

## To Whom It May Concern

### **Market Study into Residential Building Supplies**

#### **Introduction**

New Zealand needs a broader, more inclusive approach to ensure the community's supply of goods and services is reasonably priced. Our economic system has created disparities in power, a nexus that needs to be broken. Profit maximisation within industries is no longer a sustainable leadership approach.

This is no more evident and highlighted than in the New Zealand building industry, where social, economic and ethical failures have led to increased pain and inequity in the community. I know this to be true as I am currently trying to build a home. In November 2021, I was quoted a build cost of \$3,000 per square meter. In June 2022, this had increased to \$4,000 per square meter for a modest dwelling of 120 square meters.

How we respond to the issues is the critical question.

#### **Discussion**

The proposition that deregulating industry in the 1980s would set free vigorous gains that would leave everyone better off has failed. Instead, we saw the building sector consolidate into a series of oligopolies.

*Building a new home has never been so expensive. The cost of building a new dwelling soared by 18% in the March 2022 quarter, according to Statistics New Zealand. In fact, residential building costs were the single biggest reason why inflation rose to 6.9% – the largest inflation rise in more than 30 years. As far back as a decade ago, the Productivity Commission found it was 30% more expensive to build a home here than in Australia <sup>1</sup>.*

*The causes of the housing crisis are incredibly complex. But building costs are undoubtedly part of the equation. The cost of building an average house has risen 180 per cent over the past 20 years — much faster than wages and consumer goods generally.<sup>2</sup>*

Commerce Minister David Clark identified the dominance of some of New Zealand's biggest manufacturers. *There's Carter Holt Harvey, which controls nearly half of the country's structural timber trade and sells products through its building merchant Carters. Then there's Fletcher Building, the largest building materials supplier in Australasia, with a construction empire spanning 135 companies that generates over \$7 billion in revenue annually. It is one of two firms that control 85 per cent of the nation's concrete supply and one of three controlling 89 per cent of glass wool insulation supply. Its GIB board product has a staggering 94 per cent market share of the*

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<sup>1</sup> <https://www.consumer.org.nz/articles/can-we-fix-the-broken-building->

<sup>2</sup> Page 32 The High Price of Absolutely Everything August 2021 by Ollie Neas, contributing writer to North & South

*plasterboard market. It sells many of its products through its stores, PlaceMakers and Mico. And many of its products end up in homes built by its subsidiaries, such as Fletcher Living*<sup>3</sup>.

*Differentiating between issue, risk, and crisis management is complex, even for the professionals who work in those fields. Many product managers cannot differentiate between risks and issues, and the apparent inseparability of the issue and crisis management.*<sup>4</sup> What is evident is that matters of social injustice and economic power are being ignored and glossed over. This is evident in the building industry in New Zealand.

You cannot have a vibrant free market when oligopolies have vertically integrated product manufacture and sale outlets across their sectors. Who is watching these companies and their behaviour? Separating shareholder and stakeholder interests today is a false dichotomy; however, it still happens.

The building crises show the consequences of separating ethics from capitalism. Large companies may have corporate social responsibility policies and programs. But because they do not see ethics as connected to what they do and how they create value, they cannot fulfil their primary responsibilities to their customers. Instead, they destroy value for the entire economy and the community.

There needs to be a Royal Commission of Inquiry covering an interdisciplinary approach to the issues in the sector covering but not limited to commercial law, economics, history, financial management and politics.

I believe the more dominant the market position of a company, the larger the ethical and fiduciary responsibility to the community. These responsibilities must be reflected in government and regulators' applied regulations. Stakeholders must know about the power in their economic environment and what it means to manage moral behaviour.

A business takes advantage of its substantial degree of market power when, as a matter of practical business or commercial judgement, it would not have been able to engage in the conduct if it did not have that market power.

As a tiny part of the cost of a dwelling but a prime example, Winstone remains the largest wholesale supplier of plasterboard. It has maintained a market share of over 90% of the wholesale supply of plasterboard in New Zealand for many years. An investigation into Winstone Wallboards Limited, their market dominance and behaviour was undertaken in December 2014 by the Commerce Commission. As you know, these were the findings.

*A firm's size and financial resources do not provide it with substantial market power. Rather, a business has market power when it is not constrained in the way in which it would be constrained in a competitive market. In this case, if we do not consider Winstone to be substantially constrained by competitive pressures in the plasterboard market, then it will have a significant degree of market power. While we do not find it necessary to reach a final view, we consider it likely that Winstone has a substantial degree of market power. As such, we focus instead on whether Winstone has taken advantage of any substantial market power it may possess through its pricing practices.*<sup>5</sup>

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<sup>3</sup> Page 34 IBID

<sup>4</sup> Page 148 Business & society; ethics, sustainability, and stakeholder management, Ninth edition. (2015) Chapter 6 Issue, risk, and crisis management. Author Carroll, Archie B.; Buchholtz, Ann K.

<sup>5</sup> Page 15 Commerce Commission New Zealand ISBN 978-1-869454-27-2, Project no. 11.3/14505, Public version Investigation into Winstone Wallboards Limited Date: Dec. 22 2014

Now in 2022, you have to think that nothing much has changed. It has got worse. The report in 2014 makes for uncomfortable reading. You have to believe the company and the Commerce Commission have fallen short of the behaviour the community legitimately expects from the sector and its watchdog. Nothing has changed. Since 2020, the Gib shortage has been a thorn in the side of the construction industry. Orders have been delayed by months, houses have sat unfinished, and construction companies have gone under.

