

# Unpacking the Housing Affordability Crisis: Structural Drivers and Policy Pathways in New Zealand

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## Abstract

This paper analyzes the structural causes of New Zealand's housing affordability crisis, which has made homeownership increasingly inaccessible, particularly in Auckland (the world's seventh least affordable city). While demand is partly driven by demographic shifts and cultural preferences for homeownership, the root causes lie in speculative investment, distorted fiscal incentives, and supply constraints. Historical tax advantages, low interest rates, and restrictive urban planning have inflated prices and diverted capital away from productive sectors. The paper argues that the crisis is not a simple shortage but a systemic market failure. It proposes an integrated policy framework to restore balance: taxing capital gains, securing bank deposits to limit moral hazard, reforming tenancy laws to make renting viable, relaxing density regulations, and streamlining building approvals. Together, these fiscal, regulatory, and urban policies could reduce volatility, reorient incentives toward social efficiency, and rebuild affordability for future generations.

## Introduction

Since 1990, successive booms have lifted New Zealand's house prices to a point where homes have become unaffordable for most Kiwis, who are unable to spend all their scarce resources on this single item (according to the equimarginal principle). A market is “unaffordable” when the median house price is more than three times the median annual household income. None of the eight largest cities in New Zealand meets this criterion.

Although this trend is national, it is particularly powerful in Auckland, where the house-price-to-income multiple is nine, ranking it as the seventh least affordable city in the world, above London and Toronto (Demographia, 2019).



### House-price-to-income multiple in Auckland and New Zealand

Figure 1: House-price-to-income multiple in Auckland and New Zealand

As a result, the homeownership rate is plunging to levels unseen since the 1950s, as an increasing number of Kiwis are excluded from the housing market.

This paper will provide a holistic analysis of the current housing crisis. First, it will explore the reasons for this crisis and how the economy influences the trends in housing. Then, it will suggest a plan to alleviate the situation.



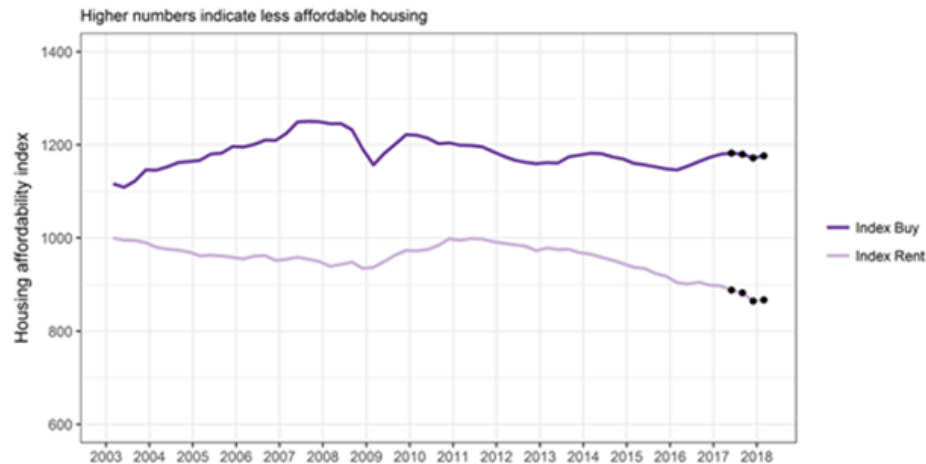
Homeownership rate. Source: Stats NZ

Figure 2: Home ownership rate. Source: Stats NZ.

## Why Is There a Crisis?

A hundred years ago, the government intervened to provide Kiwis with affordable first mortgages. The ‘Kiwi Dream’ was born. Today, it is still rooted in society and renting is regarded as a second option reserved for those who “did not make it”. Consequently, the demand for houses is high, especially as families tend to become smaller, leading to an increase in the number of households.

However, this “organic” demand is not the main reason for the price rise. Indeed, while the housing affordability index skyrocketed in the 2000s for buyers, it remained stable for renters. These data refute the idea of a housing shortage, in favour of a systemic problem that involves all the primary agents of the macroeconomy. New Zealand’s housing market has become a significant investment target for Kiwis and foreigners, creating a speculative bubble, powered by technology-enabled globalization.



Housing affordability index (1000 is the base index for renters in 2003).

Source: MBIE

Figure 3: Housing affordability index. Source: MBIE.

