



FORECAST REPORT 84

NEW ZEALAND TRENDS IN
PROPERTY AND CONSTRUCTION

THIRD QUARTER 2017

OFFICES AROUND THE WORLD

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Gaborone

Mauritius

Saint Pierre

Mozambique

Maputo

South Africa

Cape Town

Johannesburg

Pretoria

ASIA

North Asia

Beijing

Chengdu

Chongqing

Dalian

Guangzhou

Guiyang

Haikou

Hangzhou

Hong Kong

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Macau

Nanjing

Nanning

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Seoul

Shanghai

Shenyang

Shenzhen

Tianjin

Wuhan

Wuxi

Xiamen

Xian

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Dubai

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Brisbane

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Darwin

Gold Coast

Melbourne

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Sydney

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New Zealand

Auckland

Christchurch

Hamilton

Palmerston North

Queenstown

Tauranga

Wellington

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CONFIDENCE TODAY INSPIRES TOMORROW

RIDER LEVETT BUCKNALL

With a network that covers the globe and a heritage spanning over two centuries, Rider Levett Bucknall is a leading independent organisation in cost management and quantity surveying and advisory services.

Our achievements are renowned: from the early days of pioneering quantity surveying, to landmark projects such as the Sydney Opera House, HSBC Headquarters Building in Hong Kong, the 2012 London Olympic Games and CityCenter in Las Vegas.

We continue this successful legacy with our dedication to the value, quality and sustainability of the built environment. Our innovative thinking, global reach, and flawless execution push the boundaries. Taking ambitious projects from an idea to reality.

FORECAST 84

Prepared by the New Zealand Institute of Economic Research (Inc.) exclusively for Rider Levett Bucknall, Forecast is produced quarterly and provides detailed local construction market intelligence and knowledge.

CONSTRUCTION MARKET INTELLIGENCE

Forecast is supplemented by Rider Levett Bucknall's construction market intelligence publications: the International Report, regional (including the Oceania Report) and country specific reports.

KEY POINTS IN THIS ISSUE

Construction activity eased in March, but underlying demand remains strong

Residential and non-residential construction activity eased in the March quarter, in line with the slowing in building consent issuance earlier in the year. High construction costs, funding costs and lending restrictions may be impacting on feasibilities and leading to project delays, but underlying demand remains strong.

Supported by the surge in net migration

Beyond 2017, the construction outlook remains strong, supported by the continued surge in net migration.

Strong tourism activity drives demand for non-residential construction

Demand for new accommodation buildings continues to rise, reflecting the surge in tourists.

Interest rates likely on hold until mid-2018

The New Zealand economic growth outlook remains positive and annual inflation is back in the Reserve Bank's target. The main downside risk is from geo-political tensions offshore.

We continue to expect the Reserve Bank to start lifting the Official Cash Rate in the middle of next year.



BUILDING ACTIVITY TRENDS

Construction activity eased in the March quarter. Higher construction and funding costs, as well as banks' tightening access to credit, have seen some building developments put on hold.

Hotels, healthcare facilities and office space were the top three drivers of non-residential construction demand over the past year. This reflects the effects of strong tourism activity and population growth.

Net migration into Auckland of around 35,000 over the past year was the highest in over 20 years. This is the biggest driver of building activity in the region.

Although Auckland Council is issuing more dwelling consents than in previous years, the housing stock is not growing in line with the population.