The problem has been entrenched by their dominance in the market over many years. Winstone plasterboard is the preferred product of those involved in designing, consenting and building houses, including obtaining the necessary building approvals from councils. Despite their market share, I find no evidence of Winstone's corporate social responsibility policy and program. I believe they take the market for granted because of their market share, and if the Commerce Commission had made a different finding in 2014, we might have avoided the market failure.

This is a minimal component of the supply chain, but what is the status of other elements, glass, timber framing, and cement? Construction in New Zealand is death by a thousand cuts. Nobody is watching these monopolies. It beggars belief that a Minister of the Crown (David Clark) cannot make the connection between the relative cost of building in New Zealand and the market share he outlined above and not move to do anything about it.

*"New Zealand is the only country with modern competition law that requires an anti-competitive purpose and does not consider the effects of the conduct" (MintnerEllisonRuddWatts, 2019). The Commerce Commission puts it this way: A business with a substantial degree of market power can compete in the same way as a business which does not have market power" (Commerce Commission, 2019). A former commission member says of section 36 that 'its design allows anticompetitive behaviour to slip through" (Curtin, 2016, p.13).*

*In 2015, the manifest inadequacy of section 36 was highlighted at a Commerce Commission conference: 'Reliance on the counterfactual test ... will fail to condemn conduct that warrants prohibition, precisely because it fails to attribute any significance to the dominant firm's market power' (Gavil, 2015, p.1046, emphasis added). Notwithstanding decades of criticism of section 36, officials in the Ministry of Business, Innovation and Employment have continued to give pride of place to the 'efficiency' defence of monopoly<sup>6</sup>.*

*The same counterfactual test was crucial in a further Privy Council decision, Carter Holt Harvey v Commerce Commission [2006] 1 NZLR 145, which cleared Carter Holt Harvey of what (on any commonsense view of the facts) amounted to predatory pricing and exclusionary bundling, on the basis that Carter Holt Harvey was merely competing vigorously<sup>7</sup>.*

*The law still says that all firms, even those with a substantial degree of market power, are permitted to act in what they judge to be their commercial best interests, regardless of the effect on smaller competitors. What their 'purpose' may be cannot be known by outsiders nor reliably inferred from their conduct.<sup>8</sup>*

Public trust is eroded when MBIE is happy to spend time and energy, producing a framework for carbon emissions reductions for the sector but does not address the costs and monopolies within the industry and continues with the 'efficiency' defence of monopolies.

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<sup>6</sup> [www.researchgate.net/publication/343556765\\_Why\\_the\\_Commerce\\_Act\\_1986\\_is\\_Unfit\\_for\\_Purpose](https://www.researchgate.net/publication/343556765_Why_the_Commerce_Act_1986_is_Unfit_for_Purpose)

<sup>7</sup> [www.researchgate.net/publication/343556765\\_Why\\_the\\_Commerce\\_Act\\_1986\\_is\\_Unfit\\_for\\_Purpose](https://www.researchgate.net/publication/343556765_Why_the_Commerce_Act_1986_is_Unfit_for_Purpose)

<sup>8</sup> Page 84 IBID

Government must listen carefully to the Commerce Commission's recommendations and proceed with meaningful changes to Section 36 and Section 27 of the Commerce Act to ban rebates, pocket pricing, unreasonable bundling, and abuse of market power. Suppose you don't know what these behaviours are. In that case, all you need to know is that most rebates, pocket pricing, unreasonable bundling, and abuse of market power are illegal practices in Australia.

As John Gardiner from Building Confidence Ltd raises in his report, there is no fundamental reason why the building regulatory system should primarily use local standards in solutions and methods. While local standards can be positive in that they reflect local practices, they can be limited.<sup>9</sup> People don't know what they don't know! Likewise, organisations like BRANZ over the years have been highly criticised for protecting their economic position and established business relationships, primarily if they represent an established market participant. The proverbial fox is often guarding the hen house. The big issue for business is that of "trust." Can the public trust the sector as a whole?

We can sit and play around the edges, pat each other on the back, and say there is nothing to see here, as the Commerce Commission did with their 2014 report. But the real elephant in the room is the industry's structure and make-up.

### **Recommendation(s)**

The issue concerns the transfer of wealth from purchasers (the community) to oligopolies through market structure, market power, and poor competition policy implementation. If not adequately governed, these market forces restrict product access and stifle competition such that only incumbents can survive.

- There needs to be a Royal Commission of Inquiry into the building sector in New Zealand using the Commerce Commission Market Studies Guidelines Date: Nov. 19, 2020
- As per John Gardiner's submission, we need less reliance on New Zealand Standards to set product performance levels
- Lift the corporate veil and have an open-book policy on product pricing with international benchmarking for comparison
- Define a monopoly market share and look to cap it where appropriate
- Outlaw, the making of excess profits
- Have the Commerce Commission undertake independent audits on vertically integrated businesses – oligopolies and monopolies

### **Conclusion**

The best interests of the community as a whole should be at the centre of our commercial law.

There needs to be an understanding in shareholder and stakeholder theory of the symbiotic relationship in stakeholder relationships and the need for acknowledgement of their mutual dependence, and a move away from the current parasitic practices on display in the building sector in New Zealand as a result of a lack of competition, barriers to entry and a few players with dominant market positions. Unsurprisingly, this is not the only sector in New Zealand that needs looking into.

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<sup>9</sup> Page 22 Submission by John Gardiner Building Confidence Ltd

## **References**

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