BRICKONOMICS:

NEW BUILDS FOR INVESTORS

POLICIES DESIGNED TO LURE INVESTORS INTO THE PRODUCTIVE NEW BUILD MARKETPLACE OFFER A WORLD OF OPPORTUNITIES.

RESIDENTIAL PROPERTY INVESTORS across the country have patiently observed market movements from the sidelines in the face of rising interest rates, the cost of compliance, and eroding capital appreciation.

However, recent data suggests the housing market is stabilising faster than expected, offering this once-busy buyer group new opportunities as average rental rates rise and demand for homes increases.

RATE OF RETURN

Bayleys National Director of Property Management Services Stuart Bent says the new market cycle will see investors shift their mindsets to focus more on rental yield and upside potential than capital gain.

"Investors have two objectives to weigh up when investing in residential real estate – the rate of rental return (yield) and capital growth.

"Rental yields on residential investments have been low in recent years, as rents failed to keep pace with skyrocketing house prices. Because of this, investors were particularly competitive for properties with the greatest scope for long-term value appreciation.

"Current market dynamics have brought the focus back to the rate of return on rental assets, with investors carefully doing the sums to seek properties that are cash flow positive first and foremost."

Recent data shows the national median rent has reached a record high of $620 per week, while houses cost 11.2 percent less than they did last year – suggesting the yield proposition for residential investors continues to improve.

Bayleys Insights & Data Analyst Eos Li says that while rental yields have increased over the last year, it's too early to tell whether it's enough to lure investors back to the market just yet.

> "APARTMENT YIELDS OUTPERFORM THAT OF HOUSES, AND THE FAVOURABLE TAX TREATMENT ON NEW BUILD PROPERTIES IS WORTH THE INVESTMENT."
>
> ANGELA WEBB, BAYLEYS CANTERBURY INVESTMENT SALES SPECIALIST

"We estimate the average pre-tax net rental yield for a residential property is around 3.3 percent nationally, which while up from 2.8 percent on the same time last year, is still pretty low.

"The picture varies according to personal financial and tax circumstances, but generally, post-tax returns on residential investments are now lower due to changes in interest deductibility."

Li says residential investors have been working around the Government's changes to the taxation of investment properties by maximising exemptions and turning attention to new build properties.

"Investors purchasing newly built properties can still deduct interest expenses from rental income, making these properties a more favourable investment.

"Additionally, new build properties typically feature a more intensive design footprint, which may enable higher rental values with tenants willing to pay more for modern configurations.

"These properties are also often in metropolitan or urban areas which traditionally command higher average rental rates."

Bayleys data shows average net yield estimates nationwide are 3.2 percent for standalone houses and 3.6 percent for apartments and townhouses.

FAVOURABLE TAX TREATMENT

Bayleys Canterbury Investment Sales Specialist Angela Webb says there's evidence to suggest apartment rental yields outperform those of houses, and the favourable tax treatment on new build properties is worth the investment.

"To encourage new housing, interest deductibility is permitted on new build properties for 20 years following receipt of the home's Code Compliance Certificate – this generally means the post-tax rental yield is improved compared to an existing property on which investors cannot claim interest expenses.

"Recently, there's added incentive to develop or purchase new, with confirmation from the Government that new build homes will be exempt from the recent 40-percent deposit requirement rise under loan-to-value ratio (LVR) rules.

"In addition, exemptions to the Overseas Investment Act 2018 have been designed to allow overseas investors to make purchases that support New Zealand's goal of increasing its housing supply.

"These permit up to 60 percent of the apartments in a new development to be sold to offshore investors, in addition to the increased housing pathway which allows foreigners to purchase land for development in special circumstances."

Webb says that private rental supply is an area of opportunity, given deteriorating availability and rising demand.

"Any policy that influences the availability of credit or the investor value of housing will likely boost that market.

"The cost of keeping an existing investment has risen significantly for investors, particularly as insurance, compliance and maintenance costs continue to bite.

> "GREATER CONFIDENCE IN THE FINANCIAL SYSTEM IS GIVING MORE HOUSE HUNTERS A REASON TO TRADE UP, WITH MANY LOOKING TO LIFESTYLE DESTINATIONS."
>
> RAYMOND MOUNTFORT, BAYLEYS REAL ESTATE, GENERAL MANAGER LIFESTYLE

"The loss of interest deductibility places further pressure on the value proposition, and we are seeing contrasts between purchasing intentions for old and new properties."

BACK IN ACTION

A general tilting of the regulatory playing field in recent years has seen investors sit on the sidelines of the residential market while they digest changes that have focused on tenants' rights and landlord obligations.

But in a changing landscape, high rental prices and steady demand from population growth give yield-focused investments an edge.

Bayleys Auckland Residential Salesperson Cherry Kingsley-Smith says in the City of Sails, rents are rising at the fastest pace nationwide, with data from Statistics New Zealand showing an annual increase of 7.3 percent.

"Urgency plays a more significant role in rental and sales markets, as population growth through immigration puts increasing pressure on current supply levels.

"This will play into the hands of developers bringing new projects to the market, as investors may opt for new build properties, which being newer, should have lower costs for ongoing maintenance.

"At the same time, instability in the domestic construction market has contributed to recent readings that show the number of new dwellings being consented is down monthly, quarterly and annually.

"Feasibility has been challenging for developers, meaning fewer new projects are coming online. This is restraining the supply of properties at the same time, the surge in migration is fuelling rental growth.

"Ultimately, less supply spells greater competition for properties, with an upward effect on value growth. Despite every measure suggesting the residential real estate market is turning, prices in Auckland are still below the long-term price trend, providing value for investors in the current market."