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Chongqing
Dalian
Guangzhou
Guiyang
Haikou
Hangzhou
Hong Kong
Macau
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INDEPENDENT CONSULTANTS LOCAL KNOWLEDGE AND EXPERTISE GLOBAL NETWORK

RIDER LEVETT BUCKNALL
Rider Levett Bucknall is an independent, global property consultancy, providing advice focused on the cost, quality and sustainability of the built environment. It has over 3,500 staff operating from more than 120 global offices.

The firm’s philosophy is to combine global best practice with local know-how, utilising the latest cost data and innovations to deliver full property solutions for clients across a number of sectors. Services provided include Cost Consultancy and Advisory.

FORECAST 79
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

AUCKLAND LEADING THE WAY IN CONSTRUCTION GROWTH
Construction demand has strengthened across both residential and non-residential sectors, led by Auckland.

HOUSING DEMAND CONTINUES TO RISE, BOOSTED BY POPULATION GROWTH
Net migration continues to surge, with housing demand broadening beyond Auckland.

STRONG PIPELINE OF NON-RESIDENTIAL CONSTRUCTION AHEAD
Non-residential construction growth is strong as population growth support new education building, retail developments and office construction.

INTEREST RATES CUT, WITH MORE TO COME
The Reserve Bank surprised markets by cutting interest rates in March, and indicated the OCR would likely be reduced further. We expect another OCR cut by the middle of this year.

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Building activity continued to strengthen in the December 2015 quarter, and a solid pipeline of activity points to further growth over the next few years. Demand across both residential and non-residential activity is strong, buoyed by migration-led population growth and low interest rates.

Auckland continues to lead the way, with construction ramping up following a lull over the first half of 2015. Relatively strong population growth in the region is driving construction demand across many sectors. Strong activity is reflected in a lift in concrete sales in Auckland.

In contrast, construction activity in Canterbury is easing from high levels as the residential part of the earthquake rebuild programme wraps up. House-building is slowing but non-residential construction remains high with further growth likely.

Net migration has surged to new record highs of over 65,000 in the year to December 2015, with the bulk of new arrivals settling in Auckland. This strong population growth is boosting housing demand in Auckland. Demand to build stand-alone houses remains very strong, but over the past year there has been growing demand to build apartments. Housing demand is also increasing in many regions outside of Auckland.

High house prices and new rules limiting lending to Auckland property investors (from last November), are contributing to increased interest in housing in other regions particularly Waikato and the Bay of Plenty. Strengthening tourism activity is also injecting income into many regional economies, which in turn is improving employment opportunities. As a result, tourism-intensive regions are seeing relatively strong housing demand.

Auckland is leading the way in non-residential construction demand, with a jump in non-residential consents issued in the region in recent months. Rising demand in the services industries is supporting increased demand for accommodation, retail outlets and office buildings in the region. Prime office vacancies have fallen to historically low levels, and a lift in rents is encouraging the development of new office buildings.

Non-residential construction demand in the other regions has eased slightly, with consents issued in Canterbury dipping in more recent months following a jump in the third quarter of 2015. Weaker demand for farm and industrial buildings is weighing on non-residential construction in regions outside of Auckland, largely reflecting farmers paring back on spending in the wake of continued weakness in global dairy prices.

**FIGURE 1**
BUILDING ACTIVITY RAMPS UP IN AUCKLAND BUT EASES IN CANTERBURY

![Concrete Sales Graph](source: Statistics NZ, NZIER)
FIGURE 2
LIFT IN PLANS FOR STAND-ALONE HOUSES AND APARTMENTS AS POPULATION CONTINUES TO GROW

Source: Statistics NZ, NZIER

FIGURE 3
A SURGE IN PLANS FOR NON-RESIDENTIAL CONSTRUCTION IN AUCKLAND

Source: Statistics NZ, NZIER
ECONOMIC BACKDROP
The New Zealand economy picked up over the second half of 2015, with solid momentum going into 2016. Both consumer and business confidence are improving, with households and firms showing a greater willingness to spend. Strong population growth, construction and tourism will be the key supports for New Zealand economic growth over the coming years. The dairy sector remains in the doldrums with global dairy prices taking much longer than expected to recover. However, there are signs the New Zealand economy is diversifying to a wider range of export goods and services. A particular highlight is tourism, which last year overtook dairy as our top export earner.