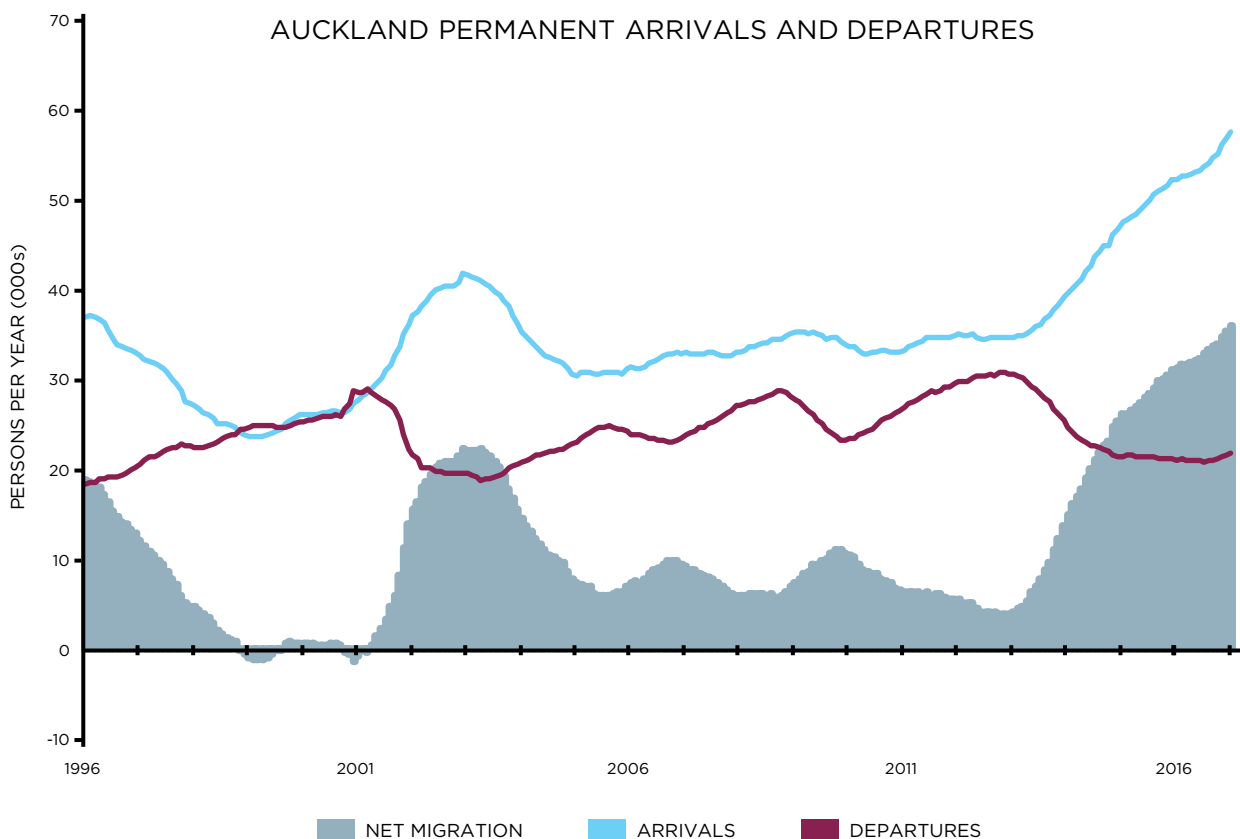
The increase in the number of permanent migrants has boosted demand in the New Zealand economy, particularly construction activity and retail spending. It has also expanded the labour supply. The increase in work visas issued over the past year have been led by jobs in the trades, and this has helped to mitigate labour shortages in the construction sector. Our Quarterly Survey of Business Opinion shows building sector firms reporting an improvement in availability of labour recently, particularly for unskilled labour.

Residential construction cost inflation in Auckland moderated in the March quarter, although annual growth at 8 percent remains very high.

Outside of Auckland, construction cost inflation is also lifting, indicating a broadening in capacity pressures on the back of increased construction activity across New Zealand. Construction demand in the "halo" regions of Waikato and Bay of Plenty increased particularly strongly. This strong growth reflects the spill-over effects of strong population growth from Auckland.

FIGURE 1
Net migration into Auckland reached new record highs

Permanent arrivals and departures, annual 000s



Source: Statistics NZ, NZIER

BUILDING ACTIVITY OUTLOOK

The continued surge in net migration points to solid underlying demand for construction. Net migration into Auckland is particularly strong, and this is where construction growth is likely to be concentrated.

Although non-residential construction declined in the first quarter of 2017, the outlook remains positive. Strong tourist inflows mean there is now a shortage in accommodation, and this is driving demand for new hotel developments. Meanwhile, population growth continues to drive increased demand for new healthcare facilities and office buildings.

ECONOMIC BACKDROP

We expect economic growth to pick up over the coming year, underpinned by solid household spending, business investment and a recovery in exports. The recovery in global dairy prices will also support the solid New Zealand economic growth outlook.

In contrast, the global backdrop remains highly uncertain. Although economic activity and inflation in the major economies are starting to pick up, heightened geopolitical tensions present a downside risk to the global growth outlook.

As a small open economy, New Zealand will not be immune to any downturn in the major economies.