This behaviour is attributable to both history and government policies. Since the 1987 New Zealand Stock Exchange crash, Kiwis have been reluctant to invest in the share market and instead consider houses a “safe” investment option, even if they turn unprofitable (endowment effect). Moreover, the government encourages investors to purchase houses with incentives such as tax-deductible mortgage interests and a seldom-applicable tax on capital gains. Also, the low Official Cash Rate (OCR) fuels the demand by letting banks offer competitive interest rates.

Initially, these incentives were intended to promote homeownership for everyone. They have proved perverse as they have generated a surge in demand, increasing prices and excluding middle-class prospective buyers, favouring investors and wealthy people. Furthermore, they led people to borrow aggressively and take huge risks. In parallel, banks tend to invest heavily in mortgages instead of businesses that create growth and wealth.

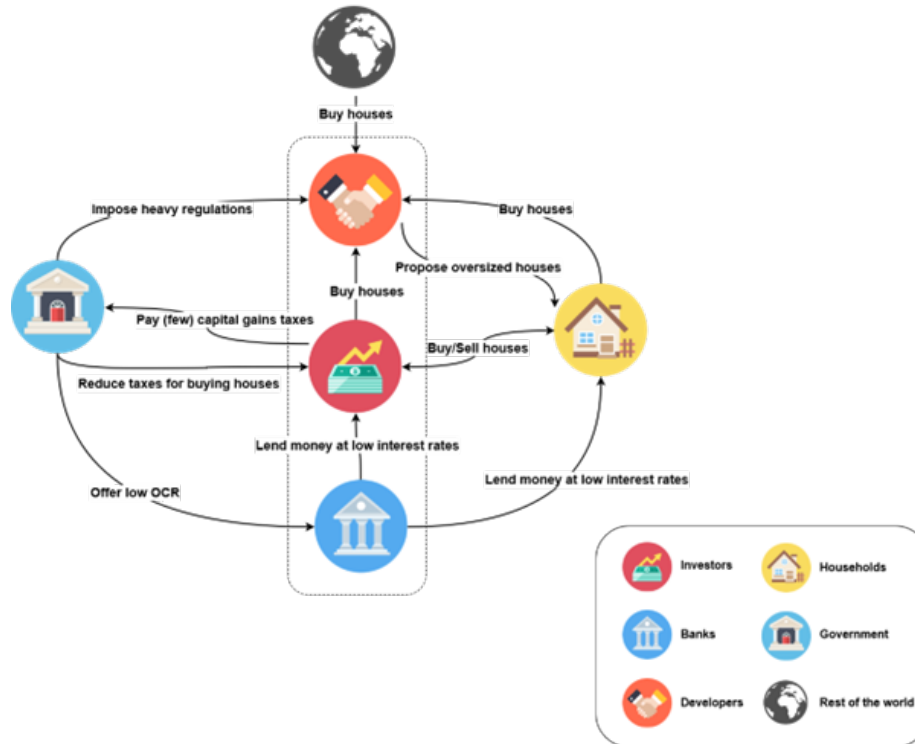


Figure 4: Overview of the New Zealand housing market. Buyers have been divided between investors (firms that are trying to maximize profit) and households (that want to maximize utility). Also, firms include banks, investors and developers

High prices are generally transient – a signal that firms and consumers are sending to each other (“invisible hand”) – and they eventually fall back when supply matches demand. In this case, kiwi firms did not manage to climb up the supply curve.

The main issue is land scarcity. The fact that land cannot be “created” drives high prices, which cannot be reversed solely by the market. Nevertheless, strict urban rules impede the efficient use of existing land (as reflected by Auckland’s extremely low density). These rules were created to improve the quality of life in the cities, but they have the perverse effect of preventing people from living in these very cities. They force them to settle further, generating pollution and adverse social effects (e.g. stress, less family time and limited access to amenities). Inner-city homeowners could enable a change in these regulations. However, they benefit from the resulting high prices and quality of life. Since they have no incentive to do otherwise, they act rationally and push back against any plan to change the situation.

