

Before the Independent Hearings Panel

Under the Resource Management Act 1991

In the matter of submissions on the Inclusionary Housing Variation to the Queenstown Lakes Proposed District Plan

Statement of evidence of Theodore Ries on behalf of the Darby Partners Limited Partnership

19 December 2023

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Introduction

- 1 My full name is Theodore Benjamin Ries.
- 2 I am an Investment Manager at Darby Asset Management.
- 3 I hold the qualifications of Bachelor of Legal Studies from the University of California at Berkeley, and Certified Commercial Investment Member.
- 4 This evidence is provided on behalf of Darby Partners Limited Partnership (**DPLP**), in relation to the Inclusionary Housing Variation to the Queenstown Lakes Proposed District Plan (**PDP**) (**Variation**).

Scope of Evidence

- 5 My evidence addresses the following:
 - (a) the imposition of costs which will markedly reduce profitability for developers; and
 - (b) the viability of new residential section construction.
- 6 I have reviewed the following documents in preparing this evidence:
 - (a) Inclusionary Housing Plan Change - Section 32 report;
 - (b) Inclusionary Housing Plan Change - Proposed Provisions;
 - (c) The economic case for Inclusionary Zoning in QLDC – An important piece of the puzzle (Sense Partners);
 - (d) Inclusionary Housing Section 42A Report (David Mead); and
 - (e) Inclusionary Housing Evidence of Shamubeel Eaqab (Economic).

Executive summary

- 7 The proposed Variation would have a significant impact on land development economics, and is likely to create adverse effects on the broader housing market. Such effects would, in turn, undermine the very goals which the Queenstown Lakes District Council (**QLDC**) is seeking to achieve.

Reduced developer profitability

- 8 Land development is a time and capital-intensive process which demands a risk premium; that is, developers need to anticipate a certain degree of profitability in order to undertake new projects. The proposed Variation will

impose costs which will markedly reduce profitability. It is not reasonable to assume that land developers will tolerate such reduced economic returns – there is simply not enough compensation for the risk that they are taking.

- 9 This means that the Variation will lead to one (or a combination of) three outcomes:
- (i) the price paid by developers to purchase development land parcels must fall in order to compensate for reduced profitability otherwise;
 - (ii) the price of developed residential sections must rise in order to create increased profits per residential section sold; or
 - (iii) neither of the two above outcomes transpires and there is simply less residential development.

Viability of new residential construction

- 10 A detailed discussion of land development economics is outside the remit of this submission. However, it is critical to understand that a 5% reduction in gross sales proceeds from a land development project (as would be the case in many instances under the proposed Variation) leads to a very dramatic shift in developer profitability, and hence the viability of new residential section construction.
- 11 A set of generic figures will illustrate this point. Consider a scenario whereby a developer wishes to acquire land and construct 30 residential sections:
- In the current environment, such a developer is likely to target an after-tax return on equity of 20%; in other words, they will seek to realise \$1.20 for every dollar of equity that they (or their investors) put into the project.
 - A typical project might use bank debt equivalent 60% of the net sales value of the completed sections.
 - Profits to the developer are comprised of the dollars left over after selling lots and: repaying the bank's principal, paying accrued interest charges, buying land, incurring planning and consenting costs, paying contractors, paying GST on sales, paying commissions, and paying tax on profit. In other words, profits are comprised of the residual dollars left over after every other party has been paid.
 - The 5% reduction in sales proceeds (or serviced lots, which bears the same net economic implications) contemplated by the Variation

would impact developers in two ways: reducing profitability while also reducing the amount which a developer can borrow. This means that there is less profit available to provide economic return for a higher required amount of equity capital. In other words, more equity is needed in order to realise less overall profit.

- It is unrealistic to assume that the costs of consenting and building sections is likely to change; indeed, many builders are already under pressure due to rising construction costs and falling margins. Likewise, availability of construction finance has become much more constrained as trading banks seek to reduce their lending exposure. Thus, the only parties theoretically capable of 'restoring' the profitability lost by developers under the proposed Variation are sellers of land and buyers of sections.
 - A 5% reduction in available revenue means that prices of completed lots would need to rise by $(100\%/95\% = 5.3\%)$ to make developers 'whole'. Alternatively, if we assume that the initial purchase of raw land comprises 50% of the overall cost of development (i.e. that the cost of raw land is equivalent to the cost of consenting and constructing sections on such land), then raw land prices would need to fall by approximately 10% to restore comparable developer economics.
- 12 The brief analysis above, shows that costs imposed via the Variation must be borne elsewhere in the market: either by land sellers or section buyers. In the first instance, if we assume that the price of raw land would need to fall by circa-10% in a typical project for the reasons set out above, then some proportion of landholders may simply elect to withdraw their property from the market. The Queenstown Lakes District is already highly supply-constrained. A single rural landowner declining to sell property to a developer, rather than take a 10% 'haircut' on price, could in and of itself significantly reduce overall potential housing stock. It is worth noting that such landowners have generally held their properties for a considerable length of time, and are often capable of waiting out an unfavourable market.

Adverse implications of the Variation on housing affordability

- 13 In the event that the costs described above are passed on to section buyers in the form of higher prices, then all that QLDC will have accomplished by the Variation is driving lot inflation in an already unaffordable real estate market. Unfortunately, the weight of this cost increase would fall most heavily on lower-income working households, particularly those seeking to get on the property ladder for the first time. Such purchasers are already

forced to cope with substantially higher mortgage rates; adding cost will mean that more such families are unable to afford homes. Again, this would exacerbate exactly the problem which QLDC I is setting out to alleviate. It is likewise work considering that added property costs are not a one-off expense. Rather, homeowners will be paying interest on the incremental cost for decades. For example, if a section which would otherwise have cost \$400,000 increases in cost to \$425,000 due to implementation of the Variation, then a typical buyer will need to come up with \$5,000 in added down payment expense, and will have to pay interest on an additional \$20,000 of borrowing for perhaps 30 years. At a blended interest rate of 7% over the life of the mortgage, this equates to \$42,000 of added cost. While this would enrich (largely foreign-owned) trading banks, it would be punitive to local residents.

Conclusion

- 14 I strongly urge the Council to reconsider the proposed Variation in light of the consequences set out above. The draft change is likely to constrain the supply of new housing which the Queenstown Lakes District desperately needs, while saddling working families with financial burdens which they will be hard-pressed to bear. Such outcomes are not only problematic in their own right, but would actively undermine the core purpose of the Variation: to make life better for the working families of the Queenstown Lakes District.

Theodore Ries

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