Rub of the green?
Auckland’s urban boundary and land prices

- Housing affordability remains a challenge for many in Auckland. Land use regulations such as the Rural Urban Boundary (RUB) are often blamed.
- But until now, no studies had looked at whether the RUB distorts land markets.
- Pre-RUB studies also underestimated the cost of infrastructure to develop greenfield (or undeveloped) areas, and in some cases ignored the value of location or mis-attributed amenity value.
- Our reviewed analysis shows the RUB accounts for at most between 0.6% and 5.2% of the price of the average developed residential property that has land and is inside the RUB.
- But market prices do not include the social impacts of more expansive development on things like congestion, emissions, viability of public transport and optimal use of existing infrastructure.

- We should evaluate whether these social impacts justify the RUB before bold recommendations are made on the RUB’s future.

The RUB debate

With housing affordability still a challenge for many in Auckland, the finger of blame often points at land use rules, such as the old Metropolitan Urban Limit (MUL) or current RUB, both of which have limited development outside certain areas of the Auckland region. If a growth boundary results in a land price premium that materially increases the cost of housing, then given Auckland’s housing affordability challenge, there would be an argument for removing the boundary.

The facts of this matter are fundamental to the shape of Auckland in terms of its growth, infrastructure provision, and economic and social outcomes. This means any policy to contain or expand development should be based on even-handed, defensible evidence.

The view that the urban boundary imposes a substantial premium on land is universally based on studies done on the obsolete MUL. On 15 November 2016, Auckland’s Unitary Plan became operative, consolidating the different zoning rules in the various legacy plans of the
councils that amalgamated to form the new Auckland Council in 2010. It replaced the MUL with the more flexible RUB, which includes around 30% more land.

The Unitary Plan was the biggest change in zoning rules in New Zealand’s history, and increased physical development capacity in urban areas by around two million dwellings. This is several times Auckland’s projected housing demand over the next 30 years. Within the RUB, allowance has been made for around 137,000 new homes in greenfield areas. These significant changes render previous studies on Auckland’s MUL obsolete.

As our full technical report points out here, previous studies also had a number of other limitations. They generally underestimated or ignored the cost of infrastructure to turn greenfield (undeveloped) areas into residential-ready areas. As a result, they overestimate any price premium on developed residential land.

One often-cited study, which estimated the cost of land use regulation under the MUL at up to 56% or $530,000 of the total price of an average property (not land) in Auckland, also excluded proximity to the CBD as a determinant of property values in Auckland. Yet practically every study that includes this variable finds that proximity (especially to the CBD and/or jobs) matters.

Previous studies have dealt with the value that amenities add to properties with varying accuracy and detail. One study accounted for amenities by using a dummy variable for each suburb, but then assigned the value of this variable to the cost of land use regulation. It effectively assumes the difference in land prices in Ponsonby, with its proximity to jobs, the water, hairdressers, supermarkets and coffee shops, and rural areas near Pukekohe is overwhelmingly the result of land use regulation. But land is not geographically identical. Location matters.

Other gaps in previous analysis that we wanted to overcome included:

- selecting an appropriate way to compare parcels of different land sizes inside and outside the RUB
- using real-world sales data rather than property valuations (to avoid modelling a model)
- accounting for net useable land when converting farm or lifestyle land into residential sized sections
- considering natural hazards such as risk of flooding in determining property values.

The question we posed

Put simply, we ask if converting farm or lifestyle-sized land outside the RUB into infrastructured residential sections similar to already developed land inside the RUB would deliver land to the market more cheaply. If there is a material premium on land inside the RUB, it would imply that the RUB is inflating land prices inside it.

Would converting farm or lifestyle land outside the RUB into infrastructured residential sections similar to already developed sections inside the RUB deliver land to the market more cheaply?

We define the RUB factor as the share of the price of the average developed residential property that has land and is inside the RUB that is attributable to being inside the RUB, if any.

