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Residential building supplies market study

Preliminary Issues paper

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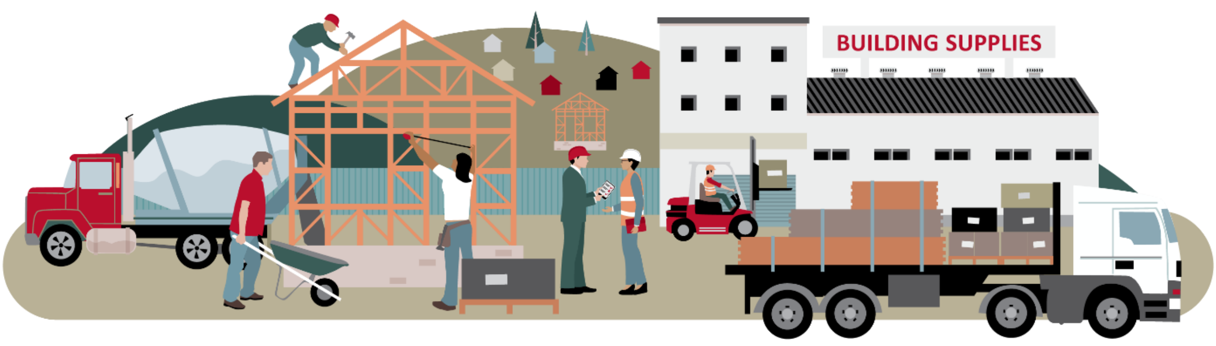

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Contents

Glossary

Builders	Market participants who conduct the onsite and/or offsite construction of residential housing including, for example, developers, group home builders and sole traders.
Building Code	The Building Code is contained in Schedule 1 of the Building Regulations 1992 and continues in force under the Building (Forms) Regulations 2004 and the Building Act 2004. The Building Act governs the building sector and sets out the rules for the construction, alteration, demolition and maintenance of new and existing buildings in New Zealand.
Building Consent Authority	The function contained within each Territorial Authority or private organisation permitted to perform building consenting and Building Code compliance certification functions under the Building Act 2004.
Key building supplies	The products and product systems used to build the major components of residential buildings.[1]
Importers	Market participants who import the building supplies used in the construction of residential buildings.
Major components of residential buildings	For the purposes of this study, the major components of residential buildings are the foundation, flooring, roof, walls (structural and non-structural, interior and exterior) and insulation.
Manufacturers	Market participants who produce in New Zealand the building supplies used in the construction of residential buildings.
MBIE	Ministry of Business, Innovation and Employment.
Merchants	Market participants who act as intermediaries purchasing building supplies from manufacturers or importers and selling to Builders or other end users.
Residential	For, or directly related to, the housing of individuals.
Vertical Arrangements	Arrangements between market participants at different levels of the supply chain; including contractual arrangements. For example, arrangements reached by suppliers to provide rebates to purchasers if a certain level of supply is purchased.
Vertical Integration	The combination in one firm of two or more levels of the supply chain. For example, one firm acting as both a Manufacturer and Merchant.

1 As detailed below, we are currently consulting on the key building supplies which this market study should focus on.

Wholesalers	The Manufacturers and Importers who supply Merchants and other parts of the distribution chain.

Introduction

1. The Minister of Commerce and Consumer Affairs (Minister) has required that the Commerce Commission (Commission) carry out a study under Part 3A of the Commerce Act 1986 (Act) into any factors that may affect competition for the supply or acquisition of key building supplies used to build the major components of residential buildings (key building supplies). For the purposes of this study, the major components of residential buildings are the foundation, flooring, roof, walls (structural and non-structural, interior and exterior) and insulation.

2. Housing plays a vital role in the wellbeing of New Zealanders. There is high demand for new residential buildings, with consents having more than tripled in the last 10 years.[2] Building materials make up a significant proportion of the cost of building new housing and renovations or extensions to existing housing. It is therefore important that competition is working well in the markets for key building supplies. If competition is working well, this will benefit consumers through the prices they pay for key building supplies, the quality and range of supplies available, and the level of innovation within the industry.

3. This study provides an opportunity to consider whether competition in the supply or acquisition of key building supplies could work better for the benefit of New Zealand consumers over the long term. This includes considering how competition is operating at all levels of the supply chain and how that might change going forwards.

4. The Commission acknowledges its obligations under Te Tiriti o Waitangi and is committed to engaging with Māori to hear the perspectives which are relevant to this study. We are committed to having regard to a Te Ao Māori view as part of the engagement process.

5. We expect this study will help to inform the public, the industry and Government about the nature of competition for key building supplies and how the industry operates at present.

6. We are required by the terms of reference to make the final report from this study publicly available by 6 December 2022. The final report may include recommendations that identify ways to improve competition in the sector for the long-term benefit of New Zealand consumers.

Purpose of this paper

7. This paper provides a brief overview of our current understanding of the residential building supplies industry in New Zealand, and the potential issues raised by the terms of reference for this study and which we may explore as part of it.

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[2] MBIE "Building and Construction Sector Trends – Annual Report" (29 September 2021) at Figure 6, available at: https://www.mbie.govt.nz/dmsdocument/16973-building-and-construction-sector-trends-annual-report-2021-pdf.

8. We invite responses from all interested parties – including industry participants involved at any level of the supply chain, such as manufacturers/suppliers, building supplies merchants and other retailers, product specifiers and purchasers.

9. Stakeholders are also likely to include construction industry associations and representative bodies, government departments, Building Consent Authorities and other interested parties or market participants.

10. We will engage with tangata whenua as Tiriti o Waitangi partners and stakeholders in the study, including with whānau, hapū, iwi and Māori industry representatives, interested parties or market participants. We plan to engage with Māori directly in this process and will be in contact with partners and stakeholders in due course.

11. We invite views from all interested parties to help further our understanding of the industry and decide where to focus our efforts during the study.

Structure of this paper

12. This paper has three main sections.

    12.1 **Our role and the process for the study** describes what a market study is, the terms of reference for this study, and how you can be involved in the process.

    12.2 **Overview of residential building supplies in New Zealand** provides a brief overview of our current understanding of the industry. It also provides some of our initial views regarding the scope of the study, having regard to the terms of reference.

    12.3 **Potential issues we may consider during the study** outlines our proposed approach to the issues raised by the terms of reference for this study. These issues are grouped under three headings:

        12.3.1 the industry structure for key building supplies;

        12.3.2 the nature of competition for key building supplies; and

        12.3.3 impediments to entry or expansion, including for new or innovative building supplies such as 'green' building supplies and novel prefabricated products.

13. The issues discussed in this paper do not pre-suppose that there are competition issues in the industry. We have attempted to identify potential factors which may be affecting competition, so that these can be explored during the study. These issues have been identified based on the information available to date and the direction given to us as set out in the terms of reference for this study.

14. We expect that the issues we focus on will be refined as our understanding of the industry develops. Feedback received from stakeholders during the study, including in response to this paper, will help us identify the issues we ultimately focus on in this study.

Our role and the process for the study

15. This section provides an overview of:

    15.1 our role when undertaking a market study;

    15.2 the terms of reference for this study;

    15.3 our intended process for this study; and

    15.4 how you can have your say on this paper.

Our role is to study competition and factors that may affect it

16. A market study, referred to as a "competition study" in Part 3A of the Act, is a study of any factors that may affect competition for the supply or acquisition of goods or services.[3]

17. Market studies allow us to examine whether markets could work better for New Zealanders. By gathering and analysing information on markets we can identify whether there are factors preventing competition from working well. We can then consider if competition in a market could be improved and, if so, make recommendations about how to make markets work better for the benefit of New Zealanders.

18. Further guidance on our approach to undertaking market studies can be found in our Market Studies Guidelines.[4]

The terms of reference for this study have been set by the Minister

19. We must carry out a market study in accordance with the terms of reference issued by the Minister. We may also consider any ancillary matters that are related to, but not explicitly covered by, the terms of reference.[5]

[3] See Section 48 of the Act.

[4] Commerce Commission "Market Studies Guidelines" (19 November 2020).

[5] See Section 51A(4)(b) of the Act.

