THIRD QUARTER 2019

FORECAST REPORT 92

NEW ZEALAND TRENDS IN PROPERTY AND CONSTRUCTION

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Cover: Wellington Harbour

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 92

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 picks up

There was a strong lift in both residential and non-residential demand in the first quarter of 2019. The increase in consent issuance in the early months of 2019 points to further growth in construction activity over the remainder of the year.

Migration picture remains uncertain

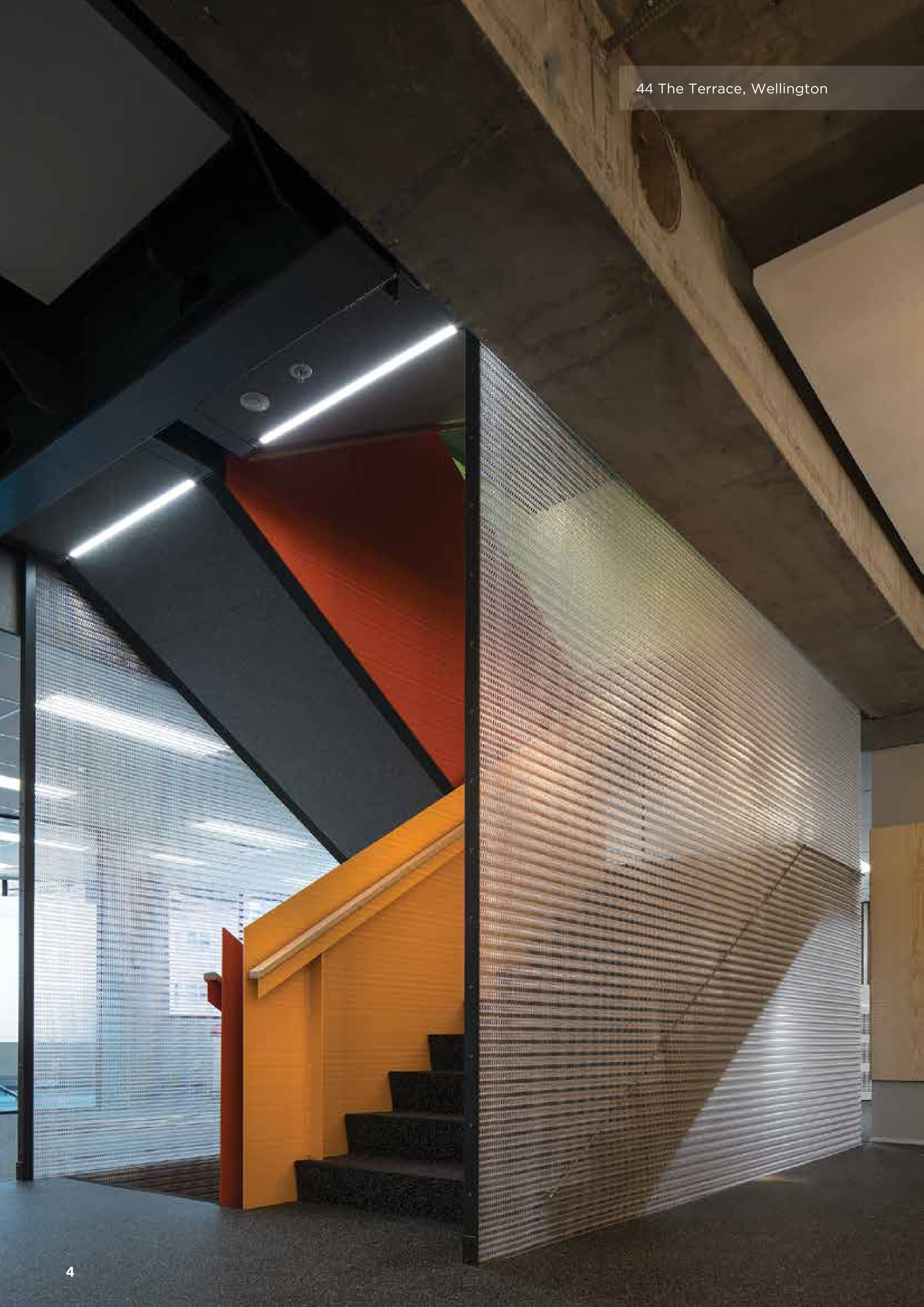
The new and revised migration data from Statistics NZ suggest strong population growth. However, there remains uncertainty over the strength of net migration inflows given the new methodology adopted by Statistics NZ in the wake of the removal of departure cards. Although net migration looks solid, there is the potential for downward revisions.

