

Monopoly Watch NZ (MWNZ) is a NZ evidence based public policy analysis group which wishes to comment on New Zealand's building materials market and explain the linkage between High HHI Ratios in building materials and low productivity in assembly of houses in New Zealand.

We want to promote a fundamental rethink on social houses in entry level market segments so that houses built with taxpayers' money are fundamentally re-engineered so that the New Zealand house assembly industry can deliver pricing at an international best practice price.

We thank the Commerce Commission for engaging with Monopoly watch and setting such a high standard for analysis and enquiry.

During the market study enquiry substantial evidence will be submitted to prove that the current industry structure is not working for consumers and suppliers.

#### **Monopoly Watch seeks to highlight**

1. Evidence which illustrates the problem and related issues
2. Commentary on major league items subject to debate
3. Ideas to uniquely fix the industry currently in a dire position

We thank the commission for its leadership and its Preliminary Issues Paper. We applaud its 60 questions.

Monopoly Watch believes the primary focus must be how we fix this problem. That means examining:

#### **Market Structure = Market Conduct = Financial Performance & Outcomes for Stakeholders.**

The industry has performed fabulously for investors who own vertically integrated supply chains, but not so for consumers or tradesfolk.

A new industry structure is needed to resolve bizarre historical behaviour issues, specifically in economy market segment of house assembly.

The question that needs to be asked also serves to as a de facto problem description:

***"In Economist terms why does it cost approximately \$NZ3800 a square metre (on weighted average basis) to build entry level social houses when international best practise like for like quality is approx. \$NZ1200?"***

Many submitters will answer that it's death by a thousand cuts and blame other components of the value chain.

Monopoly Watch predicts submission after submission blaming Councils, MBIE, Kainga Ora, the weather - everyone and everything except a thoughtful review of industry structures precluded by vested interest lenses.

Monopoly Watch submits that the solution to the problem is well capitalised: institutional international scalable sized integrated builders who may be part or all government owned. A large scalable player circa 3000 – 5000 units a year means that it removes the margin-on-margin culture and resolves the death by a thousand cuts conundrum from which bespoke small operators suffer. Guarantees, quality and the start of the panelised and off-site manufacture journey can start with this.

Monopoly Watch has an expert witness from a recently departed large building materials multinational. MR YYY, FFFF, XXXX from ABC XYZ would like to attend the commission to share market structure stories and insights on how to fix the markets in some important components.

Monopoly Watch has a series of international associates who could be available to share data and canvas world best solutions. These activities must take place initially in private and in commercial confidence to verify research.

Today Government agencies use multiple small scale (by international standards) operators who compete amongst each other for resources, essentially bidding up pricing. And although it's praiseworthy that many houses have now been built, the social housing sector has been focused on speed of build, rather than cost of build.

We urge the Commission to use this inquiry to study two possible solutions:

- 1) **Structural separation of vertically integrated building materials distributors** (this gives market structure integrity and promotes incentives to worry about builders and tradespeoples' productivity in assembly and open the door to innovation and product competition.
- 2) **The creation of internationally scalable social house building companies, specifically designed to produce standardised high quality social houses at a cost per sqm similar to the international benchmark best practice price of \$NZ1200 Per sqm** . These new enterprises, which would be largely capitalised, solve the "death by a thousand cuts" problem, that smaller operators (even large New Zealand players), cannot overcome. These new operators would build the 'easy to build "house configurations" on "easy to build" scalable sites with the specific objective of driving costs to a new low level. Scale and capital would recreate a market segment, which was destroyed in the late 1980s and early 1990s, when builders shifted to bespoke and premium builds.

**Monopoly Watch is a New Zealand public policy group** which studies and comments on competition issues in capital intensive utility and commodity industries in New Zealand. Monopoly Watch draws upon wide and varied experience from game theory economists and captains of industry to millennials, centennials or adjacent, workers, middle management, Māori, the LGTBQ community, consumers, and suppliers. It is well-established that for many decades New Zealand has had one of the weakest competition legal frameworks in the OECD.

*It is the goal of Monopoly Watch to provide evidence-based third-party commentary and policy solutions to failing and distorted market structures to advance the public interests of all Kiwis.*

### **What is the relationship between Monopoly Watch and Kiwi Infrastructure ver 1.2?**

Monopoly Watch is an evidence-based private public policy group. It is not a lobbyist or an industry association.