However, heightened uncertainty over the global outlook and continued weakness in global dairy prices present downside risks to the growth outlook. The effects of weaker dairy income returns are reverberating through the economy as farmers pare back on investment in farm buildings and equipment. We expect continued reduction in on-farm spending by dairy farmers will weigh on business investment over 2016 and 2017.

INTEREST AND EXCHANGE RATES
The Reserve Bank surprised markets by cutting the Official Cash Rate (OCR) to 2.25% in March, citing its concern that expectations of continued low inflation are becoming entrenched. Despite a pick-up in economic activity, annual inflation was just 0.1% for the 2015 – well below the Reserve Bank’s 1-3% inflation target band. Nonetheless, the OCR cut was a surprise given the Reserve Bank had earlier in the year highlighted the growing financial stability risks from monetary policy being too loose. With house price inflation broadening beyond Auckland and signs households are building up debt the risk of a sharp correction in the housing market remains acute.

The Reserve Bank has indicated further easing is likely given its focus on returning headline inflation to the 2% mid-point of its inflation target band. We expect another OCR cut by the middle of this year. Markets are speculating on the potential for the OCR to be cut below 2% in the wake of the Reserve Bank’s surprise OCR cut in March.

The New Zealand dollar fell sharply on the surprise move by the Reserve Bank, but has rebounded since then on stronger than expected New Zealand GDP data and more recent indications from the Federal Reserve that US interest rate increases are likely to be more gradual than it had expected last year. While we see potential for further limited appreciation in the New Zealand dollar over the first half of 2016 given the relatively strong performance of the New Zealand economy, the currency is likely to ease over the coming years as other economies begin to pick up.

BUILDING INVESTMENT
Demand for non-residential construction is strengthening, with a solid pipeline of work for the coming years. Strong population growth is driving demand for new education and commercial buildings.

BUILDING CONSENTS
Non-residential building consent issuance has continued to lift since late 2015 suggesting a pick-up in non-residential construction growth over 2016. Growth in non-residential construction had been subdued in 2015 reflecting caution amongst businesses, but demand is rising as confidence improves.

We expect solid growth in non-residential construction over the coming years, despite farmers reining in spending on investment including on farm buildings. We expect further growth in professional and business services will underpin the development of new office buildings as well as upgrades of existing office space.

We also expect tourism-related construction and infrastructure spending will pick up over the next decade. Auckland Airport recently brought forward plans to expand its terminal capacities by several years, and the falling vacancy rates in tourism hot spots have seen interest in the development of new four and five star hotels.

BUILDING ACTIVITY OUTLOOK
BUILDING CONSENTS BY SECTOR
Education buildings, storage buildings and healthcare facilities were the top three drivers of growth in non-residential issuance over the past year. The increase in education construction reflects both new buildings and alterations.

The majority of non-residential consents, in all sectors, issued over the past year continues to be for new building construction rather than alterations.

The effects of the dairy downturn continue to be felt in weaker demand for farm and industrial buildings. Farmers are reining in spending given reduced dairy farm income, and uncertainty over when dairy prices will recover back to more sustainable levels.

Strengthening of household spending is driving construction of new retail outlets. Despite some challenges facing the retail sector, there is increasing interest amongst the big brands such as H&M and Zara to set up shop in the urban areas in New Zealand.

Strong population growth continues to underpin many of the longer-term trends:
• New office buildings to accommodate the higher number of workers.
• Public sector spending on education buildings, along with rebuilding activity.
• Domestic demand for accommodation, on top of increased overseas tourists, should drive demand for new accommodation buildings.

FIGURE 4
NON-RESIDENTIAL CONSTRUCTION HAS BEEN SLOW TO PICK UP, BUT STRONG DEMAND EXPECTED OVER COMING YEARS

Source: Statistics NZ, NZIER
BUILDING CONSENTS BY REGION

The divergence between rural and urban conditions is reflected in non-residential consent issuance across the regions over the past year. Regions exposed to the dairy sector have felt the effects of reduced farm income, with declines in non-residential consent issuance in Southland and Taranaki over the past year.

In contrast, regions in which tourism makes up a substantial part of their economy have seen solid growth in non-residential consent issuance over the past year. Strong tourism activity is injecting income into many of these regions, with demand improving across a broad range of sectors. Non-residential consent issuance has increased in many regions including Bay of Plenty and Otago over the past year, reflecting increased demand for hotel developments and retail outlets.