We provide a brief summary of our approach later in this article but recommend the interested reader tackle our full technical report. In short, we built a standard hedonic pricing econometric model to explain property prices as a function of the dwelling, land, and location. We gathered scores of information about the nearly 37,000 farms, lifestyle blocks and residential properties with a land component that sold in and outside the RUB between 15 November 2016 and 31 March 2019. This allowed us to explain much of the variation in property prices depending on property characteristics and location.

What we found

Our goal was to isolate the un-amenitied, a-spatial value of land in farm sized (four hectares or bigger) and lifestyle sized (0.4 to four hectares) land outside the RUB, and compare it to the un-amenitied, a-spatial value of developed residential land inside the RUB (less than 4,000 m² in size).

The “un-amenitied, a-spatial land” value is what remains once we strip out other things that add value to property (such as proximity to jobs, the water, parks, or “good” schools; or the size and condition of the house, views, and contours of the land). We then estimate the value of un-amenitied, a-spatial farm or lifestyle land outside the RUB of the same size as the average developed residential property inside the RUB (618.7 m²) without these confounding factors. Here’s what we found.

**Figure 1 Un-amenitied, a-spatial value of 618.7 m² of land, before accounting for net usable land and infrastructure**

<table>
<thead>
<tr>
<th></th>
<th>Farm-sized</th>
<th>Lifestyle-sized</th>
<th>Residential-sized</th>
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</thead>
<tbody>
<tr>
<td>Outside RUB</td>
<td>$1,069</td>
<td>$7,447</td>
<td>$67,164</td>
</tr>
<tr>
<td>Inside RUB, inside FUZ</td>
<td>$21,594</td>
<td>$28,695</td>
<td>$99,203</td>
</tr>
<tr>
<td>Inside RUB, already developed areas</td>
<td>$70,098</td>
<td>$37,222</td>
<td>$132,665</td>
</tr>
</tbody>
</table>
This figure does **not** say that the average residential section in Auckland costs $132,665. It says that once you have removed almost everything that adds value to a property – its dwelling, its location and amenities, and other characteristics of the land – this is left over. The figure for farm-sized land outside the RUB is $1,069.

**But it would be a mistake to stop the analysis here.**

First, when farm or lifestyle-sized land is converted to residential use, a large share of that land will be converted into roads, stormwater run-off, parks and other uses from which no financial return will be made by the developer. This means the value per square metre of raw land needs to be adjusted upward based on an assumption about how much of the land will be used for non-recoverable purposes once converted to residential use. Recent Auckland structure plans suggest around 57% of land becomes **un**available, meaning the cost of the land must be recovered from the remaining 43%. To err on the side of conservatism (i.e. overestimating the RUB factor, if any), we assume 65% of farm and lifestyle sized land is available for cost recovery.

Second, and far more importantly to the results, the major difference between farm and lifestyle land on the one hand and developed residential land on the other is access to infrastructure – running water, flushing toilets, roads, power and the like. It stands to reason that the cost and value of that infrastructure would add massively to the value of land. Yet only one previous study we know of in New Zealand has made an explicit attempt to account for some of these infrastructure costs.

**Figure 2 RUB factor using various infrastructure cost scenarios**

<table>
<thead>
<tr>
<th>Property location</th>
<th>Higher estimate of bulk infrastructure costs</th>
<th>Average estimate of bulk infrastructure costs, 15% of subsidy priced into land</th>
<th>Average estimate of bulk infrastructure costs, 30% of value to existing users</th>
<th>Lower estimate of bulk infrastructure costs</th>
<th>No allowance for infrastructure costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Farm-sized land outside RUB</td>
<td>-$77,580 (-8.1%)</td>
<td>$15,820 (1.6%)</td>
<td>$27,220 (2.8%)</td>
<td>$50,380 (5.2%)</td>
<td>$58,420 (6.1%)</td>
</tr>
<tr>
<td>Lifestyle-sized land outside RUB</td>
<td>-$87,392 (-9.1%)</td>
<td>$6,008 (0.6%)</td>
<td>$17,408 (1.8%)</td>
<td>$40,588 (4.2%)</td>
<td>$48,608 (5.1%)</td>
</tr>
</tbody>
</table>

The Future Urban Land Supply Strategy (FULSS), which sets out the sequencing for an estimated 137,000 new dwellings in greenfield parts of Auckland **inside** the RUB, provides an insight into the likely bulk infrastructure costs. Our full technical report provides detail on how this work was used to estimate the cost per dwelling in greenfield developments **outside** the RUB. For a number of reasons we list there, the estimates we use for bulk infrastructure in this analysis are likely to be far lower than would be the case outside the RUB, but again, we err on the side of conservatism.