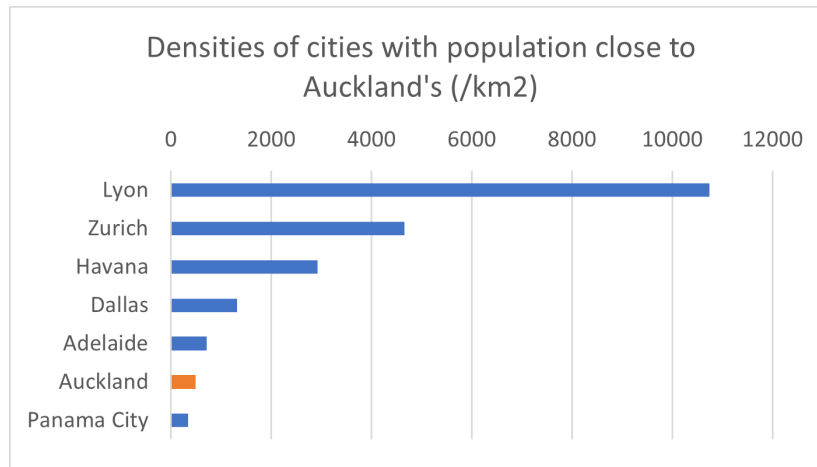


Figure 5: Density of cities with population close to Auckland.

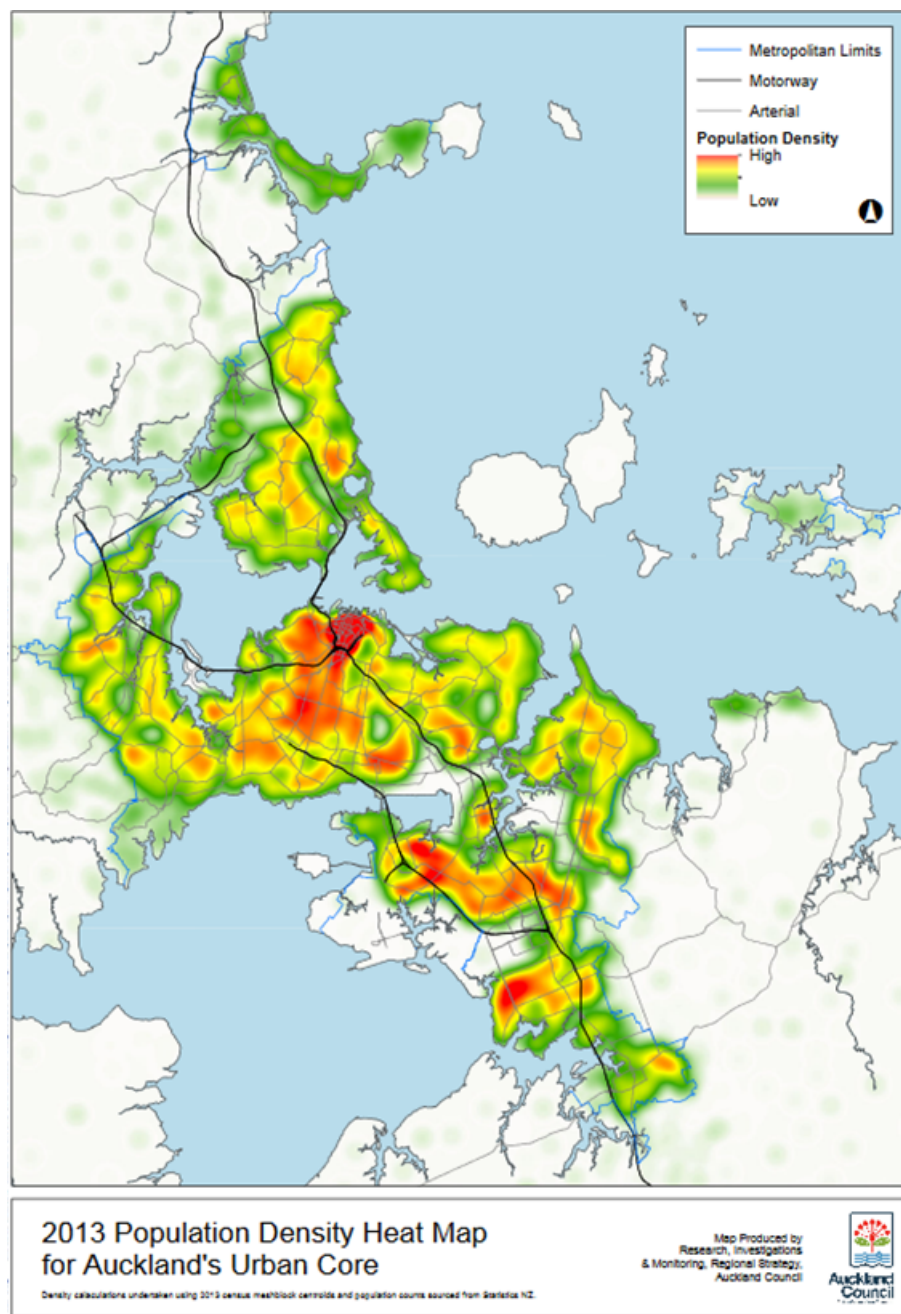


Figure 6: 2013 population density heatmap in Auckland. Source: Auckland Council.