20. The terms of reference for this study are set out in the box below.[6]

Notice for Commerce Commission Competition Study into Residential Building Supplies

I, Hon Dr David Clark, Minister of Commerce and Consumer Affairs, pursuant to section 51(1) in Part 3A of the Commerce Act 1986, require the Commerce Commission to carry out a competition study into any factors that may affect competition for the supply or acquisition of key building supplies used to build the major components of residential buildings.

Matters to be considered in the study may include, but are not restricted to:

1. The industry structure for key building supplies covered by this study.

2. The nature of competition for these key building supplies, including any industry pricing practices or acquisition requirements that impact on competition.

3. Impediments to the entry or expansion of new or innovative building supplies, such as 'green' building supplies or novel prefabricated products.

For the purposes of this study, major components of residential buildings are the foundation, flooring, roof, walls (structural interior and exterior and insulation).

The Commerce Commission should make its final report for this study publicly available by **6 December 2022**.

21. The Minister considered it in the public interest to require a study into residential building supplies. That assessment was based on the following indicators suggesting there may be impediments to competition in the supply or acquisition of key building supplies:[7]

    21.1 the supply of some building supplies is highly concentrated;

    21.2 there is a high level of vertical integration in the supply chain;

    21.3 pricing of building supplies is not transparent, with a perceived widespread use of rebates and loyalty schemes; and

    21.4 difficulties for new building supplies to enter New Zealand, including anecdotal evidence of issues in the building consent process.

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6 New Zealand Gazette "Notice for Commerce Commission Competition Study into Residential Building Supplies" (22 November 2021) (Gazette Notice), available at: https://gazette.govt.nz/notice/id/2021-au4934.

7 Cabinet paper "Initiating the Third Commerce Commission Market Study" (22 November 2021) (Cabinet paper 2021), available at: https://www.mbie.govt.nz/dmsdocument/18006-initiating-the-third-commerce-commission-market-study-proactiverelease-pdf.

Our process ends with a final report in December 2022

22. The process for this study is described in our Statement of Process paper.[8] That paper outlines the process we intend to follow over the course of the study and how interested parties can remain informed. Attachment A provides a summary of our intended timetable and indicative key dates over the course of the study.[9]

23. We welcome responses to this Preliminary Issues paper from all interested parties. We also intend to continue engaging more directly with a range of stakeholders in late 2021 and early 2022.

24. We are committed to meeting our Te Tiriti o Waitangi obligations, which includes early and authentic engagement with whānau, hapū, iwi and Māori. We welcome in particular responses from Māori representatives and industry participants involved at any level of the supply chain to inform the issues we need to focus on throughout the study.

25. We recognise the impacts that the COVID-19 pandemic continues to have for many entities and that these may affect some stakeholders' ability to engage with us during the study. We aim to be responsive to any issues that may be encountered by stakeholders due to COVID-19, while at the same time balancing those needs against the need to provide our final report by December 2022.

How you can have your say on the issues for this market study

26. We are seeking your views on the issues and questions raised in this paper, or on any other issues that you consider important. Your views will help us to understand relevant issues in the supply or acquisition of key building supplies and help us decide where to focus the effort and analysis during the study.

27. You do not need to respond to all the issues and questions raised – you can instead respond to a single issue or question or address just the issues or questions that relate to your business operations or experience.

28. Please send any responses by email to: buildingsuppliesmarketstudy@comcom.govt.nz

29. To ensure your views can be taken into account, please provide these to us by **4pm, 4 February 2022**. You will also have further opportunities to contribute to this study, as described in our Statement of Process paper.

30. For ease of reference, Attachment A to this paper includes:

    30.1 further details on how to provide your views on this paper;

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8 Commerce Commission "Market Study into Residential Building Supplies – Statement of Process" (22 November 2021), accessible at: https://comcom.govt.nz/__data/assets/pdf_file/0021/271281/Market-study-into-residential-building-supplies-process-paper-Statement-of-Process-22-November-2021.pdf.

9 Commerce Commission "Attachment A – Residential Building Supplies Market Study Preliminary Issues Paper", accessible at: https://comcom.govt.nz/?a=273554.

30.2 a complete list of the questions asked throughout this paper; and

30.3 details about what to do if you are sharing confidential or commercially sensitive information, or wish to remain anonymous.

Overview of the residential building supplies industry

31. This section provides a brief overview of our current understanding of the residential building supplies industry in New Zealand, based on the information we have reviewed to date.

32. The information in this section provides context for our proposed approach to the issues raised by the terms of reference and the potential competition issues identified later in this paper. We also set out our initial views on the scope of the study, having regard to the terms of reference.

33. This section discusses:

33.1 the importance of building supplies to New Zealanders;

33.2 the nature of the industry and supply chain;

33.3 the wide range of products used in residential building construction;

33.4 some of the unique characteristics of building in New Zealand;

33.5 the acute demand and supply chain pressures the industry currently faces;

33.6 the evolving regulatory framework; and

33.7 climate change and implications for the future of building supplies.

34. We expect our characterisation of the industry will continue to evolve as the study progresses. We welcome comments on the preliminary overview contained in this section. We are interested in views regarding all levels of the supply chain.

The importance of building supplies to New Zealanders

35. Residential construction is a fundamental part of the New Zealand economy, and has significant ramifications for the wellbeing of New Zealanders. Housing is the single biggest expenditure undertaken by most New Zealand households.[10] Maintaining and expanding our housing stock is a critical part of providing for our growing population.

36. Residential building activity has been on an overall growth trend since 2012.[11] The value of residential building work was $18.7 billion in the year ended June 2021

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[10] MBIE "Residential Construction Sector Market Study – Options Paper" (6 November 2013) (MBIE Options Paper) at page 7, accessible at: https://www.interest.co.nz/sites/default/files/residential-construction-sector-options-paper.pdf.

[11] MBIE "Building and Construction Sector Trends – Annual Report" (29 September 2021) (MBIE 2021 Annual Report) at figure 6, accessible at: https://www.mbie.govt.nz/dmsdocument/16973-building-and-construction-sector-trends-annual-report-2021-pdf.

(about 5.4% of GDP),[12] up from $5.5 billion in the year ended June 2012.[13] New residential building consents are at record high levels, with 47,331 being issued in the year ended September 2021 (up 25% from the previous year).[14]

37. New building consents appear to make up the largest proportion of the value of residential building consents. The value of alterations and additions to residential buildings has increased from $1.3 billion in the year ended June 2012 to $2.5 billion in the year ended June 2021, making up slightly over 10% of the total value of consented work.[15] Therefore, most of the growth described above comes from new building activity.

38. In considering any factors that may affect competition for the supply or acquisition of key building supplies, we anticipate we will need to consider key building supplies both for new housing and for renovations and/or extensions to existing housing. To the extent there may be differences in materials used,[16] we are likely to focus more on new buildings as this appears likely to represent a greater share by value of the work undertaken.

39. Building materials have been estimated to be around 20% of overall residential building costs.[17] Land and associated infrastructure costs, labour, GST, professional fees and a range of other costs are also significant components of the overall cost of housing. Those other costs are outside the scope of this study.

Questions on the importance of building supplies to New Zealanders

Q1 What impact is the current level of competition in the building supplies industry having on New Zealand businesses and the general public?

Q2 How important is it for us to consider building supplies for renovations separately from building supplies used for new builds?

Q3 Are there any aspects of the building supplies industry which have a particular impact on Māori?

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12 RBNZ "Gross Domestic Product (M5)" (16 September 2021), accessible at: https://www.rbnz.govt.nz/statistics/m5.

13 Stats NZ Infoshare "Building activity by region (Annual-Jun)".

14 Stats NZ "Building consents issued: September 2021" (2 November 2021), accessible at: https://www.stats.govt.nz/information-releases/building-consents-issued-september-2021.

15 Ibid.

16 For example, alterations and renovations may require work utilizing or product selections in keeping with the materials used originally for the construction of the property.