INTEREST AND EXCHANGE RATES

The Reserve Bank will be balancing a favourable New Zealand economic growth outlook and rising inflation pressures with heightened offshore geopolitical risks. We continue to expect the Bank will begin to lift the OCR from mid-2018.

In advance of this expected increase in the OCR, both floating and fixed term mortgage rates have increased in recent months. This reflects a combination of higher funding costs for banks, and financial markets' conviction that the Reserve Bank is firmly on a tightening track.

The New Zealand dollar has remained high, reflecting New Zealand's more positive economic outlook relative to the other major economies. Concerns around US President Trump's policies have weighed on the US dollar. The New Zealand dollar has been particularly strong against the Australian dollar as the economic outlooks between the two countries continue to diverge. We expect the New Zealand dollar will begin easing from late 2017 as improving prospects in the other major economies underpin an appreciation in their currencies.

BUILDING INVESTMENT

Our Quarterly Survey of Business Opinion's architects' measure of own activity show softening in growth in the pipeline of non-residential work, and there is likely to be a further modest easing in this rate of growth over the remainder of 2017. Beyond that, we expect strong population growth and tourism activity to remain a key support for demand for new offices and hotels over the next few years.

BUILDING CONSENTS

Demand for new accommodation buildings remains very strong, while demand for new office buildings recovered. With vacancy rates for prime Auckland office space at historic lows, we expect demand for new office buildings will continue to grow.

The average value per square metre consented has continued to lift sharply, in line with strong growth in other construction cost measures.

Building consents by sector

Strong population growth underpins many of the longer-term trends:

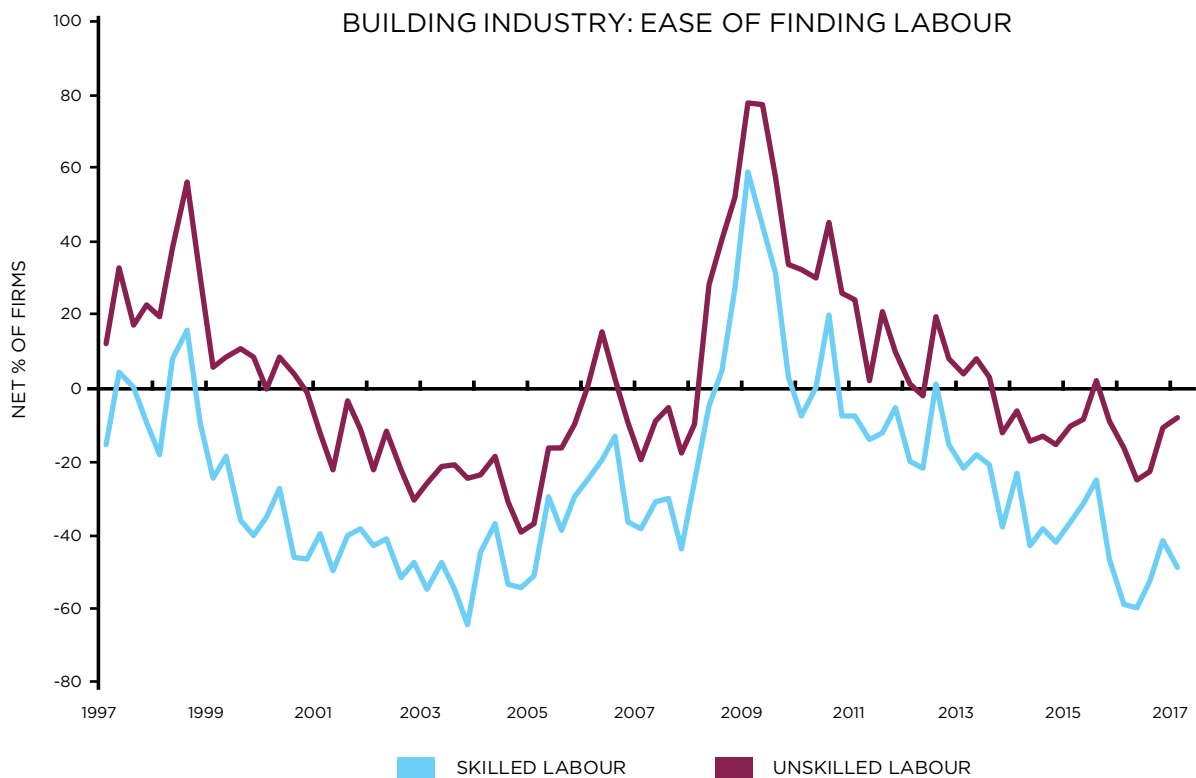
- Office growth to accommodate the higher number of white collar workers.
- Public sector spending on education and healthcare facilities, along with rebuilding activity.
- Capacity constraints in the tourism sector will continue to drive growth in demand for new accommodation buildings.