Auckland is also seeing a pick-up in non-residential consent issuance, reflecting higher demand for accommodation, retail outlets and office buildings. More recently, Auckland has bucked the national trend with stronger demand for factories and industrial buildings.

Although the residential part of the earthquake rebuild is wrapping up, non-residential rebuilding is gathering pace in Canterbury. There has been particularly strong growth in consent issuance for education buildings in the region over the past year. We expect the level of non-residential construction will remain high in Canterbury in the next few years.

Non-residential building demand continues to broaden beyond Auckland and Canterbury (see Figure 6). Regions such as Otago and Hawke’s Bay are benefitting from strong tourism activity, which is boosting demand for new hotels and motels. Meanwhile, demand for new retail and office space is driving growth in Marlborough.

In contrast, the effects of reduced dairy farm income are apparent in slowing non-residential demand in dairy-intensive regions such as Southland and Taranaki. As the farming sector hunkers down in the face of a consecutive second season of low dairy prices, demand for retail outlets and farm buildings has slowed in these regions.

FIGURE 5

STRONG POPULATION GROWTH DRIVE NON-RESIDENTIAL CONSTRUCTION DEMAND

Source: Statistics NZ, NZIER
FIGURE 6
NON-RESIDENTIAL CONSENTS GROWTH

JANUARY 2016 YEAR COMPARED WITH JANUARY 2015 YEAR, AAPC

-30.9%  41.5%

NORTHLAND
-1.0%

TARANAKI
-19.9%

MANAWATU/WANGANUI
-30.9%

NELSON
-7.2%

WEST COAST
29.8%

SOUTHLAND
-25.0%

AUCKLAND
19.6%

WAIKATO
4.2%

BAY OF PLENTY
36.0%

GISBORNE
41.5%

HAWKE’S BAY
15.4%

WELLINGTON
16.8%

MARLBOROUGH
36.5%

CANTERBURY
16.5%

OTAGO
18.8%

Source: Statistics NZ
TABLE 1
NON-RESIDENTIAL BUILDING CONSENTS BY REGION AND SECTOR

$M OF CONSENTS FOR THE YEAR ENDING OCTOBER 2015;
RED COLOUR SHADING FOR DECLINE IN CONSENTS FROM PREVIOUS YEAR

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<th>SECTOR</th>
<th>NORTHLAND</th>
<th>AUCKLAND</th>
<th>WAIKATO</th>
<th>BAY OF PLENTY</th>
<th>GISBORNE</th>
<th>HAWKE'S BAY</th>
<th>Taranaki</th>
<th>MANAWATU-Wanganui</th>
<th>WELLINGTON</th>
<th>NELSON</th>
<th>TASMAN</th>
<th>MARLBOROUGH</th>
<th>WEST COAST</th>
<th>CANTERBURY</th>
<th>OTAGO</th>
<th>SOUTHLAND</th>
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Source: Statistics NZ, NZIER
The Capital Goods Price Index for Non-Residential Buildings (CGPI-NRB) provides an official measure of cost movements in the sector. The CGPI-NRB excludes GST. The rate of increase in the CGPI-NRB can be used as an indicator of cost escalation.

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

Construction costs increases have eased more recently following solid growth over 2014, but there are differences across the regions. While resource and capacity constraints have eased in Canterbury, they are more acute in Auckland.

NZIER forecasts construction cost inflation to average just below 4% a year over the next three years. This will be the highest sustained inflation in the sector since the construction boom of the mid-2000s. NZIER does not expect the inflation to be as high as the mid-2000s given 1) the low inflation environment limits the extent to which rising costs can be passed on, and 2) strong net migration is helping to mitigate skills shortages in the building sector.

In a sign that labour shortages are easing, labour cost inflation in the construction sector has moderated more recently.

**FIGURE 7**

NON-RESIDENTIAL BUILDING COST ESCALATION

Source: Statistics NZ, NZIER forecasts
### TABLE 2
NON-RESIDENTIAL BUILDING COST INDEX

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

Source: Statistics NZ, NZIER forecasts
For further information please contact Grant Watkins +64 4 384 9198 or your nearest Rider Levett Bucknall office.

New Zealand

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<tr>
<td>Christchurch</td>
<td>+64 3 354 6873</td>
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<tr>
<td>Hamilton</td>
<td>+64 7 839 1306</td>
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<td>Palmerston North</td>
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<td>Wellington</td>
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