MWNZ uses the mosaic theory of financial analysis to present evidence-based public policy ideas on how monopolies work and cause harm and, in particular, how they should be remedied for the public interest.

Monopoly Watch benefits from a tidal wave of goodwill from the general public.

Kiwi Infrastructure is the proposed greenfield institutional company vehicle which participated for over two years in an IPT process for transforming social house construction by securing large scale, high quality repeatable social house contracts, using a highly capitalised vehicle to deliver houses at the international benchmark price.

### **How to spot a monopoly**

Monopoly Watch has identified some common denominators of dominant duopolies or monopolies which are at odds with the public interest.

- 1) Low innovation
- 2) Overcompensation in ESG, CSR, and charitable PR releases
- 3) Overcompensation with PR releases about investment in infrastructure
- 4) Distraction to consumers with use of multiple brands
- 5) Continued use of confusion to consumers
- 6) Continued blaming RMA and council regulations for any problem
- 7) Lots of brass plates on opening facilities by politicians
- 8) Well-paid lobbyists whose invisible work cannot be scrutinised by the public.
- 9) Technical and complicated submissions
- 10) Requests for more and more analysis
- 11) Promises to do better with pretend, lacklustre, and pretend solutions
- 12) Highlighting Kiwi ownership as a virtue to compensate for high prices
- 13) Over-stating fringe and peripheral competition which does not constrain market abuses
- 14) Profitability considerably higher than international benchmarks for the same asset class
- 15) Most expensive lawyers in town and ensuing legal battles as a barrier to entry or activity
- 16) Protestations of multiple stakeholder harm if market structure changes

## Evidence for discussion downstream in the Market Study Inquiry

This Chart is being delivered CIC

Evidence	Comment

### Answers to 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?

Whilst building materials are only approximately 20-25% of the cost of a house, poor competition means lower productivity, because in more competitive markets there is competition (not just on price and quality) but on time to install and fix (builders, architects, designers, specifiers, in more competitive markets take notice on installation timing.

There is a lack of innovation in New Zealand in the important “economy market segment” defined as social houses or entry level housing, on an international benchmark basis with other countries of similar size and urbanisation. For example, here are no scalable builders, which means no organisational structures to create efficiency and price competition.

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

New builds are where all the progress can be made in lowering prices for Kiwi consumers, for ease of explanation we see three market segments in NZ: 1) Economy , 2) Premium and 3) Luxury. If the market economy segment is fixed in new build, we believe that costs will drop in all market segments, including renovations.

#### Q3 Are there any aspects of the building supplies industry which have a particular impact on Māori? Māori housing needs direct consultation, in particular regarding retro fit and rebuild of houses to meet healthy homes standards. We are aware that some Māori housing, particularly in remote rural areas, is in dire need of upgrading.

---

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

It is satisfactory, but it needs to be compared with scalable developers who build quality houses internationally at \$NZ1200 per sqm ( vs currently \$NZ3800). Some examples of international locations include Toronto, Houston, and Gothenburg where big players do not have costly middle-people intermediaries

- 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.** In other EU jurisdictions competition regulators have forced structural splits where distributors also manufacture. This is to create competition in supply and competition in installation systems
- 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?**

This is a satisfactory explanation, but we urge the commission to complete some international benchmarking and make judgment calls on what the cost differences and structure differences in better performing markets are, particularly where high quality social houses are built at circa \$NZ1200 per sqm.

- 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.** Insurance companies who insure against product or construction failure.

**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?**

There is not silver bullet to the death by a thousand cuts of construction affordability rather there must be a suite of changes and interventions considered. However, in many countries the following have made a difference 1) scale and 2) offsite manufacture and panelisation processes take place. This hasn't happened in New Zealand because there have been no disrupters in the market, and large scale players like USG /Knauf et al have exited our market.

**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.**

We disagree, This is because despite research we can't find any New Zealand homes without plumbing and electrical services. There are substantial price and

productivity differences in these services and installation practices, which our out of synch with international best practice.

We urge the commission to build a model which compares a basic quality healthy home social house in New Zealand with its best practice international peer group, seismic and humidity adjusted. We also suggest the Commission then compare table 1 (including electrical and plumbing) pricing and installation times.

**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?**

Yes.