Non-residential construction demand continues to be led by Auckland

Auckland continues to dominate construction demand, driven by increased demand for retail outlets, storage buildings and accommodation. Besides Auckland, construction demand has been lifting in the smaller regions. This has seen construction cost escalation outside of the main regions pick up over the past year.

Expectations of further easing keep interest rates low

Markets are expecting further decreases in interest rates over the coming year, following the Reserve Bank's OCR cut in May. Along with (what appears to be) solid net migration, we expect lower interest rates will support housing demand and construction activity.


44 The Terrace, Wellington

BUILDING ACTIVITY TRENDS

Construction activity ramped up in the first quarter of 2019, reflecting a strong increase in both residential and non-residential construction. Consent issuance started the year on a strong note, suggesting further growth in construction activity over the remainder of the year.

Auckland continues to dominate construction demand, reflecting the effects of strong population growth in the region over the past few years. Although there was been some softening in Auckland housing demand over the past year, demand remains at high levels and is encouraging residential construction. Strong population growth and tourism activity has also underpinned demand for new retail outlets and accommodation buildings in the region.

Construction demand continues to broaden to the other regions. Residential consent issuance in Canterbury is starting to recover after the easing since 2015. Demand is also picking up in Waikato and Wellington, as higher house prices encourage new housing supply to come on board. Non-residential consent issuance in these two regions have also increased over the past year, largely reflecting stronger demand for social buildings. We expect earthquake strengthening will continue to underpin office construction demand in Wellington.

There remains a large degree of uncertainty over just how strong net migration is. The new revised migration data released by Statistics NZ shows a reacceleration in net inflows into the country. This new data is based on a passport-linked measure that requires provisional estimates to be made, hence will likely be prone to revisions.

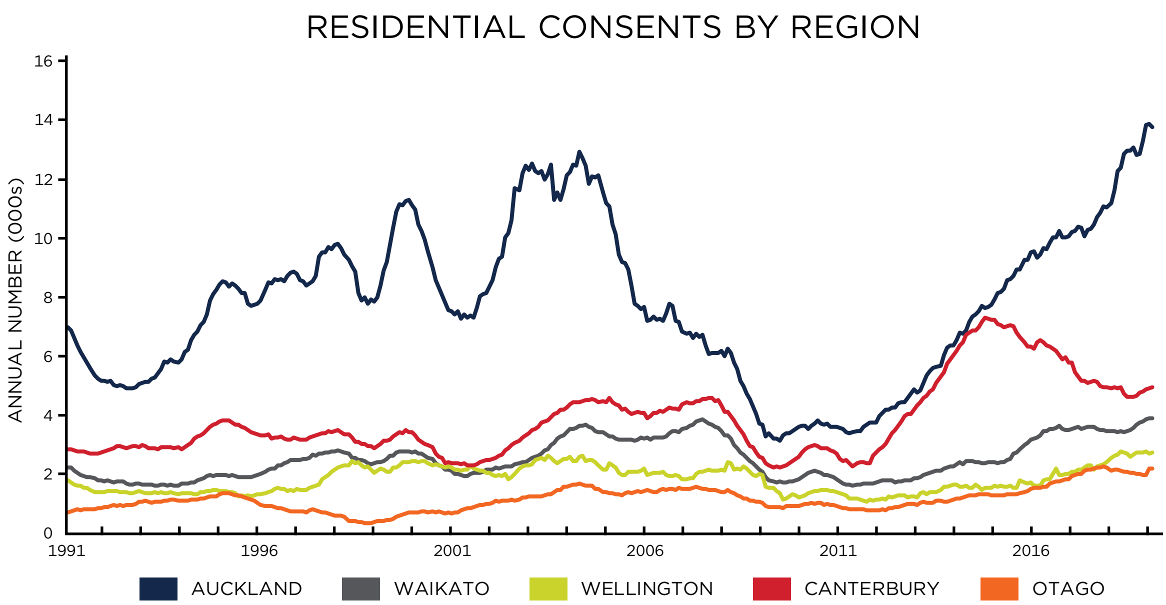
Hence the recent upward revision to permanent arrivals into the country needs to be interpreted with caution. The new data shows a reacceleration in the number of non-New Zealand citizens moving to the country, in contrast to the easing in these types of migrants under the old measure. However, we will not know the true status of travellers until 16 months after they have crossed the NZ border, given a permanent arrival is defined as someone who has spent 12 of the 16 months in New Zealand. Although there is uncertainty over the degree of strength in population growth, overall we still expect net inflows to support construction demand.