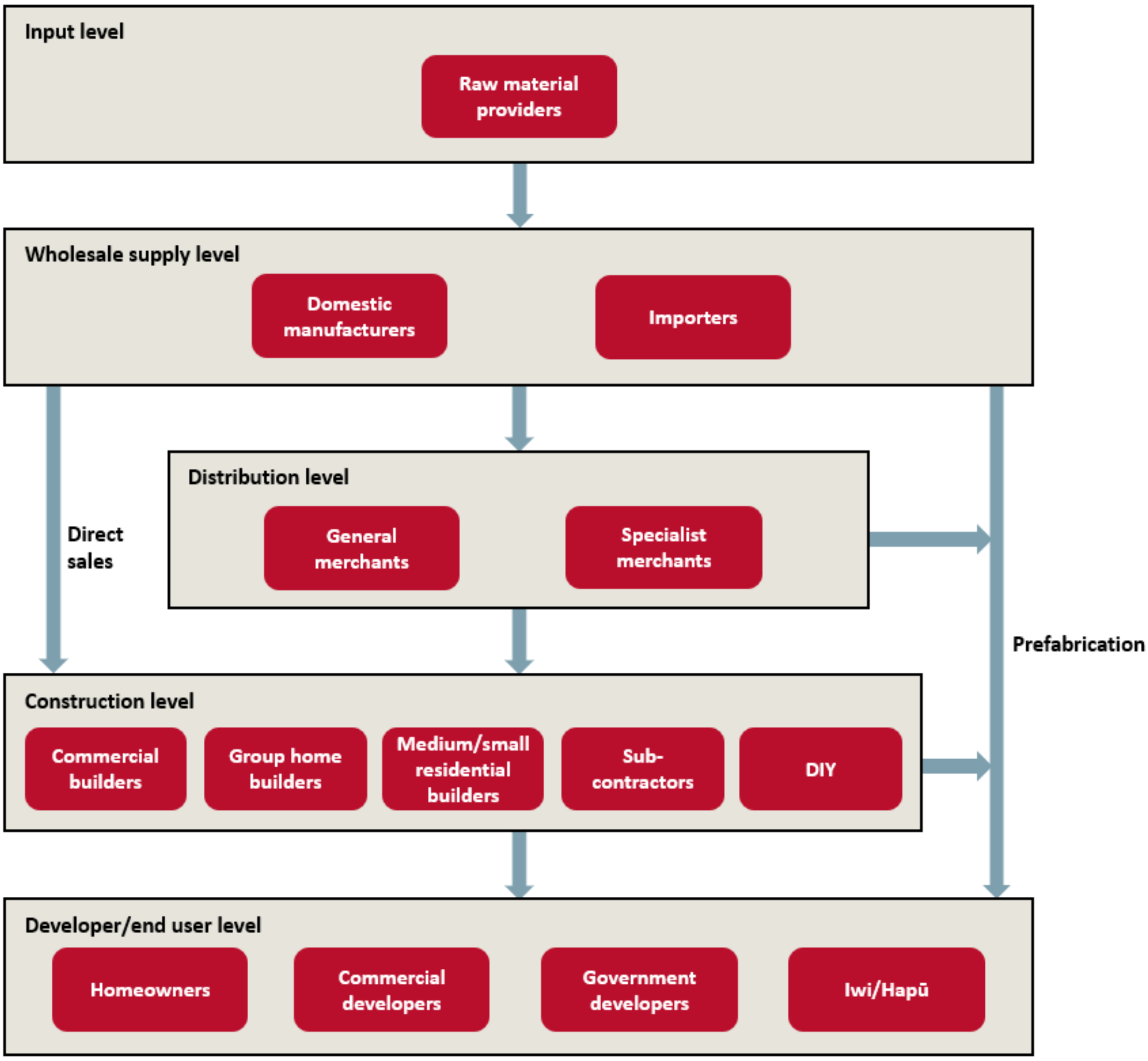
17 Increasing if land and infrastructure costs are excluded. Deloitte Access Economics "Cost of residential housing development: A focus on building materials" (December 2018) at page 13, accessible at: https://www2.deloitte.com/content/dam/Deloitte/nz/Documents/Economics/nz-en-DAE-Fletcher-cost-of-residential-housing-development.pdf.

The nature of the industry and supply chain

40. Residential building supplies pass through a series of levels of the supply chain before they are used in construction. Figure 1 below provides a high-level summary of this supply chain.

41. It is important to note that the supply chain may vary for different types of products or construction projects. For example, there may be certain products that are not sold through merchants or certain building groups that buy directly from manufacturers or importers. Figure 1 is intended to be representative only.

Figure 1: High-level summary of the generic supply chain for residential building materials[18]



42. There are at least two significant vertically integrated suppliers with activities spanning several levels of the supply chain, being:

[18] Each red box represents a group of market participants but is not intended to reflect any formally defined market.

42.1 Fletcher Building - active in wholesale supply, distribution (through building supplies merchant PlaceMakers) and residential construction; and

42.2 Carter Holt Harvey - active in wholesale supply and distribution (through building supplies merchant Carters).

43. Each level of the supply chain has other participants of varying sizes and business structures:

43.1 At the wholesale supply level, there are a number of domestic manufacturers. These manufacturers tend to specialise in one type of building supply such as timber (for example, Red Stag) or cement (for example, Allied Concrete). There are, in addition, some international building supply companies that import into New Zealand. There have been some notable departures from the industry; for example, USG Boral which previously imported plasterboard.[19]

43.2 At the distribution level, in addition to PlaceMakers and Carters, there are three other major building supplies merchants with significant national presence; being Bunnings, Mitre 10, and ITM. We understand that PlaceMakers, Carters and ITM cater primarily to builders and trade customers, while Bunnings and Mitre 10 have both trade centres and retail-focused stores (which also cater to some trade customers). Outside of these major merchants, a number of smaller merchants and retailers have varying presence and carry varying product ranges throughout New Zealand.

43.3 At the residential construction level, there is a wide range of different business models. Larger group home builders include GJ Gardner Homes, Signature Homes, Mike Greer Homes, Golden Homes, and Classic Developments. There is also a diverse range of small-to-medium enterprise builders, as well as sub-contractors and DIY builders, as shown in Figure 1.

43.4 At the end-user level, consumer preferences shape the types of structures being built and can influence the choice of materials. Other developer end-users such as Kāinga Ora can be major drivers of demand for residential construction. Hapū and iwi are also building large-scale residential developments or working in partnership with other developers.

44. We intend to consider factors that may affect competition for the supply or acquisition of key building supplies at all levels of the supply chain. We will also consider how this may change in the future, given the potential impacts that building for climate change and de-carbonisation could have on building supplies.

45. In addition to the manufacturers, importers and suppliers of key building supplies, builders and homeowners, a number of other participants play significant roles in the end-to-end construction process:

19 Brent Melville "Building group USG Boral quits NZ, 45 jobs lost" (5 August 2021) BusinessDesk. Accessible at: https://businessdesk.co.nz/article/infrastructure/building-group-usg-boral-quits-nz-45-jobs-lost.

45.1 Architects and other specifiers (such as building designers and quantity surveyors) can have a significant influence on the types of structures being built and on the selection of products and materials used.

45.2 Building Consent Authorities (BCAs) issue building consents and inspect newly constructed buildings to ensure compliance with the Building Code.[20] Each of New Zealand's 67 Territorial Authorities (district and city councils) are associated with a BCA. Consentium, an independent division of Kāinga Ora, is also a BCA.