- 1) What is international best practice
- 2) The IMPACT MARKET STRUCTURE HAS ON TIME TO FIX AND INSTALL PRODUCTS, (this is where the real cost blowout occurs) and helps economists and analysts account for the difference in costs of building social houses in NZ and EU best practice

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

The Monopoly Watch team thought it was academically lazy to canvas the market structure problems in Plasterboard (GIB) because it's too easy to understand what's wrong and the October 2014 ComCom Report explains it. What is useful is that many other less important products mirror this market structure and it's the list of the top 20 by strategic important (value and time to fix) which need attention

What's interesting about plasterboard is:

- 1) Rebates
- 2) Fixing systems
- 3) Nonsense about lateral support
- 4) Nonsense with Acqualine, which whilst still used in New Zealand to tile showers is banned in many international countries because it doesn't have a long enough life. Another interesting dynamic is that Fletcher Residential which produces it, does not allow it in their own Fletcher residential houses, choosing to use acrylic shower liners instead.

- Plasterboard
- Roofing
- Aluminium Windows
- Fixtures
- Sealants
- Premium paints
- Timber
- Plywood
- H3 and H5 poles
- Wiring & Switches in entry level segments
- Plumbing commodities

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

Greening of the building process and the eventual pathway to UK style EPC ratings means an evolution needs to occur. This is an opportunity to change the culture and pricing and productivity.

**Q11 Are the characteristics set out above an accurate reflection of residential. Please explain your reasoning.**

The impact of leaky homes continues as 3<sup>rd</sup> party professional consultants look to continue to preserve their reputations by using legacy products.

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

YES. There is no scale where the capital base of the assembly company is larger than that of the material supplier, which has the capital and the business case incentives to innovate and introduce difference systems and scalable change. The cottage industry structure of many building companies, (even the larger franchisers) means they are following the suppliers' orders, taking their rebates where possible and playing the margin on margin-on-margin game, which at every step the consumer pays for.

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

What needs to be reviewed is the HHI ratio of the products in short supply in New Zealand and the longer-term strategic impact of the sale of New Zealand forestlands in the 1990s to the American Pension Fund industry who on sold to Chinese investors. This needs to be compared with the long list of OECD countries which won't let unprocessed timber be exported. The question is often repeated how the supply of a basic commodity that New Zealand needs and leads the world in terms of product is exhausted.

**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.**

Prefabricated OSM (off Site manufacture) is not a silver bullet. It is a long-term evolution transforming from nail gun build to robotic build. This requires SCALE , SCALE and SCALE to develop. Scale lubricates capital, and scalable contracts deliver long term (7 yrs.), stable similar contracts where a Toyota-style culture can be brought to manufacture.

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

We intend to answer this question in detail with the related Kiwi Infrastructure organisation

**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.**

**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?**

No regulatory changes look at cost. They are all vested interest to specific clause, the new higher density housing is a rational place to secure “ standardised scalable structures, in say 3 configurations to complement this initiative which will lower land prices to simultaneously lower construction costs.

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

We will answer this in meetings

**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.**

With regard to regulatory issues all matters need reform to lower New Zealand building costs to the international benchmark. For well capitalised nationwide builders there needs to be a component cost of regulatory frameworks, which is similar to same percentage as in the best regulated environments such as of Canada, Texas, Sweden and other markets where building is more cost effective for citizens.

**Q21 What are the most important ‘green’ building supplies for us to focus on?**

Why are these important? CLT Cross Laminated Timber: more structure, less environmental damage, better pricing.

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

Recycling timber and materials

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

We believe the Commission would be well advised to select some well performing markets and make comparisons. Whilst travel is difficult it is possible for Commission staff and 3<sup>rd</sup> party consultant firms like McKinsey, Accenture and PWC. These firms have a wealth of information.

**Q24 Would international comparisons of key building supplies prices provide insights**



**into the level of competition in the industry? Why/Why not?**

Hell yes! Pricing can be adjusted for seismic, wind , humidity and it would also compare “TIME TO FIX or INSTALL “ in these prices.

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

- 1) EPC performance
- 2) Time to install
- 3) Use of robots % sqm built
- 4) Labour hours per sqm

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

International margin comparison would be useful in Plasterboard. Its nuts !! But the place to do the financial modelling is in the cost of construction per square meter in a comparison of a like for like social house ( i.e. 3 bed 2 bath 200sqm ) townhouse paid for by taxpayers .