Although the absolute level of construction in the Canterbury region is picking up, as a proportion of total construction nationwide, it continues to ease. This reflects the relatively greater increase in construction activity in the smaller regions, with signs that capacity pressures are picking up outside of the main centres.

FIGURE 1

Residential construction demand picking up in other regions

Number of consents issued



Source: Statistics NZ

BUILDING ACTIVITY OUTLOOK

The increase in construction activity outside of the main centres has seen construction cost inflation pick up in the smaller regions. In contrast, construction cost inflation in Auckland is moderating, with annual growth in costs easing from over 8 percent in late 2016 to just under 3 percent in the first quarter of 2019. Construction cost inflation in Canterbury and Wellington have also edged below 3 percent, indicating some easing in capacity pressures in the main centres.

Despite this recent easing, we expect construction cost inflation in Auckland will be relatively high given the substantial amount of construction activity in the pipeline. Construction sector firms continue to face headwinds of low operating margins and labour shortages.

We continue to expect high construction costs, along with a tightening by banks in accessing credit, will mean a protracted construction cycle. A protracted construction cycle is most likely in Auckland, where underlying construction demand remains strong.

Nonetheless, we expect the growth in construction costs will continue to moderate over the coming years, as rising prices attract more resources such as workers into the construction sector.

ECONOMIC BACKDROP

Activity and confidence indicators point to softer growth over 2019, but this should be temporary as solid migration-led population growth underpins demand. Lower intertest rates should also boost economic activity, and we expect growth to pick up from 2020. Overall, we expect annual GDP growth to average around 2.6 percent over the next five years. While this is well below the average of 3.4 percent over the previous five years, it still represents a sustained period of growth.

Downside risks to the growth outlook include weak business confidence and profitability, the ongoing trade war between the US and China, and continued uncertainty over whether a Brexit agreement will be reached.

INTEREST AND EXCHANGE RATES

The Reserve Bank cut the OCR in May, and left the door open for further easing in monetary policy. We expect another interest rate cut in September, given the central bank's concern with a potential deterioration in the global growth outlook.

The US Federal Reserve has also become more cautious about the growth outlook. Although the central bank has indicated it would look to keep the Fed funds rate on hold, there is increasing speculation in the markets that interest rates will be cut over the coming year.

The NZD/USD fell sharply in the wake of the Reserve Bank's shift to a dovish stance earlier this year. We expect it will track around 65 cents on average over the coming years, given the potential for a further cut to interest rates here in New Zealand.

BUILDING INVESTMENT

Consent issuance points to further growth in construction activity in the near term. Capacity pressures should limit the degree to which construction activity would ramp up further over the coming year, but underlying demand remains strong.

