NEW ZEALAND PROPERTY INVESTORS FEDERATION

It's always hard to buy a home

A situational comparison of home buying from the decades 1985 to 2015

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Report prepared by

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Liability

Background Information

New Zealand Property Investors' Federation Inc

The Federation established in 1983, comprises twenty local associations located throughout New Zealand, and is the national body representing the interests of over 7000 property investors directly and 250,000 indirectly.

NZ Rental Industry

It has been estimated that there are over 180,000 landlords in New Zealand[1] and Statistics New Zealand figures that over 472,000 households live in rented accommodation worth around $60 to$80 billion. There has also been a higher estimate of $200billion[2,3].

According to the Real ITO, the real estate industry's training organisation, about $7billion of rent is paid each year by residential tenants[4].

Overall small scale private residential landlords are the largest providers of rental accommodation in New Zealand.

Purpose

The purpose of this study is to take an objective look at the situation first home buyers operated in for the decades 1985 to 2015.

Housing is of considerable importance to everyone in New Zealand. Influencing factors involved in the housing market are dynamic, going through cycles and changing over time.

Over the last few years there has been a widely and publicly voiced view that housing has never been more unaffordable than today and people are being forced into being tenants for life rather than home owners. This widespread view has had a considerable impact on the general population's beliefs on housing affordability.

The view that tenants cannot achieve home ownership has been repeated so often that it is likely a generation will accept this and not even try to achieve a home of their own. This is bad for society as well as the individual.

The information used to make this claim is usually income to house price ratios and rental price to house price ratios. When only this information is used, it supports the view that housing has become completely unaffordable.

However just using this information does not provide a complete picture of the situation.

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[1] "Taxing times for landlords", NZ Herald 6/2/10
[2] Tax Working Group has estimated the figure at $200billion
[3] "Rental property value overinflated", NZ Herald 19/5/10
[4] Commercial property, page D16, Sunday Star Times 24/4/11

Since 1985, mortgage interest rates have dropped considerably, meaning that house buyers can service a higher level of mortgage. Marginal tax rates and rental prices relative to incomes have fallen, meaning a higher percentage of disposal income is available to save for a deposit. In addition, all of a first home buyers Kiwisaver savings and First Home Owners Grants are available for a home deposit.

The NZPIF wanted to examine the situation that first home buyers faced within each of the decades from 1985 to 2015. What factors made buying a home harder and what factors made it easier?

Many commentators are saying that younger people are no longer able to achieve home ownership. Faced with hearing this view constantly, it is understandable that it could be taken as fact and lead young New Zealanders to not even contemplate home ownership.

The NZPIF wanted to examine if it has never been less affordable to buy a home in New Zealand and if first home buyers are destined to be tenants for life.

Methodology

Two key aspects of buying your first home are the ability to save the deposit and to service the required mortgage.

The study sought to examine and compare each of these two aspects in the years 1985, 1995, 2005 and 2015 for first home buyers looking to buy the average New Zealand home. (In reality, it is likely that a first home buyer will purchase a lower than average property.)

To calculate the average house value, we used an average of the REINZ median sale price figure for the 12 months to December in each of the study years. This was to eliminate any highs or lows of any particular month during the study years.

To estimate the ability to save a deposit, the study assumed that a 20% deposit was required in each of the study years. We then estimated how many years it would take to save this deposit in each of the study years.

To do this, we took Reserve Bank income data and income tax rates in each of the study years to estimate net income. We then took off the cost of rent, usually the highest expense, and rationalised that tenants could save a third of the balance.

To complete the estimate of years it would take to save the deposit, we divided the required home deposit by the estimated annual savings.

To calculate mortgage serviceability, we estimated the size of the mortgage by taking the deposit amount from the average house price. We then applied the average floating mortgage interest rate from the four main banks operating in New Zealand, and assumed a 25 year repayment term.

Findings

The study found that all factors in the study changed over the study period. Some made it harder to acquire property and some made it easier.