Another critical issue is that New Zealand's construction firms are mostly non-vertically-integrated small structures, inducing a low price elasticity of supply. Also, development lead times take between 2 and 10 years because of regulatory complexities (New Zealand Productivity Commission, 2012). To worsen the situation, some developers prefer to bank on empty lands, slowing down supply even more.

Furthermore, the construction businesses do not allocate their resources effectively, creating a massive mismatch between demand and supply. In 2013, 70% of households had fewer than two members, while 70% of new houses offered four or more bedrooms. Building large standalone houses is, in fact, more profitable for developers because of density-related regulations. As a result, prices increase from unnecessary competition between couples without children and families.

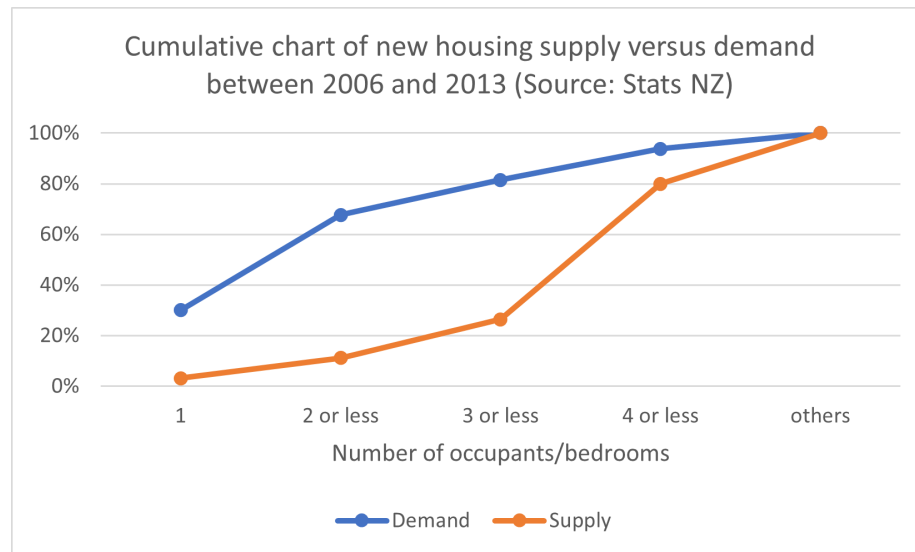


Figure 7: Housing supply vs demand between 2006 and 2013. Source: Stats NZ.

Overall, the market has failed to provide a socially optimal distribution of houses. Individual incentives led to an irrational outcome for the group: a speculative bubble that makes housing unaffordable for locals and induces a chain of displacements (ripple effect) associated with a set of undesirable social consequences. The government should intervene appropriately to support households with low incomes that are de facto excluded from the market and prevent this bubble from growing further. Indeed, as it grows, it becomes more speculative, prompting people to take more risks with debts, which makes the recession more painful when the bubble eventually bursts.

## How to Redress the Crisis?

In response to the crisis, the government launched its Kiwi Build programme in 2018, aiming to build 100,000 “affordable” homes to match demand. As discussed above, the main issue is not a shortage of houses but a set of investment-friendly incentives and an inelastic supply. Moreover, Kiwi Build homes are generally in the lower quartile of the market prices in Auckland but closer to the median elsewhere, which is far from being affordable (Ninness, 2019).

It would be more relevant to reduce the demand first and then boost the supply towards an equilibrium, where locals of all socioeconomic statuses have access to affordable housing. This section presents a plan to redress the crisis, following this strategy. A comprehensive summary is available for convenience in Appendix 1. The design of this plan has considered the effectiveness of the policies overseas (see Appendix 2) as well as other available data.