BUILDING CONSENTS

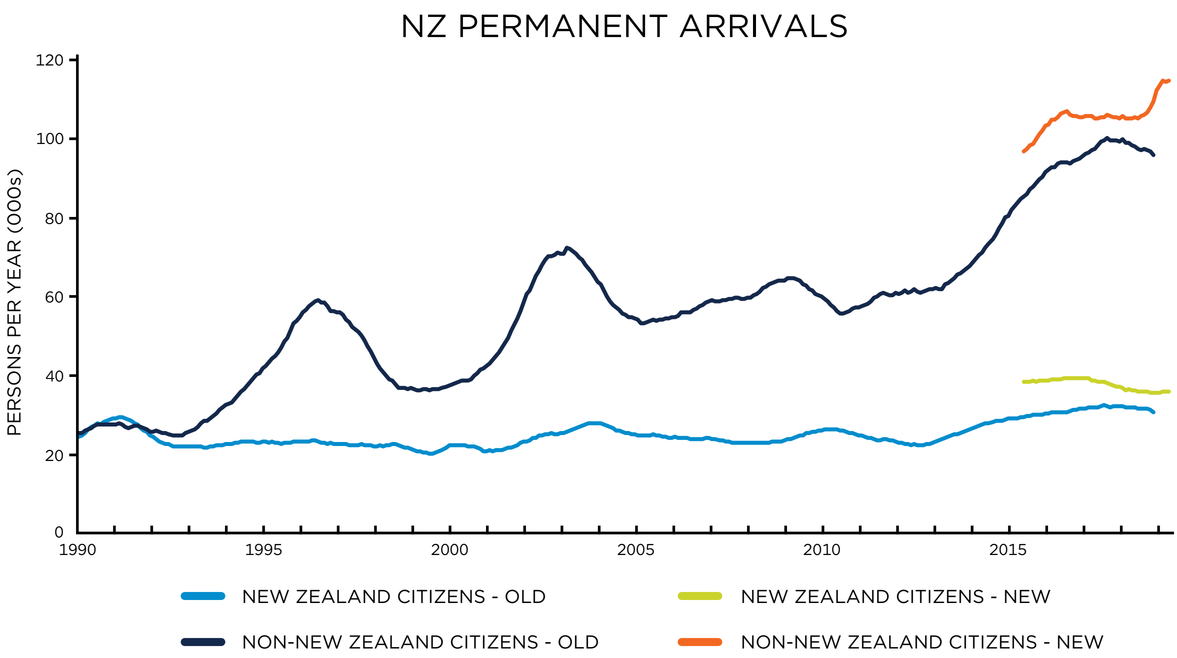
Non-residential construction consent issuance shows demand picking up towards highs last seen in the previous building boom in 2008. In contrast, there has been some easing in construction cost pressures.

Strong demand for social and storage buildings, retail outlets and hotels have driven the growth in non-residential consent issuance over the past year. In contrast, there has been a fall in demand for new office space and farm and industrial buildings. The recent easing in global commodity prices is likely to make farmers more cautious about on-farm investment.

FIGURE 2

Uncertainty over net migration picture

Annual number of people



Source: Statistics NZ


Te Ara a Tawhaki, Otaki

Building consents by sector

Although demand for storage buildings is currently strong, continued uncertainty over the effects of a potential deterioration in the global growth outlook is likely to curtail demand for this and other types of industrial buildings over the coming year.

Over the longer term, robust migration-led population growth and tourist inflows should continue to underpin demand. In particular, we expect further growth in demand for new accommodation buildings in response to the continued high numbers of international visitors, as well as strong domestic tourism activity.

Earthquake strengthening activity should also continue to contribute to non-residential construction demand.