We expect earthquake rebuilding and strengthening activity will continue to add to non-residential construction demand.

FIGURE 2

Building sector firms report an easing in labour shortages

Net % of firms reporting ease in finding labour



Source: Statistics NZ, NZIER



Building consents by region

The surge in the Auckland population continues to drive strong growth in construction demand. Besides the increased demand for housing, population growth is also supporting greater demand for schools, office buildings and healthcare facilities.

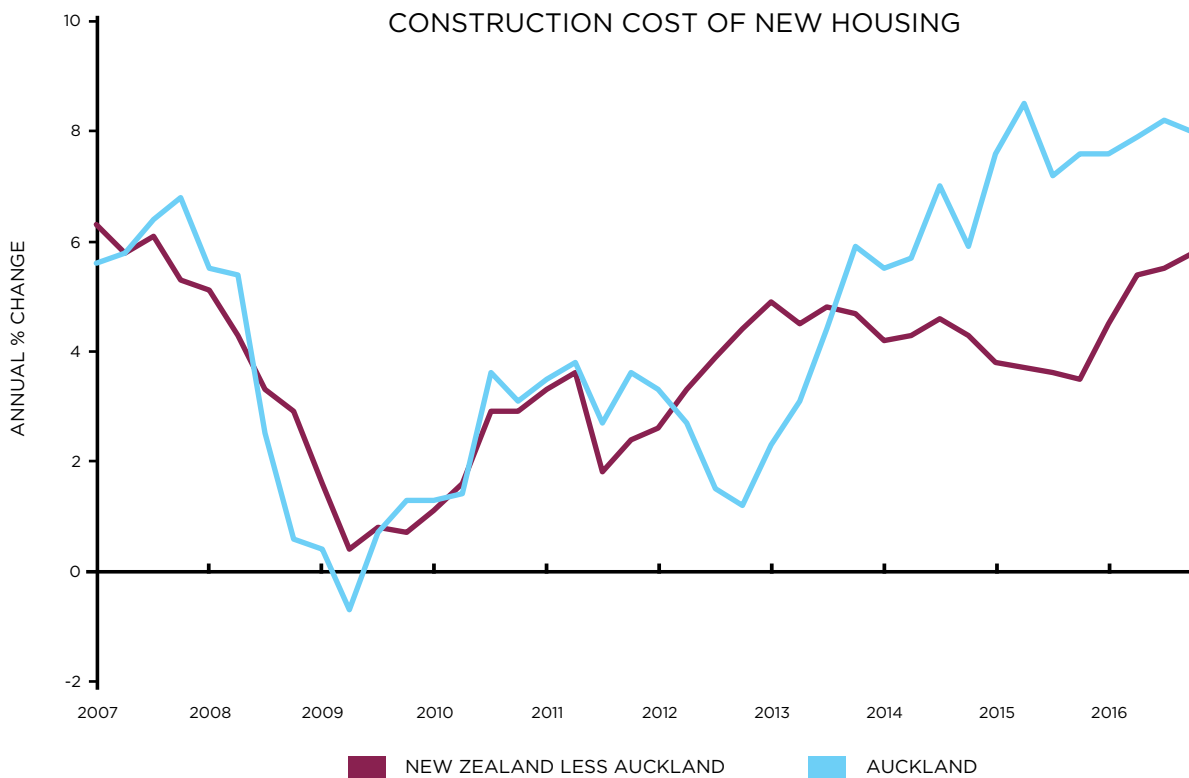
Construction activity is also broadening beyond Auckland, with population growth spilling over to Waikato and the Bay of Plenty, boosting construction demand.

Construction demand in Wellington is also lifting, albeit more modestly. An increase in demand for new office space, retail outlets and accommodation buildings is driving growth in non-residential construction.

In contrast, construction demand in Canterbury continues to decline, with councils issuing markedly fewer consents for education buildings and offices over the past year. We expect further

easing in construction demand in Canterbury over the coming year, although the level of activity should remain relatively high given population growth in the region and improved profitability in the rural sector.