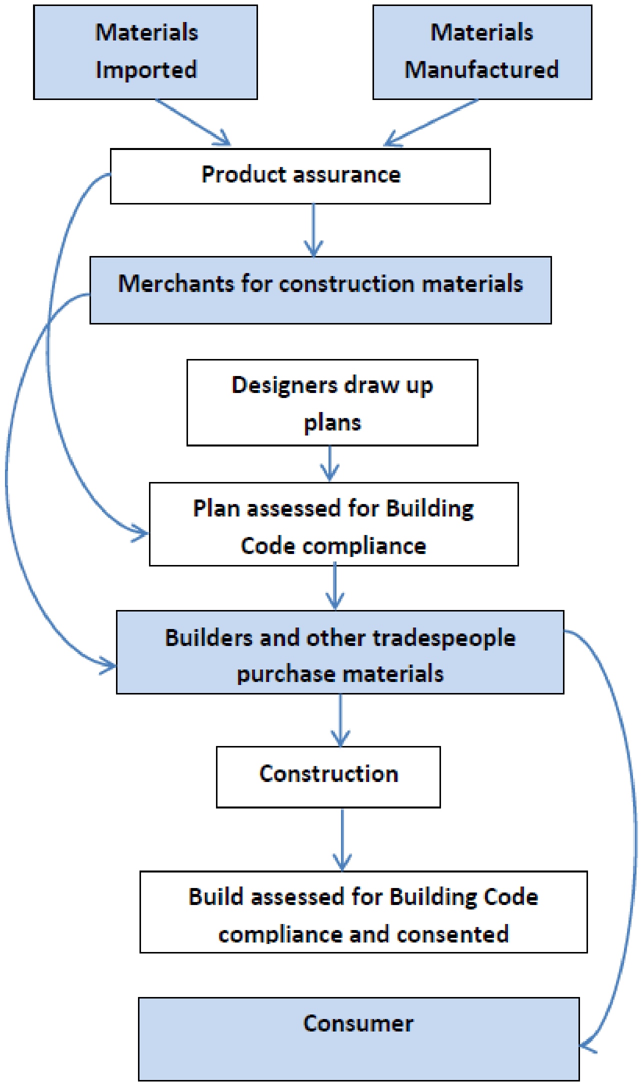
45.3 Industry bodies provide representation, regulation, and research functions for the benefit of industry participants. There is a wide range of construction industry bodies that includes the NZ Building Industry Federation, the NZ Construction Industry Council, the NZ Green Building Council, and a large number of trade-related associations and organisations.

45.4 There are also research and certification bodies, including BRANZ and other CodeMark certifiers, among others. These research and certification processes can have substantial influence over which new products make it to market.

[20] Building Performance "Roles and responsibilities of councils"; accessible at: https://www.building.govt.nz/building-officials/roles-and-responsibilities-of-councils/.

46. Figure 2 below presents a high-level summary of the construction process.

Figure 2: High level summary of the construction process[21]



[21] Source: MBIE (2013) Residential Construction Sector Market Study Options Paper.

47. We will consider how the supply chain functions, how wider participants interact and how decisions for product selection currently tend to be made. This will involve engaging with a range of industry participants and stakeholders.

Questions on the supply chain for residential building supplies in New Zealand

Q4 How does our high-level summary of the supply chain fit with your understanding?

a. Are there any other key steps in the supply chain we should consider? If so, please explain how these steps fit into the supply chain.

b. Are there building supplies relevant to this study that have different supply chain structures? If so, please describe these building supplies and how the supply chain differs?

Q5 How does our characterisation of the key participants and the other key stakeholders in the residential building materials supply chain fit with your understanding?

a. Are there any other key participants or stakeholders that play a major role in the industry? If so, please explain the role of these participants or stakeholders.

Q6 Is the structure of the supply chain changing or evolving? If so, please explain how and over what time horizon this is likely to occur?

The wide range of products used in residential building construction

48. Many different products are used to build residential housing. For example, MBIE's 2013 issues paper on the same topic notes that there are over 45,000 product lines used in the industry.[22] It is not feasible for this study to consider all of these product lines.

49. The terms of reference require us to consider any factors that may affect competition for the supply or acquisition of key building supplies used to build the major components of residential buildings. For the purposes of this study, major components of residential buildings are the foundation, flooring, roof, walls (structural and non-structural, interior and exterior) and insulation.

50. Our preliminary view is that the terms of reference are neutral as to the style of the residential building structure and define the scope of study by reference to the "building envelope".

51. At this stage, we consider:

[22] Ibid.

51.1 windows to be within the scope of the major components of residential buildings, as an integral part of interior and exterior walls; and

51.2 plumbing and electrical supplies to be outside the scope of this study.

52. The inclusion of plumbing and electrical supplies would add significantly to the scope of this study given the range of products this would include, coupled with the overlay of different regulatory systems. Our understanding is that these products were not intended to be included within the scope of this study.

53. Table 1 below provides a (non-exhaustive) list of building supplies used in the major components of residential buildings, based on the information we have reviewed to date. We consider the materials in this table are likely to be within the scope of this study.

Table 1: Preliminary list of building supplies in scope

Major components of residential buildings	Building supplies in major components
Foundation	Concrete, timber, steel joists
Flooring	Concrete, particleboard, strandboard
Roof	Steel roofing, other sheet metal roofing, metal and concrete tiles, shingle and membrane roofing
Walls (structural/framing)	Timber framing, laminated veneer lumber (LVL), steel framing, concrete masonry, polyblock, rammed earth framing
Walls (exterior/cladding)	Weatherboard (timber/fibre-cement/uPVC), clay and concrete bricks, metal cladding, non-weatherboard fibre-cement, plywood, stucco, sheet steel
Walls (interior)	Plasterboard, wet lining
Walls (interior/exterior)	Window/door framing (aluminium, timber, composite, uPVC, fibreglass, and steel), glazing, doors
Insulation	Walls and ceiling: Glass wool and polyester Floor: Underslab, polystyrene, glass wool, polyester, perimeter edge, under footing

Sources: Commerce Commission review of BRANZ (2020), Trends in materials used in new houses; Deloitte Access Economics (2018), Cost of residential housing development; BRANZ (2008), New house price modelling.

54. In considering the factors that may affect competition for the supply or acquisition of key building supplies, we may find it useful to narrow our focus to a smaller selection of supplies that appear to be particularly affected by one or more factors. When considering other factors, such as the role the regulatory and standards systems play, we may choose to widen our focus to look across a broader range of building supplies.

55. Possible criteria we may consider when identifying the key building supplies to focus on include:

    55.1 whether the cost of the building supply comprises a significant proportion of the overall cost of building supplies used. We may choose to focus on key materials that represent a significant proportion of the overall cost;

    55.2 the number of manufacturers or suppliers who supply the building supply. We may choose to focus on building supplies that are only available from a limited number of manufacturers or suppliers, or predominantly through one or other of the two major vertically integrated suppliers;

    55.3 the extent to which the building supply is able to be substituted for alternatives, including new or innovative building supplies. We may choose to focus on building supplies for which there are few existing alternatives and/or for which the entry or expansion of new or innovative materials could have an impact on competition for the supply or acquisition of existing materials;

    55.4 whether the building supply itself is new or innovative, or may be anticipated to become increasingly prevalent (eg, due to the changing regulatory framework); and

    55.5 the views of industry participants and other stakeholders on what constitutes the key building supplies used to build the major components of residential buildings.

56. When considering the extent to which each material comprises a significant proportion of the overall cost of building supplies, we may consider different forms of residential housing.

57. Residential housing in New Zealand can take many forms but can be broadly categorised into stand-alone houses, townhouses, and apartments. Between these different types there will be points of differentiation that might affect the relevant set of materials and their overall cost contributions.[23]

58. Our current understanding is that many of the materials listed in Table 1 above are common in a range of housing types, and we do not expect to need to assess competition for key building supplies separately for different housing types.

59. However, to the extent we narrow our focus to a smaller selection of materials, we will consider the extent to which the narrower focus covers the different forms of residential housing. This will ensure our selection captures factors that may affect competition to supply or acquire key building supplies used in a particular type of

[23] For example, we understand construction of high-rise apartments is generally a more specialised process than the construction of low-rise apartments and can involve different materials. For example, timber framing is generally only used in buildings of three storeys or less. MBIE "Using NZS 3604 Timber-framed buildings" (6 July 2021), accessible at: https://www.building.govt.nz/building-code-compliance/how-the-building-code-works/using-nzs-3604-timber-framed-buildings/. (Viewed 9 December 2021)

residential building. We would also look to consider any associated trends (eg, increasing intensification) to ensure this study takes a forward-looking approach.

Questions of the scope of "key building supplies" to be considered in the study

Q7 Do you agree or disagree with our preliminary view on the "key building supplies" in scope for this study, as described in paragraphs 49-52 and Table 1? Please explain your reasoning.

Q8 If we focus on a narrower selection of building supplies to assess certain issues, are the factors set out in paragraph 55.1-55.5 appropriate to guide our focus? Are there any other factors we should also consider?

