ELECTION INSIGHTS

IF NEW ZEALAND'S 2020 GENERAL ELECTION WAS ALL ABOUT POST-PANDEMIC RECOVERY, FOR THE COMMERCIAL PROPERTY SECTOR, 2023 IS ALL ABOUT ECONOMIC RECOVERY AND CALMING AN ALMOST UNPRECEDENTED PERIOD OF VOLATILITY AND INFLATION.

THOUGH GENERAL ELECTIONS often cause a slight market pause as commercial landlords and tenants wait for the dust to settle, this year, with transactions already down and costs rising, the sector is looking for some clarity and certainty about what the economic future holds.

Total Property asked some of the country's political candidates and commercial property commentators about what they see as the major challenges facing the sector ahead of the October election.

Christopher Luxon
National Party Leader

The Government took too long to normalise our border settings and open up access to immigration. The resulting skills shortages have stoked inflation, further driving up interest rates. Now Kiwis are experiencing the consequences in the form of massive increases in the cost of servicing mortgages.

Soaring interest rates aren't just smashing families, they're rippling through the whole economy. For commercial property investors, rising interest rates not only pull down asset prices, but an accompanying recession will inevitably threaten cashflow of many tenants.

Long term, we need to see a real economic plan. Labour has forgotten that every dollar they spend has to be earned by someone – and we've seen no focus on addressing the main challenges affecting business. Continuing to spend heavily while the economic fundamentals are ignored will just mean persistently high interest rates, weak economic growth, and more talent flocking offshore. If businesses struggle, investors will too.

The commercial property sector is a real-time look at the success of the underlying economy. National is absolutely committed to being strong economic managers, to maximise New Zealand's potential to deliver the world-class services Kiwis want and expect.

National's five-point plan to beat inflation will bring inflation down and end the cost-of-living crisis. We'll return the Reserve Bank to a single mandate of fighting inflation, stop imposing wasteful regulations on business, eliminate the bottlenecks holding back growth – like broken immigration settings, and let Kiwis keep more of what they earn, by adjusting tax brackets for inflation.

Broken regulations, wasteful infrastructure priorities, and an obsession with new taxes are holding Kiwis back from being their best.

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> CHRISTOPHER LUXON, NATIONAL PARTY LEADER

National will work relentlessly to make life easier for those Kiwis who want to innovate, invest, grow and succeed.

We've already announced some of our policies that will deliver on that vision. I announced National's plan for Getting Back to Farming – eliminating 19 regulations holding farmers and growers back from their potential and supercharging the rural economy.

I've also announced National's plan to Electrify NZ – our commitment to unlock investment in renewable electricity, so we can meet our modern energy needs while achieving our commitment to Net Zero 2050.

Last month, I announced our commitment to achieving a Free Trade Agreement with India. Just last year, India's economy grew by $560 billion – larger than New Zealand's whole economy. Australia has a trade agreement with India and the UK is about to achieve one. I will not have New Zealand be left behind.

And I've also announced Teaching the Basics Brilliantly – National's plan to get schools back focused on the basics. Delivering a great education system isn't just about ensuring all Kiwi kids have the best opportunity to succeed (where many are currently being left behind), it's about ensuring businesses can access the skilled workers they need to innovate and invest for the future.

Megan Woods
Building and Construction Minister, Labour Party

There's no doubt that the residential construction sector is seeing some stiff headwinds at the moment. Post-Covid we've seen rising global inflation impact us here in New Zealand. Increasing prices for building materials and fuel have been key drivers to the cost-of-living crisis. The Government's strong response through programmes like a $230 million investment in apprentices, seeing more than 57,000 receive an Apprenticeship Boost and the wage subsidy - we ensured our economy got through the worst of the global shutdown and came out in a much better position than many countries.

Throughout the pandemic, the Construction Sector Accord, was pivotal in bringing together the industry and Government to solve problems like supply chain shortages. That work continues with the Accord's Transformation Plan to improve productivity, innovation and the skills of construction sector leaders. Through the Accord, we are now expanding the focus from Government clients to improving procurement practices right across the industry. The Government's role in providing certainty to the sector and a strong pipeline of construction activity is significant.

"THE RECORD-BREAKING INCREASE IN BUILDING CONSENTS (200,000+) DURING THIS GOVERNMENT'S TENURE DIDN'T HAPPEN BY ACCIDENT."

MEGAN WOODS, BUILDING AND CONSTRUCTION MINISTER, LABOUR PARTY

The $3.8 billion Housing Acceleration Fund to pay for critical infrastructure like pipes and roads is a massive stimulus to the sector. It's turbocharging housing developments and civil works - nearly a billion dollars (almost $930 million) from the fund has been allocated across 28 New Zealand cities to enable around 30,000 to 35,000 new homes over the next 10 to 15 years. This is in addition to the huge amount of activity that comes from the biggest public housing building programme since the 1970s. It's not just public housing we're supporting; we are increasing the number of rental properties by making build-to-rent programmes more viable.

Back in 2020, we took steps to provide some counter-cyclical ballast to the anticipated headwinds. $350 million was allocated to provide some stability in the downturn in residential construction everyone thought was coming. That didn't happen, so we put the money aside for when the winds did change.

Now is the time and we're deploying that money and stepping in to financially support some build-ready developments by purchasing land or underwriting homes off the plans to reduce risk for developers – which means we can continue to build homes. I do not want to see a repeat of the global financial crisis where the building of affordable homes fell through the floor. The record-breaking increase in building consents (200,000+) during this Government's tenure didn't happen by accident; we have fundamentally changed the settings in the housing system to encourage more building activity so we can fix the housing crisis that accumulated over decades.