Building consents by region

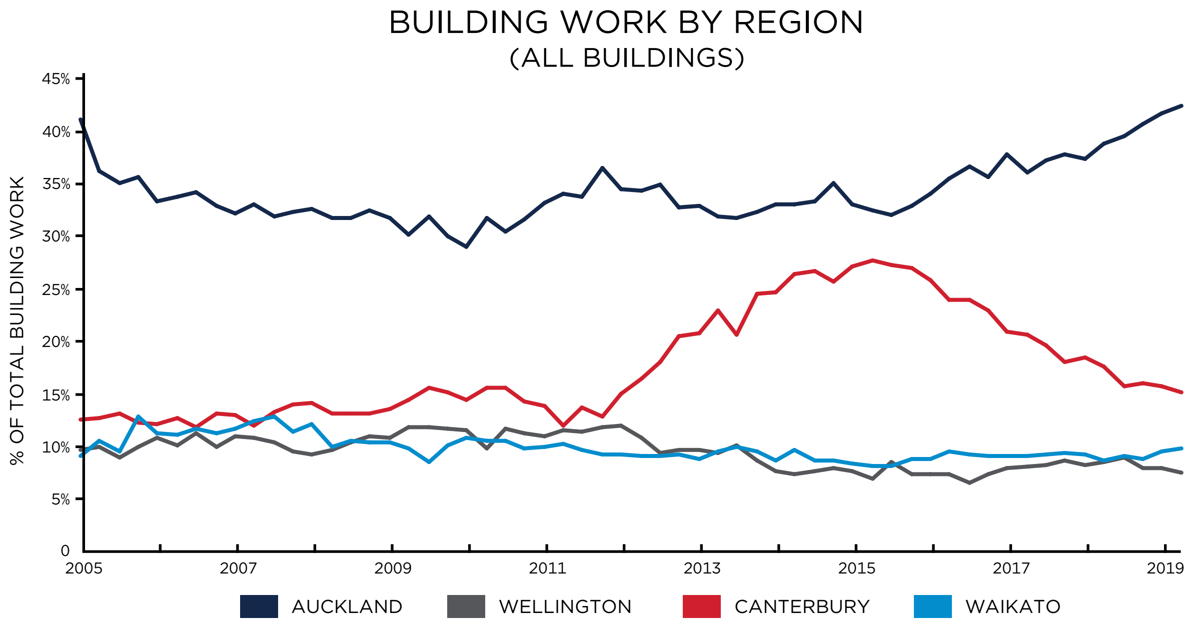
Auckland continued to lead the way in growth in non-residential construction demand over the past year, followed by Waikato and then Wellington.

Growth in Auckland non-residential construction issuance reflected stronger demand for retail outlets, storage buildings and hotels over the past year. Increased demand for storage buildings was also a key driver of growth in non-residential construction consent issuance in Waikato over the past year. In Wellington, demand was more mixed. While there was increased demand for social buildings and office space, this was partly offset by reduced demand for hotels.