Q9 Which key building supplies do you think should be assessed in greater detail, or otherwise prioritised? Please explain your reasoning.

Q10 How will key building supplies evolve in the future? Will different materials become more important?

Some of the unique characteristics of building in New Zealand

60. From preliminary discussions with some industry stakeholders, we understand there are some unique or unusual characteristics that set residential building in New Zealand apart when compared with other countries.

61. These characteristics may have some important implications for the nature of competition in the industry. For example, if the characteristics of residential building in New Zealand are different from other parts of the world, it may be harder for international suppliers to export into New Zealand and meet the demands or regulations of the local market.

62. We understand that some of the unique characteristics of building in New Zealand may be:

62.1 performance and durability requirements, including to mitigate the risks of earthquakes and wind;[24]

62.2 the traditionally more bespoke nature of housing stock, with the example given of windows in New Zealand commonly made-to-measure with fewer standardised sizes;

62.3 plasterboard used to support the structural integrity of buildings (ie, providing bracing functionality); and[25]

[24] See for example, https://www.building.govt.nz/managing-buildings/building-safety-in-earthquakes/.

[25] Deloitte Access Economics, above n 17.

62.4 engineers or architects may be specifying brands of certain building supplies in plans presented for building consent.[26]

63. As part of this study, we will consider the characteristics of building in New Zealand, how these may evolve going forwards and the implications these may have on competition for key building supplies.

Questions on the unique characteristics of building in New Zealand

Q11 Are the characteristics set out above an accurate reflection of residential building in New Zealand? Please explain your reasoning.

Q12 Are there any other characteristics of residential building in New Zealand which are important for us to understand?

The acute demand and supply chain pressures the industry currently faces

64. The COVID-19 pandemic has placed pressures on the residential building supplies industry, among others. As well as the impact of lockdown restrictions in New Zealand, there has been major disruption to global supply chains.

65. A survey conducted by the Construction Sector Accord identified the top two key issues facing the wider construction sector (including residential) in mid-2021 as being:[27]

65.1 increases in the price of materials and supplies; and

65.2 shortages of materials and supplies, particularly structural and non-structural wood products.

66. The survey also highlighted that although the COVID-19 pandemic was the main driver of these issues, a large proportion of respondents also viewed it as exacerbating existing issues. Worldwide shipping was viewed as being the primary cause of the issues, followed by delays in manufacturing.

67. The international supply chain and shipping is outside the scope of this study. We will, however, be mindful of the pressures the industry is under as we carry out our engagement with the sector.

68. We will also consider the relationship between supply chain resilience and competition as we explore the extent to which competition is working well in the industry and how it may evolve in the future.

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26 MBIE Options Paper, above n 10.

27 Construction Sector Accord "Construction Sector Accord supply chain research issued" (21 September 2021), accessible at: https://www.constructionaccord.nz/news/news-stories/construction-sector-accord-supply-chain-research-issued/.

69. As well as the short-term impacts from COVID-19 pandemic and international supply chain disruptions, rising land price inflation and housing supply shortages are also increasing the importance of efficiency with an increasing need for residential housing to be built at scale.

70. We note that increased use of technologies such as prefabricated housing and panellisation may provide pathways to easing some of these pressures by facilitating efficient, large-scale manufacturing.

71. Prefabrication (which involves the offsite manufacturing of entire building structures) is commonplace in overseas residential construction but is still relatively novel in New Zealand.[28] Panellisation involves the offsite construction of components, such as structural insulated panels for wall systems.

72. Prefabrication and panellisation may use building supplies in different ways and could encompass multiple elements of the major components of residential building. We will consider whether such manufacturing approaches face impediments to competition. Paragraphs 119 -138 discuss the impediments to the entry or expansion of new or innovative building supplies, such as 'green' building supplies or novel prefabricated products.

73. Such moves to alternative approaches may also be driven by regulatory reform and the move to find 'greener solutions'. We discuss these trends in the following two sub-sections.

Questions on the demand and supply chain pressures on residential construction

Q13 Does our summary of the external pressures facing the residential construction industry accurately reflect the current situation? Please explain why/why not.

Q14 To what extent are these external factors temporary or likely to continue in the long term?

Q15 Would an increased use of technology, such as prefabricated housing, help to address some of the longer term pressures facing the industry? Please explain why/why not.

Q16 Please describe any other examples of innovative technologies or approaches that could increase efficiency in the sector over the longer term.

Q17 Please describe any other major external factors that are currently impacting (or have recently impacted) the New Zealand residential building industry that we should consider in this study and the time horizon over which they will impact the industry.

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28 "In some countries, nearly 80 per cent of newly built homes are prefabricated offsite, in New Zealand it's about 10 per cent." Hon Jenny Salesa "More prefab homes to be built as red tape cut" (media release, 11 October 2019). Accessible at: https://www.beehive.govt.nz/release/more-prefab-homes-be-built-red-tape-cut.

The evolving regulatory framework

74. The regulatory framework informs and adapts to emerging trends and developments in the residential construction sector. For example:

74.1 MBIE reviews and updates the Building Code annually to ensure it keeps pace with modern construction methods.[29]

74.2 MBIE is also currently progressing the building law reform programme. The Building (Building Products and Methods, Modular Components, and Other Matters) Amendment Act 2021 aims to improve the efficiency, quality, and accountability of the construction sector (including through allowing for more streamlined consenting of prefabricated housing).[30] Key changes established by the Amendment Act include:[31]

74.2.1 mandating minimum information requirements for building products, to enable more efficient BCA decision-making;[32]

74.2.2 establishing a streamlined framework for consenting pre-fabricated structures and structures built offsite; and

74.2.3 strengthening the CodeMark framework to improve trust and confidence in the scheme.

74.3 The Building for Climate Change Programme has developed adaptation and emissions mitigation frameworks to confront the challenges posed by climate change and to help ensure New Zealand reaches its goal of net zero carbon by 2050.[33]

74.4 Proposed amendments to the Resource Management Act 1991 (RMA) may facilitate higher-density residential housing, which is already becoming more common in New Zealand (partially in response to rising land prices and our growing urban population).[34]

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29 Building Performance “Maintaining the Building Code”, accessible at: https://www.building.govt.nz/building-code-compliance/annual-building-code-updates/.

30 Building Performance “Building law reform programme”, accessible at: https://www.building.govt.nz/getting-started/building-law-reforms/.

31 Accessible here: https://www.legislation.govt.nz/act/public/2021/0021/latest/LMS264715.html.

32 The information required will be set by regulations which are still to be developed.

33 Building Performance “Building for climate change”, accessible at: https://www.building.govt.nz/getting-started/building-for-climate-change/.

34 Ministry for the Environment “Proposed RMA amendments to enable housing intensification” (media release, 27 October 2021). Accessible at: https://environment.govt.nz/what-government-is-doing/areas-of-work/urban-and-infrastructure/proposed-rma-amendments-to-enable-housing-intensification/.

75. Understanding how these regulatory changes (and the associated emerging trends) affect the demand for certain types of building supplies will be important in ensuring this study takes a forward-looking approach. We discuss the role of regulation and its potential impact on competition in paragraphs 123 -132.

Questions on the evolving regulatory framework around residential construction

Q18 How might the regulatory changes described in paragraphs 74 and 75 affect the demand for or supply of certain types of residential building supplies?

Q19 Please describe any other major recent or ongoing regulatory changes that might affect demand for certain types of residential building supplies.

Q20 Does the regulatory environment pose challenges to the introduction of prefabricated products? If so, please explain where you see the issues and whether these will be addressed by the latest regulatory reforms.

Climate change and implications for the future of building supplies

76. Government policy to address climate change will make it increasingly important for residential housing (building structures and materials, and the construction process itself) to be sustainable and to limit carbon emissions, as part of reducing the emissions contribution of the construction industry as a whole.

77. It is also becoming more important for residential housing to be resilient to withstand the effects of the changing climate. This is likely to include higher temperatures, rising sea levels, more frequent extreme weather events, and changes in rainfall patterns.[35]

78. The introduction of new and innovative 'green' building supplies may be a key pathway to reducing the carbon footprint of residential housing.