New Zealand badly needs more homes which is why our Government is investing so heavily into increasing supply. So, while we are dealing right now with higher prices across the sector, we know that as inflation comes down there's a strong pipeline of construction ahead to give the sector certainty. This has been my goal since I took over the Housing portfolio and I'll continue to look at ways Government and the sector can work together to get things done for all New Zealanders.

Brooke van Velden
ACT Deputy Leader

I think the biggest challenges we face are skills shortages right across the country, alongside huge inflation, rising interest rates and some of the lowest business confidence levels in history.

In that environment, if a business is unsure about what is going to happen in the next one or two years, a lot of commercial tenants and business owners will be risk-averse. They will be less likely to hire new staff or take on a new, bigger facility.

We'd like to see cuts to wasteful spending that is fuelling inflation. It is also having an impact on rising interest rates which puts additional pressure on anybody who has a loan for their business, but also anybody who is using loans to finance their investments.

We're also still seeing challenges to the Credit Contracts and Consumer Finance Act (CCCFA) in that some businesses aren't able to get access to the same amount of loans from the banks in the way they used to. That is creating more uncertainty which could have a flow-on effect in terms of whether businesses are willing to sign on for contracts on commercial premises. I've talked to business owners who say they've been with the same bank for 20 years, and have always had a good relationship with the bank and now they're having to provide so much more paperwork for anything they need. It just creates another unnecessary barrier to getting funds a business may need to operate and to grow.

"WE'D LIKE TO SEE CUTS TO WASTEFUL SPENDING THAT IS FUELLING INFLATION."

BROOKE VAN VELDEN, ACT DEPUTY LEADER

In the past five years, we've seen Government spending go from around $87 billion to around $139 billion, and many people just aren't sure that they're getting any added value for that. People do not yet see a road to recovery where inflation decreases. Inflation of 6.7 percent should not be celebrated, even if it's down from 7.2 percent. We really do need to get that down to a reasonable level.

Our other priority is to implement my GST sharing member's bill, which would ensure every time there is a new residential home in a local area, half the GST on construction would go back to the local council to help fund infrastructure. It is estimated to deliver $1 billion every year to support local development enabling infrastructure, but councils that consent more, get more. While that may not be a direct benefit to the commercial sector, it will help councils fund the vital infrastructure such as roads and drainage that supports thriving cities and enables growth in all areas.

Leonie Freeman
Property Council New Zealand CEO

At the Property Council New Zealand, we are focused on industry leadership and advocacy initiatives.

"WE NEED ALL PARTIES, INCLUDING THE PRIVATE SECTOR, WORKING TOGETHER WITH A FOCUS ON OUTCOMES AND HOW TO ACHIEVE THEM."

LEONIE FREEMAN PROPERTY COUNCIL NEW ZEALAND CEO

That industry leadership includes everything from promoting build to rent, sustainability and resilience, to addressing housing issues, value capture, seismic strengthening and developing thriving cities. Our advocacy work is with both local and central Government covering a range of legislative reforms from resource reform, build to rent, the building act, and building for climate change, to fire and emergency funding, transport and infrastructure, as well as annual plans, development contributions and rates.

Through all that what we really hope to ensure is that all relevant government parties are talking to each other and working together on legislative reform.

Without that, too often we can discover down the track that legislation has had unintended consequences that actually impede progress or create new problems. Too often government agencies can find themselves working on projects in quite a siloed way that makes it much harder to solve crucial issues effectively.

If the 2020 election was all about managing a level of COVID-19 uncertainty, we are now largely through that and this election is about looking further ahead. We need to start thinking innovatively and with a longer-term perspective in both central and local government, rather than what can be achieved in a three-year term. And we need all parties, including the private sector, working together with a focus on outcomes and how to achieve them.

Cameron Bagrie
Bagrie Economics Economist

The first issue impacting the commercial property sector is that interest rates have moved up, and cap rates are also undergoing an adjustment north. At the moment that adjustment is still in its early days, and when cap rates go up, valuations go down. Interest rates look close to a peak, but cap rates have not moved much.

Listed property vehicles are trading at a pretty big discount to their net tangible asset backing. That suggests the market is fully anticipating further asset write downs and revaluation in the coming 12 to 24 months. There hasn't been a lot of transactions in the market so cap rates are lagging behind the movement in interest rates by a considerable margin.

The second issue concerning the market is refinancing risk and access to credit. It's probably going to be a lot more problematic in the United States because of the pressure on regional banks, but we will start to see some overflow from that in New Zealand. As valuations fall, your leverage goes up and the banks start to have a bit of a closer look at what they're lending and to whom.

The third issue is an increasingly segmented market in terms of quality. Good stuff is in demand, second tier stuff less so. Those B, C and D-grade properties are going to be under a fair bit of pressure. Quality is key if you're a business trying to entice staff back to work, and I think a lot of companies do want their people to be back in the office. Working from home is fine but you don't get that same level of on-the-job learning and knowledge transfer. To get that you really need to be in a team environment. To make that happen, as a company you need to be able to offer your staff all the bells and whistles in an office.

The best thing a Government can do to help the commercial property sector is help the Reserve Bank battle inflation. The more the Government spends, the more the inflationary wheels will keep turning.

The last thing we want is for the Reserve Bank to feel it has to do more, because the Government feels obliged to spend more to keep up with inflationary pressures. At that point you're a mouse on the exercise wheel where more spending adds to inflation and encourages more spending which keeps the inflation pulse strong. We need to break that cycle.

The flipside of all this is that while higher interest rates have a negative impact on commercial property values, inflation can provide a bit of a crutch. When the replacement value of a building has gone up because of rising construction costs, then the value of existing building stock is supported somewhat because of inflation.

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CAMERON BAGRIE, BAGRIE ECONOMICS