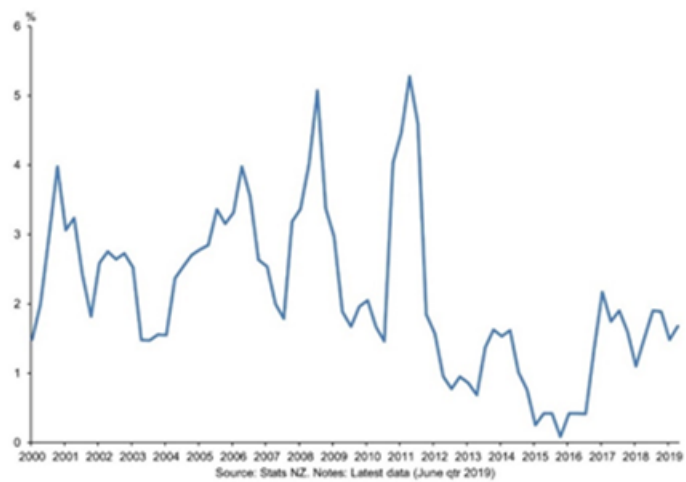
### Reducing Speculative Investment

The government’s priority should be to reduce incentives for speculators. Subsequently, as rational economic agents, they will likely look to sell. Demand and supply will begin to rebalance.

An obvious fiscal policy would be to tax capital gains on every house sale, regardless of the owner’s initial intent, except for owner-occupiers. However, the government should be cautious with its implementation. Indeed, brutally taxing capital gains reduces supply by discouraging people from selling (Aregger, Brown, & Rossi, 2013). Conversely, if such a policy were to be planned and advertised, the “fear of missing out” would rush current investors into selling. Prospect speculators would also walk away.

Moreover, an educational campaign could explain that diversified investments are safer and potentially more profitable. In this respect, purchasing a house is not ideal, especially in unaffordable cities like Auckland, due to the opportunity cost of giving up other investment options.

Finally, one could argue that raising the OCR would be a relevant solution to limit borrowers’ access to finance. However, the Consumer Price Index in New Zealand is equal to 1.7%, which is already below the 2% target (Reserve Bank of New Zealand, 2019). A contractionary monetary policy would further hurt inflation and, therefore, wages and employment.



**New Zealand Inflation**

Figure 8: NZ inflation between 2000 and 2019. Source: Stats NZ.

## Securing Bank Deposits

Given the current banks' dependency on mortgages, a drop in house prices would significantly increase the risk of bank failure, similar to the situation during the 2008 crisis. Under the current law, the Reserve Bank can theoretically shut down a failing bank and force a recapitalization by zeroing all its depositors' accounts. Realistically, the government will probably bail out the bank to prevent a ripple effect on the whole economy.

As a result, the New Zealand property market can be considered "too big to fail". Investors (and banks) have no reason to worry about speculating on houses as the government – and ultimately, the taxpayers – bear the risks. The government should terminate this "moral hazard" by setting up a "Deposit Insurance" where banks and depositors pay a premium to guarantee their deposits. In Europe, for instance, deposits are secured up to 100,000 € per account.

## Promoting Renting as a Viable Option

The contrast between France and New Zealand regarding renting is striking (Sources: French-Property.com, Tenancy Services):

	France	New Zealand
Minimum lease duration	Three years	-
Tenant notice	30 to 60 days	21 days (if periodic)
Landlord notice	Must wait for the end of the lease	42 to 90 days (if periodic)

French regulations enable flexibility for tenants, avoiding the anxiety characterizing New Zealand's system. Otherwise, the quality of French rental properties is excellent due to draconian rules and the systematic use of bonds to perform minor repairs between tenancies. In New Zealand, the overall quality of rental houses is poor because tenants lack incentives to maintain them properly, and most landlords view them merely as speculative investments.

After addressing the speculative issue, New Zealand could benefit from implementing a policy that bridges the gap with the French model. This policy would force landlords to think carefully before purchasing houses (although renting would remain a viable "Maximin" investment strategy). Also, tenants (including low-income and unemployed people) would stay longer in a place they could call "home", increasing their involvement in the community.

## Aligning Supply with Demand

Once demand is down to a sustainable level, the government should focus on supply. The priority should be to align supply with demand by improving the allocation of current resources.

Loosening density regulations should remove the incentive to build oversized houses and allow for meeting people's needs. Moreover, coupled with well-designed urban planning (e.g. "walkable neighbourhoods" with green areas), it would have other positive outcomes regarding pollution and inhabitants' well-being. It is also advised to adopt a preventive Keynesian approach to smooth the business cycle, as this policy requires infrastructure investments to be effective.

To overcome the expected resistance from current inner-city homeowners, the government may increase rates to include externalities, such as pollution and the well-being of outer-city homeowners. The rational decision may then change to be in favour of higher density if the tax to pay outmatches the willingness to accept the new policy.