The cost for bulk infrastructure, notwithstanding they are lowball estimates, is eye-watering, ranging from $72,600 to $208,600 per dwelling. The average estimate per dwelling inside the FULSS area is $115,200. We would also note that even these figures do not include all of the infrastructure provided by central government or other costs of subdivision, including surveying, resource consent, legal and Land Information New Zealand fees that would be incurred in cutting up a farm or lifestyle land into residentially-sized sections.

Applying six different estimates of the possible cost of bulk infrastructure to develop farm and lifestyle land outside the RUB into useable developed residential properties similar to those inside the RUB, yields the RUB factors in Figure 2. The most defensible **upperbound** estimates of the RUB factor are in the dark grey boxes. We have pointed out the absurdity of a view that no infrastructure costs should be allowed for, but present that result too for the sake of completeness.
The most likely upperbound range of values for the RUB factor is 0.6% to 5.2% of the value of the average developed residential property with land inside the RUB (value of $960,000). We label this an upperbound range in large part because of the low estimates of infrastructure we have used throughout, and our exclusion of other subdivision costs altogether.

We ran numerous sensitivity tests on different model specifications, many at the suggestion of our external reviewers. None of the tests changed the modelled results in either direction by more than a few percentage points.

This last point is important. At higher infrastructure cost estimates, or different model specifications, it is possible that properties outside the RUB actually carry a premium. This would likely be because often two-thirds or more of the cost of bulk network and social infrastructure in greenfield areas is not borne by the property developer. Assumptions that this will continue to be the case may be encouraging land prices to be bid up outside the RUB, with the anticipation that the RUB might expand or disappear altogether.

What does all this mean?

Our analysis shows that the RUB factor, if any, is massively lower than previous work on the MUL had suggested. The reality of what the Unitary Plan has seemingly done to land markets, and accounting better for infrastructure and amenities matters significantly to how we think about the impact of the RUB.

What about the social costs of sprawl?

Further, market prices do not include the relative social impacts of more expansive development on congestion, emissions, viability of public transport and optimal use of existing infrastructure, for instance. Our work provides a starting point for an informed debate on whether a RUB factor of up to 5.2% is justified given the social costs that may be part of more expansive development that would come with relaxing or removing the RUB.

A thorough analysis of whether these social impacts justify the RUB should be completed before bold recommendations are made on the RUB’s future, given the impact keeping or removing the RUB has on the shape of New Zealand’s largest city, its infrastructure needs and community outcomes.

How we did it

The interested reader will want to read our full technical report. But in summary, we used hedonic price models with spatial error disturbances to explain prices in farm, lifestyle and residential properties. We tested numerous models, but settled on a three-model approach with separate models for farm, lifestyle and residential sized properties, all of the same specification. This allowed for different values to be placed on amenities or the value of an additional square metre of land by property size category.

We did not use a “difference in difference” modelling approach, as we were not asking how the RUB affects land market prices relative to the MUL, but rather how the land market operates today, since the Unitary Plan and RUB were introduced. Further, the results of a difference in difference analysis could almost certainly not be meaningfully interpreted. Land that was outside the MUL but is now in greenfield areas inside the RUB would be expected to increase in value given the promise of infrastructure, but how much would be largely a subjective interpretation.