FIGURE 3
Construction cost inflation broadening beyond Auckland
 Annual % change in residential construction cost

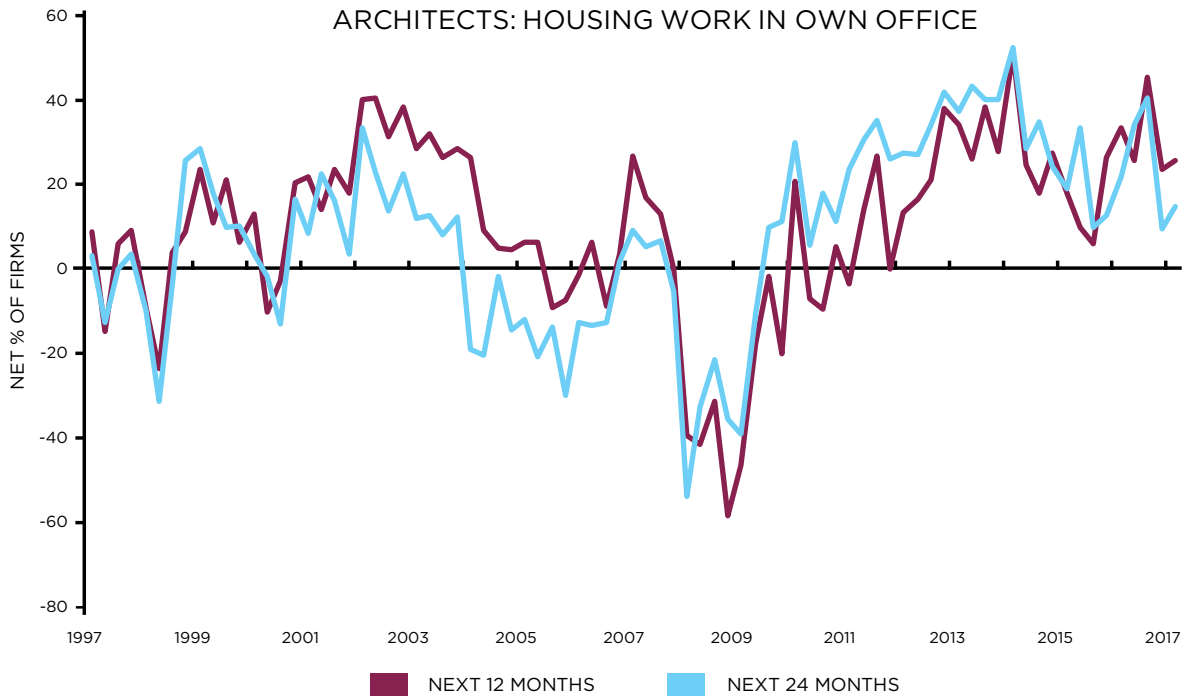


Source: Statistics NZ, NZIER

FIGURE 4

Easing in growth in pipeline of construction work

Net % of firms reporting an increase in activity