## Increasing Supply Speed

The last item on the agenda is to address supply speed in the building sector to absorb variations in demand better.

First, the government should dramatically simplify regulations to reduce the time needed to obtain the required permits to build a house. Also, creating negative incentives on land banking (i.e. taxing vacant land) would make this capital more productive. Although one could argue that these incentives weaken the "private property" characteristic of a perfect market, it is questionable whether a market should be perfect in the first place. In Pittsburgh, land taxation has proved crucial in the city's economic development, as it stimulated building activity while avoiding rate increases.

At this stage, the government should also use ambitious programmes, like Kiwi Build, to encourage Kiwi construction companies to gather and combine their effort. They could achieve economies of scale at several levels (typically labour and technical levels) by spreading fixed costs over a larger number of goods. Moreover, Schumpeter's "creative destruction" process could allow for reducing marginal costs through innovation. These new large vertically integrated firms would then have excess capacity, allowing them to be highly reactive and competitive in the long term.

## Conclusion

The current housing affordability crisis in New Zealand is due to a combination of massive demand, fueled by cultural and government policies, and limited supply, mainly due to land scarcity and burdensome regulations.

The government should act now to reduce volatility and avoid the human cost associated with the expected rough patch. The goal is to relieve the pressure of the housing market while balancing a complex set of competing interests. The envisioned strategy aims to reduce speculation-related demand, increase supply capacity, and provide affordable housing alternatives through a series of fiscal, monetary, and regulatory policies.

An unintended consequence of this government's intervention could be that, with lower house prices, current owners would see their wealth decrease and spend less, reducing inflation. However, it seems like a beneficial trade-off considering the blatant threat of severe economic recession when the speculative bubble bursts. Moreover, doing nothing would cause New Zealand to climb the Gatsby curve and reinforce intergenerational immobility, as the only way for the new generation to own a house would be through inheritance. Also, the adverse social effects would worsen kiwis' overall well-being and New Zealand's "Happy Planet Index" would cringe. In the future, these intangible costs should be included in the government's cost-benefit analysis.

## Appendices

### Plan Summary

#	Policy	Agent	Expected behaviour	Potential unintended consequence	Risks mitigation plan
1	Taxing capital gains	Investors	Sell and change investment strategy	Lock-in and refuse to sell, continue investing if the tax is not dissuasive	Plan and advertise, perform educational campaigns
2	Setting up 'Deposit Insurance'	Banks, Investors, Households	Reduce speculation and inconsiderate risks	-	-
3	Reinforcing tenancy regulations	Investors, Households	Reduce speculative purchases, increase demand in rentals, improve rental houses quality	Shortage of rental properties (less attractive for investors)	Reinforce maintenance expectations and retain bond if required
4	Loosening density regulations	Developers	Provide homes that meet kiwis' needs	Resistance from inner-city homeowners, pollution and a decrease in overall well-being	Threaten to increase rates, invest in urban planning

#	Policy	Agent	Expected behaviour	Potential unin- tended conse- quence	Risks mitigation plan
5	Simplifying permits procedures	Developers	Build houses faster	Natural hazard (e.g. earth- quakes, storms), pollution	Perform a Cost- Benefit Analysis
6	Taxing vacant land	Developers	Stop land banking, build houses faster	Inefficiency due to the high cost of building	See #5 and #7
7	Undertaking develop- ment pro- grammes	Developers	Team up to create strong con- struction firms	Monopolistic market (low likelihood)	Favour competi- tion, ask for a minimum number of candi- dates, assign projects to different firms
<b>Overall</b>		Investors, Develop- ers, House- holds, Rest of the world	Balance demand and supply	Drop house prices, bank failure	See #2



## Examples of Implementations of Similar Policies Worldwide

Policy	Places
Taxing capital gains	France, Switzerland (Aregger, Brown, & Rossi, 2013), Germany
Setting up ‘Deposit Insurance’	Europe
Reinforcing tenancy regulations	France, Germany (Bruce, 2017)
Loosening density regulations	USA (Han & Sun, 2019)
Simplifying permits procedures	Sweden, Japan (Malyshev, 2006)
Taxing vacant land	Brazil, Colombia, Democratic Republic of Congo, Mexico, Philippines, United Kingdom (Haas & Kopanyi, 2017), USA (Seattle, Hawaii, Pittsburgh (Oates & Schwab, 1997))
Development programmes	France (Chomard, 2017)

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