The key elements to causing change over the study period were house price and incomes increases, plus mortgage rates declines and the introduction of Kiwisaver.

Falling relative rental prices and income taxes also influenced home affordability over the study period.

Mortgage serviceability

House prices increased from $80,000 in 1985 to $460,000 in 2015, an increase of 475%. This corresponded with income increases from $23,542 to $61,173, an increase of 160%.

Clearly house prices had increased at a markedly faster rate than incomes, from a house price to income ratio of 3.4 in 1985 to 7.5 in 2015. This is the figure mostly used by parties looking to show that house prices have become highly unaffordable since 1985.

However in addition to increasing incomes going some way to offsetting home un-affordability, reducing mortgage rates were also a factor.

Mortgage rates fell markedly from 18.9% in 1985 to 5.6% in 2015. This meant that although house prices and therefore the size of the required mortgage increased markedly, the actual cost of the mortgage did not increase significantly.

Mortgage costs increased 124% from 1985 to 2015, which is lower than the increase of incomes at 160%. This means that mortgage serviceability actually improved between 1985 and 2015.

In percentage terms, mortgage serviceability fell from 52% of an average income in 1985 to 45% in 2015.

An added factor that wasn't included in the study was house sizes. The size of our houses has increased significantly over the study period, which would account for a portion of the increase in house prices. If as a population we had continued to build and buy smaller properties, mortgage serviceability would be even better than it is today.

However the positive impact of larger house sizes could be compensated by the impact of the introduction of student loans which would have a negative impact on some first home buyers. This was another factor not included in our study due to it not being universally applicable.

Ability to save for a deposit

Higher house prices also had the effect of increasing required deposits. The required deposit for the average home increased from $16,000 in 1985 to $92,000 in 2015. As with house prices, this was markedly higher than incomes. The required deposit went from 68% of income in 1985 to 150% of income in 2015.

However there were factors that helped 2015 home buyers to save a deposit.

The cost of rent is a large expense for home buyers who are renting while saving for a deposit. The cost of rent as a percentage of income has dropped from 42% of income in 1985 to 32% of income in 2015. This has the effect of increasing disposable income and a home buyers ability to save for a deposit.

If rental prices in 2015 were the same percentage of income as 1985, then the rental price would be $25,673 rather than the $19,760 that it was. This means that first home buyers have the potential to save an extra $5,013 a year towards their home deposit.

Marginal income tax rates have also reduced from 21.5% in 1985 to 18.6% in 2015, which also allows the potential for first home buyers in 2015 to save more towards their home deposit.

Home buyers in 1985 had access to Home Ownership Accounts, which could provide $4,612 towards a home deposit. This amounted to 28.8% of the average required deposit.

Home Ownership Accounts ended in 1986, so were not available for the following decades.

However Kiwisaver has effectively replaced Home Ownership Accounts in helping first home buyers with their deposit. The Kiwisaver first home grant provides $5,000 to first home buyers buying an existing home, or $10,000 towards building a first home. First home buyers can also withdraw all of their Kiwisaver funds to go towards a deposit. At a contribution rate of 3% this amounts to $20,959 within the study period.

The Kiwisaver contribution accounts for 28.2% of the average required deposit in 2015, which is remarkably similar to the 28.8% average of old Home Ownership Accounts of 1985.

To estimate how long it would take a first home buyer in each decade to save for a deposit, we started with the required deposit and took away any amounts from Home Ownership Accounts or Kiwisaver leaving the amount that the first home owner would have to contribute themselves.

We took the average income minus tax and the cost of renting, then assumed savings of 33% of the balance. This equated to between 12% and 15.5% of total income over the four study years.

We then divided the amount that the first home owner would have to contribute themselves by the calculated savings amount in each of the study years.

It was clearly easiest to save for a home deposit in 1985, when it took four years. After home ownership accounts were withdrawn, it started to take longer for first home owners to save a deposit.

It took 6.3 years to save a deposit in 1995 and 7.5 years in 2005.

The increasing time to save a deposit reversed in 2015, when it took 7 years to save for a deposit. This was primarily due to Kiwisaver.