FIGURE 3

Construction continues to be dominated by Auckland

% of total building work per quarter, by value each quarter

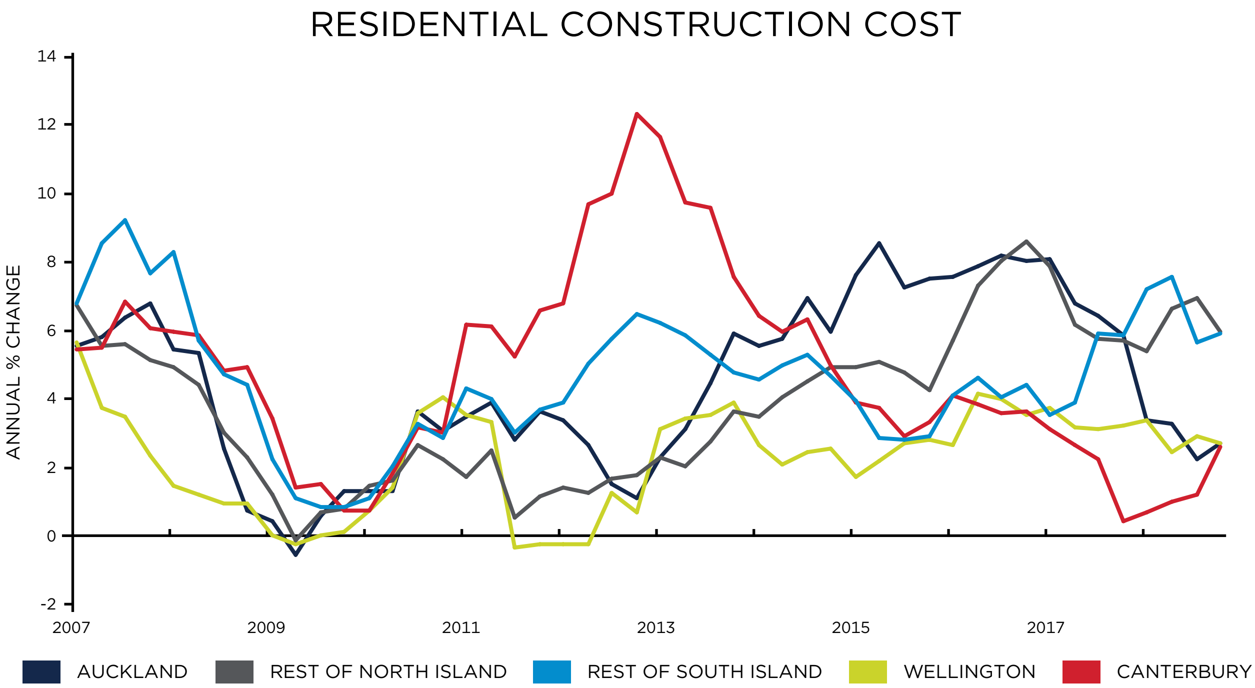


Source: Statistics NZ

FIGURE 4

Construction cost inflation moderating in the major regions

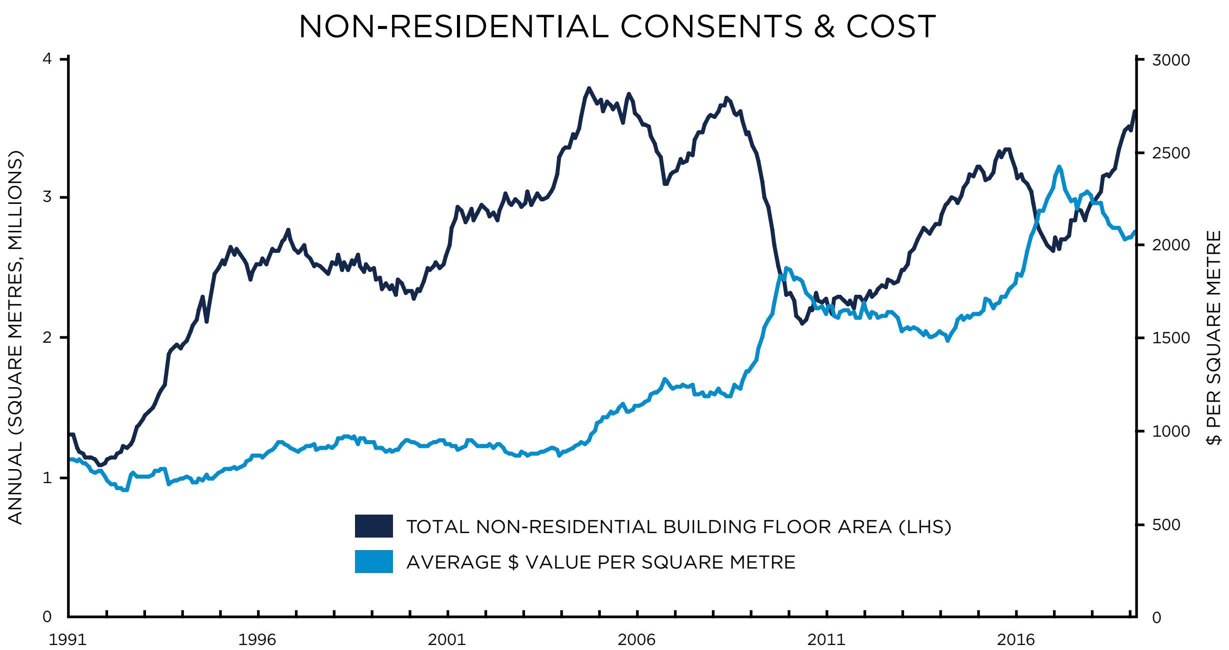
Annual % change



Source: Statistics NZ

FIGURE 5

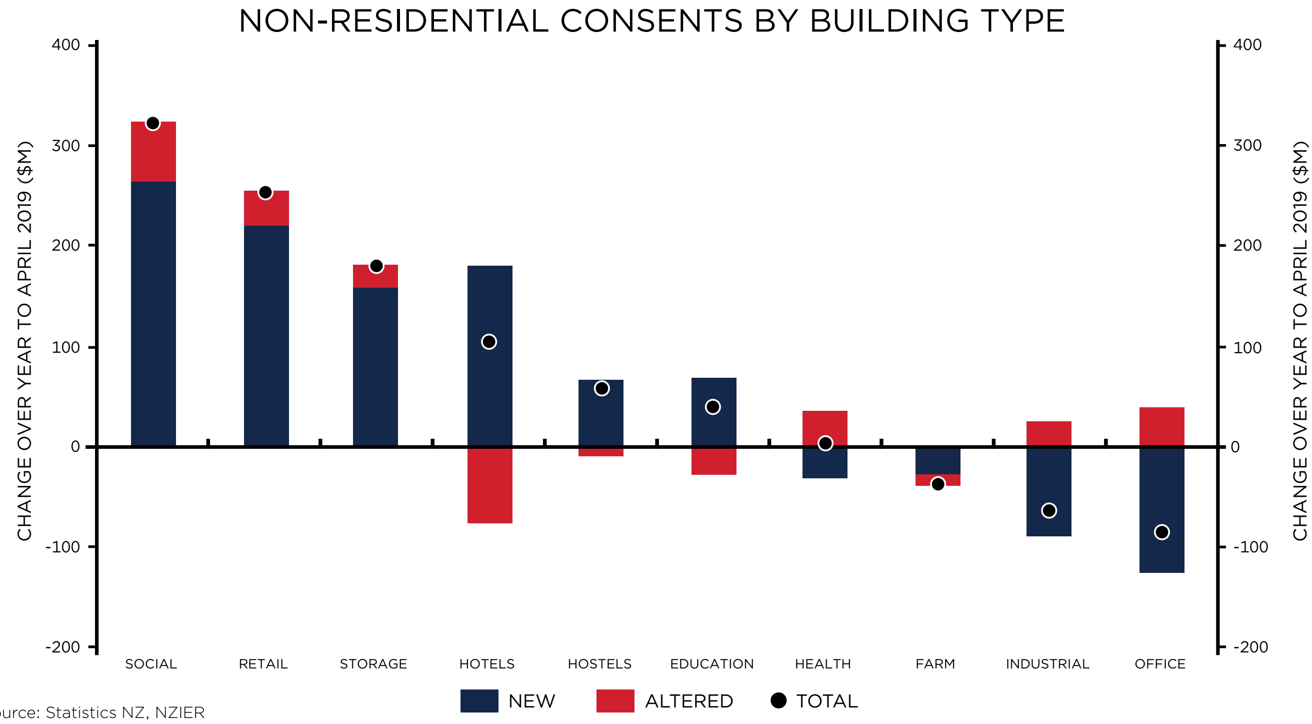
Non-residential construction demand picking up



Source: Statistics NZ, NZIER

FIGURE 6

Demand for social buildings drive non-residential construction demand



Source: Statistics NZ, NZIER

TABLE 1

Non-residential building consents by region and sector

$m of consents for the year ending April 2019; red colour shading for decline in consents from previous year