We are confident in the reasonableness and explanatory power of our preferred model, but we ran numerous sensitivity tests. These tests included using spatial error and lag models; a number of different spatial weights; models with and without median income; with and without zoning; with and without additional RUB, or RUB and FUZ dummy variables; with different thresholds for setting size categories; using log forms for estimating the value of an additional square metre of land; using capital value instead of actual sale prices; and using one combined model instead of three.
Auckland Economic Commentary

Shyamal Maharaj
Economist, Chief Economist Unit

- In a year plagued with downbeat confidence measures, the Auckland economy held its own despite sentiment.
- The market appears to be applying more weight to real-world data rather than sentiment, which is a welcome change.
- Auckland’s unemployment rate fell to 4.1% (the lowest rate for the year), the participation rate improved a touch coupled with strong wage growth, which continues to support the view of a tight labour market.
- House prices are back on the rise through historically low mortgage rates, certainty over capital gains tax and improving sentiment. We expect house prices will continue to rise modestly against such a backdrop.
- Residential buildings consented surged past 15,000, and with the pipeline of building work yet to be completed, the construction sector is likely to remain a key driver for the Auckland economy in 2020.

Auckland’s economy is doing quite well and solid growth is set to continue over 2020. A grey cloud over 2019 was the increasingly disconnected and pessimistic results from business confidence measures. However, in the latter months of the year, business confidence came off its lows (albeit still net pessimistic), signalling that businesses are better connecting sentiment with reality.

The unemployment rate fell to 4.1% in Auckland for the December quarter, driven mostly by a fall in the unemployment rate within the 40-54 age category. These figures ended 2019 on a positive note, signalling that businesses in actuality continue to hunt for workers.

The participation rate improved a touch in the December quarter and has remained broadly flat compared to the year before. Wages continue to grow more strongly, which is a strong signal that businesses are doing better than sentiment has suggested throughout 2019. As wages rise, people will spend, supporting inflation and thus translating into achieving the goals of the RBNZ’s interest rate policy. But stronger wage rises, absent until about nine months ago, also signal that we may now be approaching the bottom of the unemployment curve.

A tight labour market in terms of policy suggests to some like the RBNZ that an unemployment rate of 4.0% is at or around the maximum sustainable level. This is the rate at which inflation neither increases nor decreases from one additional worker being employed. This is likely to be vital in considering future policy moves for 2020.

House prices in Auckland have regained momentum especially at the back end of 2019, driven largely by historically low mortgage rates and with the OCR expected to remain at low for a considerable period of time. March 2020 is likely to see median house prices in Auckland rise above $900,000. Higher house prices generally mean higher spending, as home owners spend some of their wealth gains on new furnishings and/or other nice to haves. This bodes well for the broader Auckland economy, but does create further risk of a widening wealth gap.

For 18 months we argued against further price declines given the underlying housing shortfall, that since the Global Financial Crisis has led to a rise in people per dwelling. The current rise in house prices will mean the brief period of having the most affordable housing in almost six years has come to an end. We expect mortgage serviceability to deteriorate despite a backdrop of low mortgage rates.

The one potential spanner in the works is the coronavirus outbreak. It has already sent some jitters through global markets. If it does establish further in New Zealand, we could see nervousness in housing markets that could stall the current buyer positivity as confidence would fall.

Dwellings consented surged past 15,000 in 2019, breaking all previous Auckland records. In the last twelve months, new dwellings consented rose by 18% and since the Unitary Plan we have seen a 48% rise in annual dwellings consented. 2019 was the first year since records began where every month had over 1000 dwellings consented in Auckland.

This record high level of dwellings consented signals a strong pipeline of construction activity for 2020 and beyond. Notably, the recent buoyancy in the housing market is also expected to further support residential building consents. Nevertheless, we recognise that there is a chance that 2020 could see these numbers peak especially as a backlog of building still remains.

Meanwhile, commercial building consents have peaked and fallen back off record highs. Although levels have peaked, there is a large backlog of building yet to be done. As the Commercial Bay development wraps up, the capacity from there is likely to be redirected elsewhere within Auckland. Construction on the New Zealand Convention Centre came to an abrupt halt due to the fire but recent news suggests construction on that project may recommence shortly.
Additionally, the government has recently announced spending on a range of much-needed infrastructure for Auckland, bringing forward many projects. But we note this may pull away capacity from private construction activities, and could see cost rises as the public and private sector battle it out for resources/capacity.