**Q27 Are there other assessments that would provide better insights**

- 1) Search out international best practice in economy segment social housing cost per sqm seismic and wind adjusted
- 2) EPC ratings cost
- 3) Productivity measures (labour hours per sqm metre ) benchmarked

**Qu 28 On what geographic basis (e.g., local, regional, national) should we assess the concentration of key building supplies. Please explain your view.**

National – will revert with more detail

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

- 1) Plasterboard
- 2) Aluminium windows
- 3) Roofing iron
- 4) Timber trusses
- 5) Fixings
- 6) Concrete
- 7) Sealants

**Q30 What are the barriers to importers of key building supplies competingeffectively with domestic manufacturers?**

- Regulatory
- Rebates
- Distribution

**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.**

More detail to be supplied later.

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

Commodity building products are essentially capital intensive fixed costs business models. Scale is everything and barriers to entry are erected in NZ.

Because there are so many products that go into a house ('death by 1000 cuts'), we urge the Commission to choose the top 20 products and then closely look at the impact of competition on time to install and certification.

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

Distribution and architect / designer specification

**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?**

Yes, rebates, delivery times, other discounts, incentive trips, but essentially even a big New Zealand group house builder has no scale in terms of upstream negotiation capability.

**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.**

Yes, only where there is no competition. Vertical integration helps consumers unless HHI ratios are too high. This creates bad outcomes and no choice, but no competition in installation times.

**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?**

Yes, if there were 5 equal players with low HHI's then there is benefit. The problem is capital intensive business with vertical integration with high HHIs.

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

1. Market power
2. Accommodating behaviour
3. Rebates
4. End customer doesn't see "benefits" of training trips, rebates etc
5. No incentive for new products, green products, or quicker to fix products

**Q39 What forms do supplier rebates and loyalty payments typically take in this industry? (e.g., monetary, non-monetary, lump sum etc.) Does this vary by type**

**of building supply? If so, please explain how.**

Sports parties, training workshops and nightclub activity, (makes 1980s NY stockbrokers look tame).

**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?**

Both

**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?**

Yes , CIC will discuss

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

Tying arrangements cause market harm also productivity harm.

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

CIC discussion in meeting

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

The discounts and rebates are not disclosable, (working example: Gerry Smith builders shows client invoice for job ( \$1000 for XXX products),the client may see this, but they don't see the rebates, entertainment, they are not even invited to the nightclub!

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

Yes, productivity impact that tidy, prompt deliveries have and the fact that the major cost to the builder is delivery time, site management and sequencing.

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

Example: 2013 Cook Street Placemakers and Carters: a prosecution took place, and the fine was less than the cost of drinks on Friday evening

Monopoly watch applaud the Commission in it leading a discussion on Game Theory behaviours to preserve market structure. We will discuss the Accommodating behaviours in a meeting

**Q47 How transparent is pricing for key building supplies?**

It's not because of rebates, discounts and bundling. Things could not be opaquer.

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

Credit terms given to builders and their non disclosable rebate benefits: This is a problem in all industries the major problem in building is the absolute cost of

construction. All industries have bad behaviours. In construction it's the sharing of monopoly rents up and down the supply chain to preserve dominance.

Construction is hard, occasionally physically demanding, dusty and complex, the relationships at suppliers hugely impact productivity.

These bespoke incentives enable distributors to control tradies. An institutional scalable economy segment builder institutionalises these relationships, and these incentives are removed as real choice in purchasing evolves.

**Q49 Do the regulatory and standards systems (e.g., 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.**

Work in progress. We urge the Commission to hire international management consultants to review this area in detail.

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

Market power will just be transferred to the next technology.

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

Incumbents, by history, control of regulatory process, job swapping, knowledge, distribution chain, industry knowledge, rebates etc, consumer and regulatory preference

*"Mr XXX builder throws the GIB Fixing handbook at the customer and says, FFF, FFF, FFFFFUUU, if you want elephant board you will never get council approval"*

**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.**

Hell Yes! CIC, will discuss in meeting

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

To get the supplier warranties or council sign off you need the official bolts, screws, sealants, glues, etc.

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

Targets for transformation need to be set to international best practice

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

Specifiers and Architects, and Councils who want risk mitigation.

**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?**

We will answer this in detail in a meeting

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

Not always

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

Yes, we will revert on this

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

Long term impact of the leaky home crisis and how that has been used to secure the status quo.

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

- 1) Top 20 building materials by value in social housing. These should be listed and benchmarked internationally
- 2) A review of the linkage of high HHI ratio situations leading to poor productivity in installation and fixing
- 3) A review of cost per sqm, international best practise in social housing

**Thank you for Considering the position of Monopoly Watch NZ**

**Tex Edwards  
Financial Analyst**