Discussion

Property prices have continued to increase in a cyclical manner throughout the study period between 1985 and 2015. In the mid 80's it was easier to save a home deposit, but harder to afford the mortgage cost due to high interest rates.

Over the following two decades it became harder to save for a home deposit, but easier to afford the mortgage cost.

The ability to buy a first home would likely have been easier if, as a population, we continued to live in similar sized properties. Instead, it appears that we used falling mortgage interest rates to buy bigger and better homes. Increasing regulation on new buildings is also likely to have contributed to better but more expensive homes.

Falling mortgage interest rates offset higher house prices and meant that this period had the second best mortgage affordability costs among the four study years.

The introduction of Kiwisaver first home grants and the ability to withdraw Kiwisaver funds as a first home deposit improved first home owners ability to save for a home deposit. The 2015 year had the third lowest number of years to save a first home deposit.

Conclusion

The study sought to examine if it has currently never been less affordable to buy a home in New Zealand and if first home buyers are destined to be tenants for life.

The study found that the study year of 2015 was not the worst of the four years in the study for either saving a home deposit or the ability to pay for a mortgage.

Directly comparing 1985 with 2015, it was easier to save a deposit in 1985 but harder to service the mortgage.

It appears that there has always been a factor when buying your first home that has made it difficult for the first home buyer. However this has always been the case and recent first home buyers are not facing the worst combined conditions in the four decades of the study. In fact they were not the worst conditions for either saving for a deposit or serviceability of the mortgage.

Commentators who state that it has never been less affordable to get into your first home are wrong and may inadvertently be doing a great disservice to first home buyers.

Being told that they cannot achieve home ownership is likely to stop potential first home buyers from even trying. Rather than standing up for first home buyers, those who continue to state that housing has never been less affordable may in fact be condemning them to being tenants for life.

This is a poor outcome for the individual, but also a serious risk for New Zealand, as tenants are likely to be less financially secure in retirement and may require a higher level of taxpayer support.

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Table 1.

Summary of home buying comparisons from the decades 1985 to 2015

	1985	1995	2005	2015
House Value	$ 80,000	$ 140,000	$ 260,000	$ 460,000
Deposit (20%)	$ 16,000	$ 28,000	$ 52,000	$ 92,000
Mortgage	$ 64,000	$ 112,000	$ 208,000	$ 368,000
Mortgage Interest Rate	18.9%	10.8%	9.5%	5.6%
Incomes	$ 23,542	$ 31,200	$ 44,491	$ 61,173
Rent (pw)	$ 190	$ 220	$ 270	$ 380
Mortgage payments	$ 12,208	$ 12,979	$ 21,807	$ 27,382
Ratio of incomes to House Prices	3.4	4.5	5.8	7.5
Mortgage as % of income	52%	42%	49%	45%
Deposit as a % of income	68%	90%	117%	150%
Rent as a % of income	42%	37%	32%	32%
Tax as a % of income	21.5%	20.0%	21.5%	18.6%
Home Ownership Account (pre 1986)	$ 4,612	N/A	N/A	N/A
Kiwi Saver First Home Grant				$ 5,000
Kiwi Saver First Withdrawal				$ 20,959
Potential Deposit Savings	$ 2,838	$ 4,462	$ 6,897	$ 9,308
Years to save for deposit	**4.0**	**6.3**	**7.5**	**7.0**

Assumptions and calculations

House Value: Average of the REINZ monthly national median sale price for 12 months to December

Mortgage interest rate: Average floating mortgage rate of four main banks

Incomes: Reserve Bank M9 Labour Market survey. Average hourly earnings multiplied by 40 hour week.

Potential deposit savings: 33% of net income after tax, gst and rent costs deducted, plus 3% taken off for Kiwisaver from 2015

Kiwi Saver deposit help: Assumes full 5 year claim. Contributions at 3% for both employer and employee. Only 5 years savings to offset lower income at start of saving. Assumes Government contribution for the full 7 years.