79. The terms of reference direct us to consider any impediments to the entry or expansion of new or innovative building supplies. This could include:

79.1 relatively new 'green' building supplies looking to gain acceptance; and

79.2 prefabricated products and panellisation systems.

80. We discuss this further in paragraphs 119 -138.

81. Ensuring competition is working well for existing materials may also have important implications for the move to more sustainable and environmentally-friendly buildings. For example, ensuring that the market for insulation is working well will enable more homes to be built in an energy efficient way.

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35 MBIE 2021 Annual Report, above n 11.

82. Building for climate change is likely to drive significant innovation over the next 10 years. We are interested in understanding the different types of innovations in the industry and how the regulatory and standards systems may accommodate them.

Questions on impact of climate change for building supplies

Q21 What are the most important 'green' building supplies for us to focus on? Why are these important?

Q22 Please describe any other ways in which building for climate change might drive change and innovation in the residential construction sector.

Potential issues we may consider during the study

83. In considering the factors that may affect competition for the supply or acquisition of key building supplies, we have identified a range of potential competition issues that we may explore during this study. This section seeks feedback on those issues.

84. We have grouped our discussion of factors that may affect competition under three headings based on the terms of reference:

66.1 the industry structure for key building supplies;

66.2 the nature of competition for key building supplies; and

66.3 impediments to entry or expansion of building supplies, including of new or innovative building supplies, 'green' building supplies and novel prefabricated products.

85. The potential issues identified under each of these headings do not pre-suppose that there are competition problems in the industry. We are seeking feedback from stakeholders and any interested parties on the issues we have identified at this point in time, to help us decide where to focus our efforts during the study.

86. As part of our assessment of the factors affecting competition, we will also consider competitive outcomes in the sector. This may include assessing:

86.1 prices, choice, quality and innovation in the industry;

86.2 the margins earned by key suppliers; and

86.3 whether there are other outcomes that are not consistent with those expected in a workably competitive market.[36]

[36] The High Court has noted the following points regarding workable competition: "A workably competitive market is one that provides outcomes that are reasonably close to those found in strongly competitive markets… The degree of rivalry is critical. In a workably competitive market no firm has significant market

87. At this stage we do not think it is necessary for this study to attempt to find conclusively whether profits and/or prices are high in order to find that competition in a market is not working as effectively as it could.

88. The subsections below explain each of the potential issues that we currently propose to explore and set out questions that we invite views on. We also welcome views on whether there are other issues that we should consider during the study, having regard to the terms of reference.

Questions on our high-level approach for our market study into residential building supplies

Q23 Do you have any comments on our proposed high-level approach to the study as discussed in paragraphs 83 to 87 above?

Q24 Would international comparisons of key building supplies prices provide insights into the level of competition in the industry? Why/Why not?

Q25 How should we assess the levels of innovation in the industry? Is there a way to measure this or benchmark internationally?

Q26 Would assessing the margins of the manufacturers and/or merchant sales of key building supplies provide insights into the level of competition? Why/Why not?

Q27 Are there other assessments that would provide better insights?

The industry structure for key building supplies

89. Industry structure was one of three areas highlighted in the terms of reference for this study for consideration.[37]

90. The structure of the building supplies industry can have important implications for the way in which competition takes place. When considering industry structure we propose to explore how competition is impacted by the number of, and types of, suppliers in the market as well as the extent of common ownership across different levels of the supply chain.

91. This section provides further detail on our thinking on industry structure, we consider this under the headings of two potential issues:

power and consequently prices are not too much or for too long significantly above costs… In our view, what matters is that workably competitive markets have a tendency towards generating certain outcomes". *Wellington International Airport Ltd and Others v Commerce Commission* [2013] NZHC 3289 at [14]-[15] and [18]. See also more generally the discussion at [6] - [28].

37 Gazette Notice, above n 6.

91.1 **Concentration** – whether there is a limited number of providers of some key building supplies and whether this appears to be resulting in weak competition and poor outcomes for consumers.

91.2 **Vertical integration** – whether the degree of vertical integration in the supply chain for key building supplies poses a barrier to competition from independent manufacturers/importers or to independent merchants.

Concentration

92. An industry or market is considered to be more concentrated if relatively few suppliers control a large share of supply. The most extreme example of concentration is where a single supplier controls all the supply (ie, a monopoly).

93. The supply in New Zealand of certain building materials does appear to be highly concentrated. The Cabinet paper supporting the terms of reference for this study notes one company (Fletcher Building) as having a market share of 94% in the supply of plasterboard and, between them, two companies (Holcim and Fletcher Building) as having a combined market share of 85% in the supply of concrete.[38] The Cabinet paper also notes there are only five major building merchants.

94. High concentration is not necessarily a bad thing. It can be the outcome of suppliers gaining market share by offering the best price or quality product and competing hard to maintain that position against the threat of new entry.

95. However, high concentration can also indicate a weakening in the competitive process, particularly when maintained over a long period. It can be a result of other suppliers being prevented from competing effectively due to high barriers to entry or expansion in the market. This can lead to some suppliers having a high degree of market power and the ability to set higher prices or to reduce quality.

96. It is also possible that market power is constrained by other factors. For example, to the extent that prices are determined by negotiations between buyers and sellers, countervailing buyer power could act as a constraint on suppliers' market power.[39]

97. We propose to consider the degree of concentration in key building supplies and the drivers of this, including exploring:

97.1 the extent of economies of scale in the supply chain for key building supplies;

97.2 the extent to which different building supplies are substitutable;

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38 Cabinet paper 2021, above n 7, at page 3.

39 A business has substantial market power when its actions are not constrained by competition. For example, a business with substantial market power can profitably hold prices above competitive levels for a sustained period of time. Such a price rise will only be profitable if the business does not face effective competition from rivals or entrants in the same market. When assessing whether a business has substantial market power, we consider how much existing and potential competition the business faces. We also look at other factors such as whether buyers can exercise countervailing power (ie, special characteristics that allow them to substantially influence the price charged by suppliers).

97.3 the barriers to importing building supplies into New Zealand;

97.4 whether there are regional differences in concentration within New Zealand;

97.5 how concentration is changing over time; and

97.6 whether high concentration is leading to poor outcomes for consumers.

Questions on concentration

Q28 On what geographic basis (eg, local, regional, national) should we assess the concentration of key building supplies. Please explain your view.

Q29 Are there any key building supplies which stand out as having a limited choice of suppliers? If so, please explain which building supplies.

Q30 What are the barriers to importers of key building supplies competing effectively with domestic manufacturers?

Q31 Are there building supplies you are aware of that are not available in New Zealand, but you think would benefit New Zealanders? Please describe these supplies and benefits.

Q32 How do economies of scale in the supply chain for key building supplies impact the number of suppliers?

Q33 What are the main barriers to new providers of key building supplies establishing domestic manufacturing in New Zealand?

Q34 Are customers, (for example, merchants when purchasing from wholesalers, or builders when purchasing from merchants) able to constrain their suppliers due to their own size or negotiating position? Please explain why/why not?

Vertical integration

98. As discussed above, the terms of reference direct us to consider the industry structure for key building supplies, and the Cabinet paper supporting the terms of reference points to vertical integration in the supply chain.

99. We are aware that:

99.1 Fletcher Building manufactures products including concrete and plasterboard;[40] it also operates PlaceMakers, a building supplies merchant;[41] and is also active in residential construction and development.[42]

99.2 Carter Holt Harvey manufacturers products including structural timber,[43] and it also operates Carters, a building supplies merchant.[44]

100. There are possible advantages and disadvantages of vertical integration. Vertical integration could be generating significant efficiencies in managing the supply chain, and therefore have a positive or benign effect on competition. However, vertical integration can also make it hard for independent (non-vertically integrated) firms at different levels of the supply chain to enter and compete, because they may not be readily able to access competitive distribution services or secure the supply of key inputs.

101. A high level of vertical integration may leave little scope for independent firms to enter at sufficient scale to compete effectively.