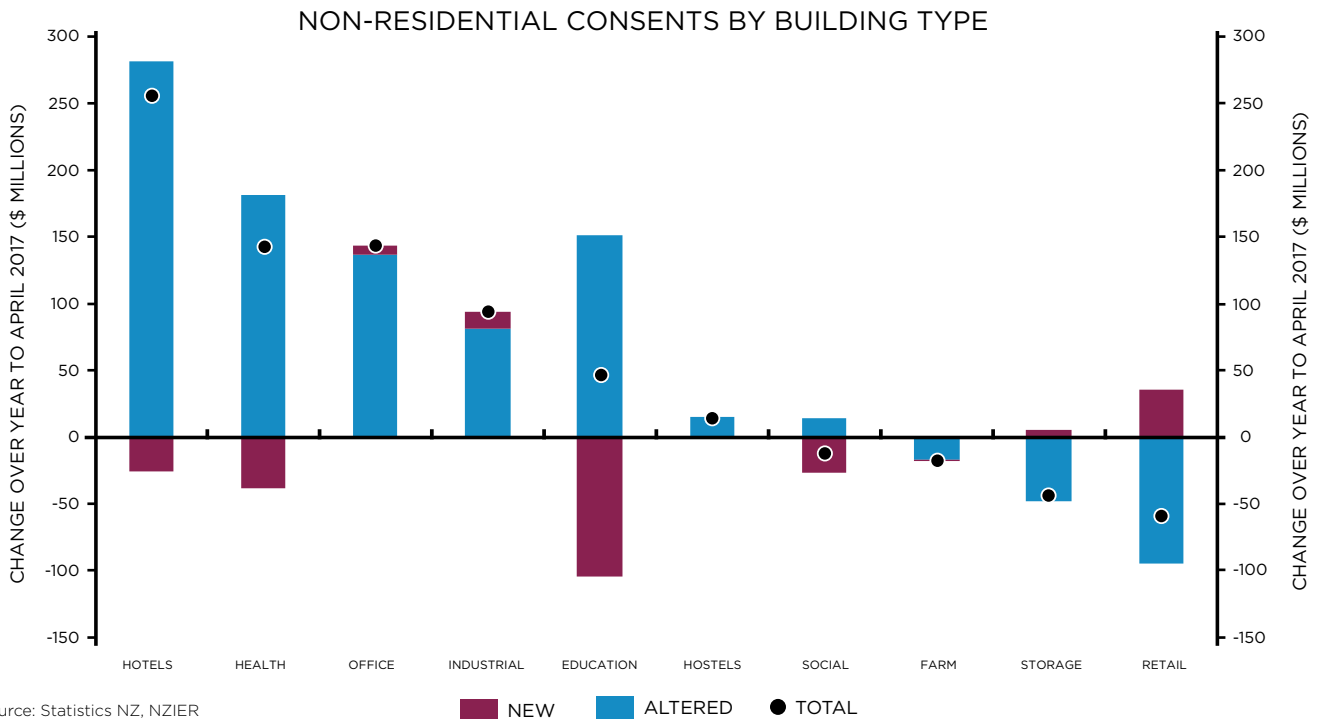


Source: Statistics NZ, NZIER

FIGURE 5

Strong tourism activity continues to drive demand for accommodation buildings

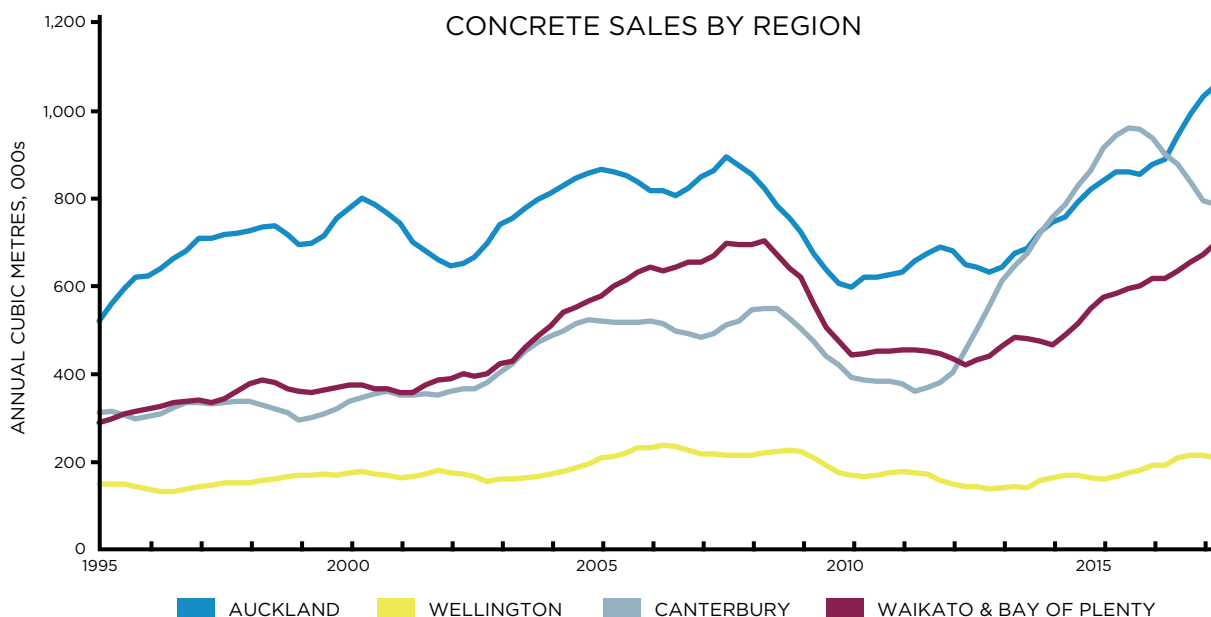
Annual change in consents, \$m, year ended April 2017