The one damper on the Auckland economy is tourism. Growth has been mild over the 12 months to December, but again coronavirus will hit visitor numbers hard in the March quarter data, so expect to see weak results when we report on those in our May edition of the AEQ.

Coronavirus aside, we would have expected 2020 to be a year of solid across many fronts in the Auckland economy. But uncertainty over how long and how intense New Zealand’s exposure to the virus makes it hard to predict this early on how quickly Auckland will bounce back.

With real impacts on tourism already occurring, and some other industries facing demand and supply chain disruptions, it is likely the Reserve Bank will take action in March. The government will also look to provide further financial support should the situation worsen in New Zealand.

More data woes

Sadly, another useful Statistics New Zealand dataset on international connections – commercial accommodation guest nights – has come to an end, so we can no longer report on this.

We would also note that Statistics New Zealand is undergoing a four-step process of reviewing Household Labour Force Survey data in light of Census 2018 and updated population estimates. Two of the four steps are complete, but two more revisions are on the way. This makes direct comparison of this quarter’s youth unemployment rates with previous quarters invalid, so interpret these numbers with a pinch of salt for now.

Data summary provided by Ross Wilson - Analyst, RIMU

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Dec-19 quarter</th>
<th>Sep-19 quarter</th>
<th>Dec-18 quarter</th>
<th>5-year average</th>
<th>Rest of New Zealand Dec-19 quarter</th>
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<td>Employment indicators</td>
<td></td>
<td></td>
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<tr>
<td>Annual employment growth (%pa)</td>
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<td>0.8%</td>
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<td>2.6%</td>
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<tr>
<td>Unemployment rate (%)</td>
<td>4.1%</td>
<td>4.2%</td>
<td>4.3%</td>
<td>4.8%</td>
<td>4.0%</td>
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<td>Unemployment rate among 20 to 24 year olds (%)</td>
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<td>9.4%</td>
<td>9.9%</td>
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<td>Unemployment rate among 15 to 19 year olds (%)</td>
<td>17.5%</td>
<td>17.1%</td>
<td>21.5%</td>
<td>20.6%</td>
<td>18.0%</td>
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<td>Earning and affordability indicators</td>
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<td>Annual nominal wage growth (%pa)</td>
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<td>3.1%</td>
<td>2.7%</td>
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<td>Annual geometric mean rent growth (%pa)*</td>
<td>-0.4%</td>
<td>1.9%</td>
<td>1.5%</td>
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<td>Geometric mean rent to median household income ratio (%)*</td>
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<td>27.1%</td>
<td>27.9%</td>
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<td>Annual median house price growth (%pa)*</td>
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<td>Mortgage serviceability ratio (relative to Dec-06)*</td>
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<td>Construction</td>
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<td>Annual new residential building consents growth (%pa)</td>
<td>17.8%</td>
<td>13.0%</td>
<td>10.8%</td>
<td>14.7%</td>
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<td>Annual m2 non-residential building consent growth (%pa)</td>
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<td>International connections</td>
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<td>Annual Auckland Airport passenger movements (%pa)</td>
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<td>Confidence</td>
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<td>Annual retail sales growth (%pa)</td>
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<td>4.5%</td>
<td>-17.8%</td>
<td>6.1%</td>
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<td>Quarterly Survey of Business Opinion (net optimists)</td>
<td>-12.4%</td>
<td>-38.4%</td>
<td>-28.6%</td>
<td>-1.9%</td>
<td>-26.3%</td>
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<tr>
<td>Westpac Consumer Confidence*</td>
<td>112.9</td>
<td>106.7</td>
<td>109.5</td>
<td>110.8</td>
<td>109.9</td>
</tr>
</tbody>
</table>

Sources: Chief Economist Unit, Auckland Council; Statistics New Zealand; Ministry of Business Innovation and Employment; Real Estate Institute of New Zealand; New Zealand Institute of Economic Research; Westpac; Reserve Bank of New Zealand. * Rest of New Zealand figures are for all of New Zealand including Auckland. Data is not seasonally-adjusted.

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