102. We propose to consider the potential impacts vertical integration may be having on competition for key building supplies and the extent to which non-vertically integrated suppliers and/or merchants are able to compete effectively. As part of this assessment, we consider it may be appropriate to explore:

102.1 the views from industry participants and other stakeholders on the benefits of vertical integration in key building supplies and the efficiencies this brings;

102.2 the extent to which the sale or acquisition of building supplies for non-vertically integrated players is reliant on the provision of products or services by rivals;

102.3 how the profit margins of key building supplies vary throughout the supply chain;

102.4 the views from industry participants and other stakeholders on the impact of vertical integration on competition; and

40 Fletcher Building "Building Products", accessible at: https://fletcherbuilding.com/our-business/building-products/.

41 Fletcher Building "Distribution", accessible at: https://fletcherbuilding.com/our-business/distribution/.

42 Fletcher Building "Residential and Development", accessible at: https://fletcherbuilding.com/our-business/residential-and-development/.

43 Carter Holt Harvey homepage, accessible at: https://chhwoodproducts.co.nz/.

44 Carters homepage, accessible at: https://www.carters.co.nz/.

102.5 the extent to which vertical integration may be acting as a barrier to entry or expansion for key building supplies.

Questions on vertical integration

Q35 Does vertical integration act as a barrier to entry/expansion for independent rivals? Does this differ for different building supplies? Please explain your view.

Q36 Is being vertically integrated necessary to compete effectively in this sector? Please explain your view.

Q37 What are the benefits in this industry to being vertically integrated? Do consumers benefit from this?

Q38 Are there any other factors we should be aware of in considering the vertical integration of key building supplies?

The nature of competition for key building supplies

103. The nature of competition (that is, the way firms interact with rivals, their customers and suppliers) has important implications for the competitive process.

104. The intensity of the competitive process for the supply or acquisition of key building supplies and, ultimately, competitive outcomes could be affected by a range of conduct. The potential issues we have currently identified as potentially appropriate to explore further can be grouped as follows:

104.1 **vertical arrangements** - are there contractual arrangements entered into between participants at different levels of the supply chain which dampen competition between rivals or prevent the entry or expansion of new market participants?

104.2 **accommodating behaviour** - is there conduct that suggests market participants may be accommodating one another in a way that dampens competition between rivals?

Vertical arrangements

105. The terms of reference direct us to consider the nature of competition for key building supplies, including any industry pricing practices or acquisition requirements that impact on competition.

106. The Cabinet paper supporting the terms of reference posits that:[45]

> Pricing of building supplies is not transparent, with the widespread use of rebates and loyalty schemes shaping the market. A Residential Construction Market Study

[45] Cabinet paper 2021, above n 7.

conducted by MBIE in 2013/14 highlighted the potential negative effects of rebates and loyalty schemes on the relationship between suppliers and merchants, merchants and builders, builders and customers.

107. We propose to consider the industry pricing practices and acquisition requirements between market participants at different levels of the supply chain. For example, arrangements by suppliers to provide rebates to purchasers if a certain level of supply is purchased. We refer to these industry practices as vertical arrangements. We understand that vertical arrangements for key building supplies may feature a range of pricing or other practices, including:

107.1 rebates;

107.2 exclusivity agreements; and

107.3 tying (ie, refusing to supply one product without the purchase of another) or bundling (ie, selling multiple products together at a discount).

108. In particular, we understand that rebates may be a common feature in the markets for key building supplies. They may include:

108.1 builders receiving rebates, other loyalty payments or non-monetary incentives for purchasing quantities of key building supplies from a particular merchant; or

108.2 merchants receiving rebates, other loyalty payments or non-monetary incentives for stocking particular manufacturers' products.

109. We also understand that some key building supplies may be bundled or tied together as part of a system of products, and that product warranties may be conditional on the use of all components comprising the system.

110. Vertical arrangements such as rebates, exclusivity arrangements, bundling and tying can have beneficial effects. They can improve the coordination of activities at different stages of the supply chain and deliver savings in transaction and inventory costs.

111. However, despite their potential to enhance efficiency and consumer welfare, these types of vertical arrangements can have a detrimental effect on competition by preventing potential rivals' access to inputs or customers, or by increasing rivals' costs. This can ultimately lead to weaker competition and worse outcomes, such as higher prices or lower quality, for consumers.

112. The extent to which any benefits from rebates and loyalty schemes are passed on to consumers will also depend on a range of factors, including:

112.1 the structure of the rebate, with lump sum payments potentially less likely to be passed through to consumers than wholesale price discounting;[46]

112.2 the extent to which consumers have full information (ie, whether rebates or incentive arrangements are transparent). For example, if consumers are aware of the benefits builders may be receiving from choosing a particular type of branded product, they can take this into account when selecting their builder and considering advice from builders on material selection; and

112.3 the extent to which the decision-maker's interests align with that of the consumer. For example, if builders are incentivised to minimise the cost of building supplies in order to win customers, they may be more likely to pass on any rebates on received.

113. We propose to consider the role of vertical arrangements in the supply of key building supplies, and the extent to which these arrangements may be impacting competition at any level in the supply chain. We also propose to consider whether these arrangements are impacting consumers.

Questions on vertical arrangements

Q39 What forms do supplier rebates and loyalty payments typically take in this industry? (eg, monetary, non-monetary, lump sum etc.) Does this vary by type of building supply? If so, please explain how.

Q40 Do rebates / loyalty payments usually relate to one product or category of product, or are they often applied across multiple products or product categories?

Q41 Do rebates / loyalty payments inform or restrict a merchant's or builder's decision about which product(s) to acquire? If so, how significant is this consideration?

Q42 Is tying of products or product "systems" a prevalent practice? What levels of the supply chain are characterised by tying arrangements?

Q43 Are exclusivity agreements prevalent? What levels of the supply chain are characterised by exclusivity agreements?

Q44 Do the benefits of rebates and pricing pass through to end-consumers? Why/Why not?

Q45 Are there any other factors we should be aware of in considering the vertical arrangements of key building supplies?

46 Commerce Commission *Investigation into Winstone Wallboards Limited* (22 December 2014) at 18, fn 52. Accessible at https://comcom.govt.nz/__data/assets/pdf_file/0028/94393/Winstone-Wallboards-Limited-Investigation-closure-report-22-December-2014.pdf.

Accommodating behaviour

114. Accommodating behaviour (also known as coordination) involves firms recognising that they can all reach a more profitable outcome if they act to limit their rivalry when taking each other's actions into account (such as by following a rival's price increases). If firms are collectively exercising market power through accommodating behaviour, this could lead to higher prices, or reduced choice or quality.[47]

115. Such conduct does not necessarily require an explicit agreement or express coordinated behaviour between competing firms, which may breach cartel laws.[48] It can develop instead by firms repeatedly observing each other's actions and reactions so that they each learn how the other will respond.

116. Accommodating behaviour is possible in concentrated markets. However, this is not inevitable – several conditions must hold for it to occur, including:[49]

    116.1 firms must be able to reach similar views on how they can increase industry profits;

    116.2 firms must be able to detect and punish cheating, so that the potential individual profit gains from a firm's cheating are outweighed by the costs of punishment; and

    116.3 the accommodating behaviour must not be undermined by threat of entry or expansion by other firms, or the ability of consumers to disrupt coordination.

117. We do not currently have any views as to whether accommodating behaviour may be occurring for key building supplies, but we recognise that, due to the concentration apparent in some markets for key building supplies, this could be a potential issue.

118. We intend to explore the extent to which the required conditions for accommodating behaviour are apparent in this industry.

Questions on accommodating behaviour

Q46 Is accommodating behaviour likely to be an issue in this industry? Please explain why/why not.

Q47 How transparent is pricing for key building supplies?

Q48 Are there any other factors we should be aware of in considering accommodating behaviour in building supplies?

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47 There are some circumstances where collaboration can be a valid response to market failure, for example, to stabilise supply and protect vulnerable consumers during the COVID-19 pandemic.

48 Section 30 of the Act.

49 Commerce Commission *Market study into the retail fuel sector: Final report* (5 December 2019) at [7.78].

Impediments to entry or expansion of building supplies, including new or innovative building supplies, 'green' building supplies and novel prefabricated products

119. The ability of rivals to enter markets and expand their sales is a vital part of the competitive process. Even in a market where there are relatively few competitors, the threat of entry and expansion or development of new innovative products can constrain the behaviour of existing firms.