Source: Statistics NZ, NZIER

FIGURE 6

CONSTRUCTION GROWTH LED BY AUCKLAND, BUT BROADENING ANNUAL VOLUME, THOUSAND CUBIC METRES



Source: Statistics NZ

TABLE 1

Non-residential building consents by region and sector

\$m of consents for the year ending April 2017; red colour shading for decline in consents from previous year

REGION	SECTOR									
	HOSTELS, PRISONS ETC	ACCOMODATION	HEALTH	EDUCATION	SOCIAL, CULTURAL, RELIGIOUS	RETAIL	OFFICE	STORAGE	INDUSTRIAL	FARM
NORTHLAND	0.0	5.2	5.7	23.8	2.7	9.8	9.6	3.8	6.1	8.3
AUCKLAND	144.9	219.6	193.9	413.0	72.8	308.1	560.8	253.9	134.9	24.4
WAIKATO	0.9	10.7	32.0	46.1	30.5	67.2	42.2	37.0	61.6	55.9
BAY OF PLENTY	0.9	1.0	26.5	38.7	27.3	40.9	38.6	70.8	26.2	10.0
GISBORNE	0.0	0.0	1.1	3.1	7.3	0.2	9.6	0.7	2.5	1.9
HAWKE'S BAY	9.5	0.4	12.5	11.9	10.4	11.4	7.5	24.3	33.4	6.2
TARANAKI	0.7	4.8	4.9	16.5	12.2	3.1	15.2	3.5	30.8	19.3
MANAWATU-WANGANUI	6.0	3.9	8.9	24.2	10.2	18.8	30.1	3.0	17.8	15.0
WELLINGTON	13.8	37.0	28.8	101.8	64.2	88.6	283.8	19.1	25.2	5.7
NELSON	0.1	0.0	2.9	6.8	9.4	4.7	24.3	14.7	8.0	0.8
TASMAN	0.0	0.4	0.5	3.0	0.1	3.3	2.8	10.2	4.9	4.1
MARLBOROUGH	0.3	1.6	0.1	6.1	3.9	0.7	8.6	4.3	12.7	4.6
WEST COAST	0.0	5.2	55.4	0.8	2.7	1.3	1.6	0.7	0.8	2.0
CANTERBURY	25.9	81.1	302.1	282.4	122.1	166.4	238.5	177.5	120.3	53.5
OTAGO	24.1	41.7	11.5	188.3	19.0	53.3	25.9	21.4	28.9	14.0
SOUTHLAND	5.2	1.5	1.1	5.2	0.6	6.7	5.5	8.6	22.0	9.0

Source: Statistics NZ, NZIER



BUILDING COSTS

The Capital Goods Price Index for Non-Residential Buildings (CGPI-NRB) (the Index) is an official measure of cost movements in the sector. The Index excludes GST. We use the Index as an indicator of cost escalation.

