Submission of the

Auckland Property Investors' Association (Incorporated) to the

Reserve Bank of New Zealand

Housing review stage two: asset class treatment of residential property investment loans in BS2A and BS2B

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Background

The Auckland Property Investors' Association is a not-for-profit organisation established by its members with a mandate to provide educational and networking opportunities. We run over 100 property investment focused seminars every year.

We have over 1,000 individual members and from a recent survey of the membership our members have approximately 3,700 rental properties (excluding their own primary residence).

Feedback to RBNZ Proposal

The proposals states the RBNZ is looking at trying to 'maintain financial stability' within the New Zealand financial sector. Out of this there appears to be a school of thought that property investment poses a significant risk to the financial market in the event of a cyclical down-turn.

We have recently come through the most turbulent economic times since the Great Depression, that being the Global Financial Crisis (GFC) and property investors clearly were not the cause of the financial markets collapsing.

The risk within the property sectors generally tends to be in the development sector in which many Finance Companies were heavily invested, and the consequential unfortunate results speak for themselves.

A second point is many small to medium businesses owners rely upon the security of their own homes as collateral for bank finance, which provide essential working capital to operate and expand their own business and provide much needed cash flow at various stages of the business cycle. In many cases these loans, which provide finance to support the business, will be riskier than property investment loans.

Another area of the property market that is always hard hit in a cyclical downturn is seaside holiday homes. If cash is needed, these tend to be the first items that are sold, and generally fetch wildly fluctuating prices depending upon the stage of the property cycle at the time that they are being marketed.

Property investment, as distinct from property trading/developing/speculating, is a cash-flow driven business. The majority of landlords and members we represent have been successful over the long term and purchase with a cash flow philosophy. This assists those investors to ride out the economic cycles as the cash flow from the property covers the outgoings. For those investors that don't have sufficient cash flow, they quickly reach a glass ceiling with the banks as the criteria banks use to assess serviceability of loans is generally more conservative than used in many investors calculations, which work out a basic net return on the potential investment. This is because banks will normally factor in a higher interest rate than what is currently available. The more properties an investor owns the more stringent the banks become with their criteria.

As we all are aware, with any new form of regulation always brings in unintended consequences. Rodney Dickens was recently quoted as saying 'No matter how well justified the lending restrictions on low deposit borrowers and the planned targeting of investors by the RBNZ may seem, history teaches us that such interventions impose costs and will most likely have unexpected and undesirable consequences'.

This exact situation has played out with the LVR restrictions allowing a reduced pool of first home buyers to purchase properties. If targeted regulation is brought in to impose statutory capital controls on property investors this will, over time, mean fewer property investors thus reducing the supply of rental accommodation which will inevitably lead to an increase in rental prices. This will be particularly evident in areas like Auckland where there is already a shortage of affordable residential rental properties.

Summary

The RBNZ don't appear to be focusing on the risky sectors within the property market that being property developing, trading and speculating, rather taking aim at the more secure sector of the market being property investment. The guise under which this is proposed is to 'maintain financial stability' within the New Zealand Property sector.

We have recently come through the greatest economic turmoil being the GFC since the Great Depression. This financial calamity being the most severe in the majority of our lifetimes was not driven out of the property investment industry. In fact property investors in general weathered the GFC better than many sectors of the economy. This has clearly proven that property investment is robust, plus this provides clear proof that the servicing and equity requirements the banks currently place upon investors when seeking loans is working.

For the above reasons we don't support any changes to the capital requirements for property investors.