120. Impediments to entry and expansion can limit the number of competing suppliers. The expected profitability of entry and expansion depends on the costs and risks associated with entry and expansion. If entry and expansion are difficult, less competitive offerings (with higher prices, lower quality and resulting higher profits) are more likely to persist in the longer term, to the detriment of New Zealand consumers.

121. The terms of reference direct us to consider the impediments to the entry or expansion of new or innovative building supplies, such as 'green' building supplies or novel prefabricated products. The Cabinet paper supporting the terms of reference refers to difficulties for new building supplies to enter the New Zealand market, including anecdotal evidence of issues in the building consent process.[50]

122. The potential issues relating to market structure and vertical arrangements discussed above all have the potential to restrict the ability of new firms to enter the relevant markets or expand their existing offerings. In this section, however, we consider the potential impact of regulation and behavioural biases as possible impediments to entry, expansion, and/or innovation, ie, as potential barriers to entry.

Regulatory and standards systems

123. Ensuring buildings are structurally sound and safe to live in is self-evidently important. To ensure buildings are of sufficient standard, the regulation of building materials, standard setting and specifications play a substantial role in the industry.

124. There is a range of regulatory bodies and standard setters involved in residential building construction, including MBIE, BCAs, BRANZ and other CodeMark certifying bodies.

    124.1 MBIE is the over-arching regulator of New Zealand's building system. Among other things, MBIE is responsible for building law reform, and its "Building System Regulatory Strategy – Building for the Future" plan sets out a vision for the future of building regulation. MBIE is also responsible for updating the Building Code and building standards. The Government's building and construction regulator, Building Performance, is leading work to modernise the Building Code.

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50 Cabinet paper 2021, above n 7.

124.2 BCA's roles and responsibilities are defined by the Building Act 2004. Among other things, BCAs issue building consents and Building Code compliance certificates, and carry out follow up inspections for new buildings.

124.3 BRANZ is an independent research and testing organisation involved in understanding the design and construction of the built environment in New Zealand. Its work feeds into the Building Code and Standards.

124.4 CodeMark is a voluntary product certification scheme that enables a manufacturer to demonstrate that its product(s) comply with the Building Code. A product that has CodeMark certification must be accepted by a BCA in the consenting process.

125. The functions of MBIE, BCAs, CodeMark and BRANZ are all important to the quality assurance of New Zealand's residential buildings.

126. At the same time, rules and regulations impose a compliance burden on businesses, and this has the potential to disproportionately impact smaller or emerging businesses. Where this is the case, the regulatory environment can make it harder for small businesses or prospective new entrants to compete in, or even enter, a market. Liability and risk are likely to be important considerations and potential drivers of behaviour.

127. We are aware, for example, of large international building supplies manufacturers that have, in recent years, entered the New Zealand market intending to remain on a long-term basis but have exited again in the relative short-term. While the exit of those businesses may have occurred for many reasons, we are interested in understanding whether New Zealand's regulatory and compliance environment imposes a burden on businesses that affects their ability to enter, expand or compete in the relevant markets.

128. We are also interested in understanding the experiences of manufacturers or importers attempting to bring new and innovative products to market in New Zealand, and whether the regulatory and standards systems facilitate or hinder those efforts, and in what ways.

129. Rules and regulations relating to risk mitigation can also impact on the way that businesses design their operations, and the way businesses, such as builders or manufacturers and consumers interact with one another.

130. We propose to consider the role of the regulatory framework in this industry, including understanding how the regulatory and standards systems and building consent processes work in practice and whether, and if so how, this impacts on the supply of new or innovative building supplies.

131. Our preliminary view is that we should consider whether the regulatory and standards systems may pose potential impediments to competition for key building supplies. As part of this assessment, we consider it may be appropriate to explore whether the regulatory and standards systems:

131.1 pose barriers to prospective international or domestic entrants to New Zealand markets;

131.2 create a disproportionate compliance burden for emerging manufacturers of innovative products, including ‘green’ building supplies or novel prefabricated products;

131.3 incentivise vertical integration or vertical supply arrangements, potentially to mitigate liability and compliance risks; and

131.4 impede competition in the markets in any other way.

132. In addition, we may seek to understand at which levels of the supply chain any potential impediments impose a constraint on competition. For example, we may explore whether the regulations impose constraints on competition at the manufacturer level, which flow downstream, or at the downstream architectural design / build level, which may have upstream effects.

Questions on regulatory and standards systems

Q49 Do the regulatory and standards systems (eg, product accreditation framework, building code and standards or consent process) make it easy or difficult for new and innovative building supplies to enter the New Zealand market and establish a presence? Please explain any difficulties posed and your view on whether it would be beneficial to make it easier for new suppliers to enter the New Zealand market.

Q50 What impact does the current regulatory environment have in encouraging or discouraging a move to ‘green’ building supplies?

Q51 Does the current regulatory regime favour incumbent suppliers over new entrants? If so, please explain how.

Q52 Does the current regulatory regime encourage vertical integration (including, for example, in-house product compliance) or vertical arrangements in the sector? If so, please explain how.

Q53 Does the current regulatory regime encourage the offer of ‘systems’ of products? If so, please explain how.

Q54 Are there any other factors we should be aware of in considering the regulatory and standards systems for building supplies?

Behavioural impediments

133. It appears that a number of different parties may be involved when it comes to selecting the building supplies for any residential building project.

134. The parties involved might include any one or more of: the architect or engineer, the quantity surveyor, the builder or the client. Each of these market participants will likely have their own incentives, preferences and potential biases. These participants' experiences in using certain products and the building consent and Building Code compliance certification processes may influence such preferences.

135. Making decisions on the most appropriate building supply to use can be complicated and involve choosing from a range of options. If the information needed to make decisions is not available or is costly to assess, there is a risk that decisions will not be made in the consumer's best interests.

136. It is also possible that the incentives operating in this industry may skew product choices towards selections based on familiarity and whether products are 'tried and tested'. This could be, for example, in response to the cost of searching for information on alternatives, in anticipation of the decisions of building inspectors or due to concerns over liability if things go wrong.

137. If decision-makers are less willing to try new products or suppliers, it may prevent alternatives from gaining traction and competing effectively. This may be the case even when these alternatives are meeting the required standards and potentially offering a better price or quality product. Warranties or other guarantees may play a part in reassuring decision-makers, however there may be uncertainty as to the extent these will be valid.

138. We propose to consider the way decisions on selecting building supplies are being made, including by exploring:

138.1 the role each party plays in making decisions on building supplies;

138.2 how consumer preferences impact the choice of building supplies;

138.3 the information available to decision-makers and ability to use that information;

138.4 the role of risk aversion in decision-making including the impact of warranties and liability on decision making; and

138.5 the extent to which the incentives of decision-makers are aligned with interests of consumers.

Questions on behavioural impediments

Q55 Who are the key decision-makers for key building supplies?

Q56 How do decision-makers choose the most appropriate building supplies to use?

a. Do decision-makers default to choosing building supplies which have been used in the past? If so, please explain why.

b. Do decision-makers on key building supplies have full information available to them to make informed decisions? How costly is it to obtain this information?

c. What role do warranties or other guarantees have in the decision to choose the key building supplies?

Q57 Do the incentives of the decision-makers on key building supplies align with the interests of consumers?

Q58 Are there any other factors we should be aware of in considering decision-makers' behaviour in respect of building supplies?

Prioritisation

139. The list of issues we are seeking views on is based on our preliminary assessment of the terms of reference for the study issued by the Minister and the issued outlined here are not intended to be exhaustive. Following responses on this paper we may focus on a confined number of these issues and/or other issues not raised in this paper.

140. We invite you to provide views on which potential issues are the most significant issues worth considering and to raise any other issues and information that you consider to be relevant to the study.

Questions on other issues and prioritisation

Q59 Are there any other issues not raised in this paper that could impact competition in the key building supplies?

Q60 Which potential issues do you think should be the priority issues to focus on? Please detail the reasons why.