agreements, show swifter growth, about 6 per cent a year, but still less than the double-digit increases in house prices.

A survey of landlords in 2003 - still in the foothills of the housing boom - found capital gains the most commonly cited benefit of investing in property.

And those gains are untaxed.

For some reason our political leaders don't trust us to be able to grasp the proposition that it makes little sense to tax people if they increase their wealth by the sweat of their brow but not if they increase their wealth by holding the right asset over the right period.

Changes to the depreciation rules in last year's Budget made investment properties somewhat less attractive.

But the Savings Working Group argued that rental, and even more owner-occupied, housing is still treated favourably by the tax system compared with investment in shares or interest-bearing instruments.

It will be surprising if the commission comes to a different conclusion.

It will also be looking at how taxes have affected affordability in the housing market, especially for first-home buyers, and how the overall burden of taxation (including rates) compares with other countries.

New Zealand households have collectively been spending more than their income since the early 1990s.

OECD work indicates a correlation, though not a particularly tight one, between rising real house prices and falling saving rates. But it also suggests that in New Zealand's case the saving rate, until recently, was trending down even without accounting for house prices.

Whatever the extent to which it is housing-related, our chronically negative household saving rate has underpinned persistently large current account deficits, which represent the gap between national investment and national savings.

The gap would have been wider still if business investment over the past 25 years had not been persistently below the OECD median as a share of GDP (which in turn is nothing to write home about).

By contrast business investment in Australia has been well above the OECD median over the same period.

As the Aussies would say, New Zealand has Buckley's chance of narrowing the productivity and income gap between the two countries unless there is a radical change in the amount of capital expenditure its businesses are willing and able to undertake.

Hugh Fletcher reminded the conference that the big swings in interest and exchange rates firms have faced for decades have hardly been conducive to business investment.

Rodney Dickens argues the Reserve Bank's heavy-footed approach, to accelerator and brakes alike, is to blame.

"We are a small economy trying to compete in a tough international environment. If you move the 90-day bill rate from 4 to 5 per cent, that's a 20 per cent increase. Why make our businesses face such a huge change in one of their most important costs?"

A similar argument holds for households and mortgage rates.

Currently mortgage interest rates are at historically low levels. But the bank has signalled, on its present forecasts, that rates will rise about 2 percentage points over next year.

Given the legacy of household debt built up in the last housing boom, that is going to hurt.

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