	SECTOR									
REGION	HOSTELS, PRISONS ETC	ACCOMODATION	HEALTH	EDUCATION	SOCIAL, CULTURAL, RELIGIOUS	RETAIL	OFFICE	STORAGE	INDUSTRIAL	FARM
NORTHLAND	1.9	10.7	12.9	30.8	24.4	21.7	12.1	12.7	15.9	19.0
AUCKLAND	102.7	220.9	155.1	465.4	318.6	624.9	407.4	479.9	247.7	33.6
WAIKATO	36.7	27.2	53.2	59.1	56.7	57.1	59.9	85.7	114.1	100.2
BAY OF PLENTY	0.2	24.3	69.7	35.6	33.5	107.2	41.5	94.8	45.1	13.9
GISBORNE	0.1	1.1	0.1	9.2	3.8	1.3	2.7	0.9	2.1	2.4
HAWKE'S BAY	7.3	5.9	25.1	6.6	15.6	14.0	35.7	21.2	15.8	7.4
TARANAKI	0.0	3.2	2.9	14.5	8.1	11.6	27.9	11.0	17.1	16.9
MANAWATU-WANGANUI	4.5	1.2	3.7	27.6	18.7	7.1	37.4	20.5	22.1	19.7
WELLINGTON	6.5	6.9	57.7	67.0	136.7	42.9	146.9	24.7	57.3	9.2
NELSON	0.0	0.1	30.2	5.3	1.1	4.6	4.5	5.0	4.0	0.1
TASMAN	0.7	6.1	0.7	6.6	1.4	2.9	3.4	6.8	8.3	1.9
MARLBOROUGH	0.7	0.0	0.2	3.0	6.0	11.2	0.6	2.0	10.8	6.7
WEST COAST	0.0	1.9	1.4	2.2	2.5	1.6	2.7	0.5	9.3	5.0
CANTERBURY	68.2	59.9	66.0	343.8	407.5	172.4	132.0	210.6	73.0	48.6
OTAGO	6.2	93.2	21.0	62.6	17.3	45.2	30.5	18.0	40.2	24.1
SOUTHLAND	1.0	2.5	1.2	4.6	5.1	24.6	3.0	7.5	18.0	9.6

Source: Statistics NZ, NZIER

Ngā Wai Hono – AUT University, Auckland

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 2019 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 ease below 4 percent in over the second half of 2019 before moderating to just over 3 percent by the end of 2023.

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
2014	MARCH	1415	0.8	3.7
	JUNE	1432	1.2	4.4
	SEPTEMBER	1444	0.8	4.3
	DECEMBER	1460	1.1	4.0
2015	MARCH	1474	1.0	4.2
	JUNE	1484	0.7	3.6
	SEPTEMBER	1498	0.9	3.7
	DECEMBER	1507	0.6	3.2
2016	MARCH	1519	0.8	3.1
	JUNE	1533	0.9	3.3
	SEPTEMBER	1553	1.3	3.7
	DECEMBER	1591	2.4	5.6
2017	MARCH	1601	0.6	5.4
	JUNE	1618	1.1	5.5
	SEPTEMBER	1635	1.1	5.3
	DECEMBER	1656	1.3	4.1
2018	MARCH	1670	0.8	4.3
	JUNE	1689	1.1	4.4
	SEPTEMBER	1711	1.3	4.6
	DECEMBER	1731	1.2	4.5
2019	MARCH	1747	0.9	4.6
	JUNE	1762	0.8	4.3
	SEPTEMBER	1777	0.9	3.8
	DECEMBER	1793	0.9	3.6
2020	MARCH	1808	0.9	3.5
	JUNE	1823	0.9	3.5
	SEPTEMBER	1839	0.9	3.5
	DECEMBER	1855	0.9	3.5
2021	MARCH	1871	0.9	3.5
	JUNE	1888	0.9	3.5
	SEPTEMBER	1904	0.9	3.5
	DECEMBER	1921	0.9	3.6
2022	MARCH	1937	0.8	3.5
	JUNE	1953	0.8	3.4
	SEPTEMBER	1969	0.8	3.4
	DECEMBER	1984	0.8	3.3
2023	MARCH	2000	0.8	3.3
	JUNE	2016	0.8	3.2
	SEPTEMBER	2032	0.8	3.2
	DECEMBER	2046	0.7	3.1

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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