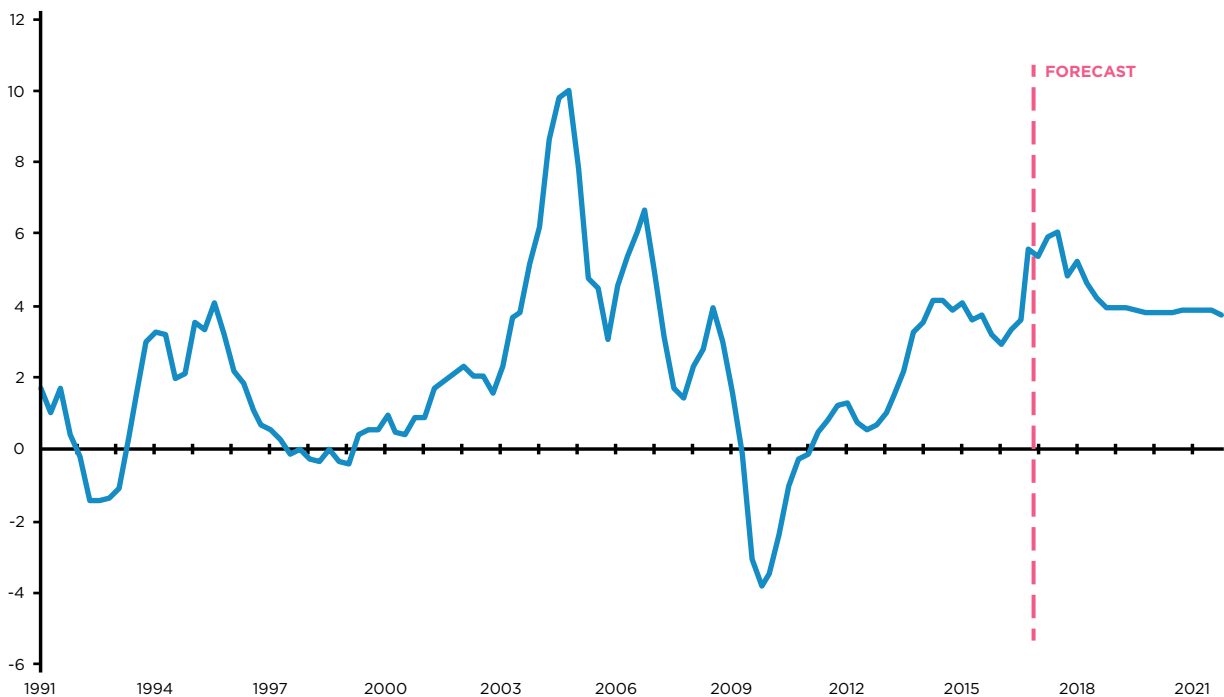
The Index is a national average across all building types. We therefore advise caution in applying the increase in the CGPI-NRB as an indicator of cost escalation for specific projects.

The Rider Levett Bucknall Second Quarter 2017 Oceania Report provides local regional comment and tender price relativity between the main New Zealand and Australian centres. This publication is available at www.rlb.com or on request from any Rider Levett Bucknall office.

We forecast construction cost inflation to moderate to below 5 percent by the second half of this year. Beyond 2017, annual construction cost inflation should

average around 3.5 percent. Despite the solid construction growth outlook for the next three years, we do not expect the inflation to be as sharp as the mid-2000s given that the lower inflation environment limits the extent to which rising costs can be passed on quickly, and strong net migration is helping to mitigate skills shortages in the building sector.

FIGURE 7
Non-residential building cost escalation
CGPI-NRB index, annual % change



Source: Statistics NZ, NZIER forecasts

TABLE 2**Non-residential building cost index**

YEAR	QUARTER	INDEX	QUARTERLY % CHANGE	ANNUAL % CHANGE
2012	MARCH	1351	0.1	1.3
	JUNE	1352	0.1	0.7
	SEPT	1354	0.1	0.5
	DEC	1358	0.3	0.7
2013	MARCH	1365	0.5	1.0
	JUNE	1372	0.5	1.5
	SEPT	1383	0.8	2.1
	DEC	1402	1.4	3.2
2014	MARCH	1413	0.8	3.5
	JUNE	1429	1.1	4.2
	SEPT	1440	0.8	4.1
	DEC	1456	1.1	3.9
2015	MARCH	1471	1.0	4.1
	JUNE	1480	0.6	3.6
	SEPT	1494	0.9	3.8
	DEC	1502	0.5	3.2
2016	MARCH	1514	0.8	2.9
	JUNE	1529	1.0	3.3
	SEPT	1548	1.2	3.6
	DEC	1586	2.5	5.6
2017	MARCH	1595	0.6	5.4
	JUNE	1619	1.5	5.9
	SEPT	1641	1.4	6.0
2018	DEC	1662	1.3	4.8
	MARCH	1679	1.0	5.2
	JUNE	1694	0.9	4.6
	SEPT	1711	1.0	4.2
2019	DEC	1728	1.0	3.9
	MARCH	1744	1.0	3.9
	JUNE	1761	1.0	4.0
	SEPT	1777	0.9	3.9
2020	DEC	1794	0.9	3.8
	MARCH	1810	0.9	3.8
	JUNE	1827	0.9	3.8
	SEPT	1845	1.0	3.8
2021	DEC	1863	1.0	3.8
	MARCH	1880	1.0	3.9
	JUNE	1898	1.0	3.9
	SEPT	1916	0.9	3.9
	DEC	1933	0.9	3.8

Notes: The current and forecast CGPI-NRB is a national average, which does not differentiate between regions or building types. We therefore advise caution in applying the increase in the CGPI-NRB as a measure of cost escalation for specific building projects.

Source: Statistics NZ, NZIER forecasts

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