Infometrics
Economics put simply
construction update
BCITO He Hunga Hanga Mātou building people | Te Pūkenga
November 2023

Soft landing for economy, but interest rate cuts still a year away

	Latest	Dec 2024	Dec 2025
Gross domestic product[(1)]	3.3%	1.1%	1.4%
Residential consents[(1)]	-20.4%	-12.1%	-14.4%
Non-residential consents[(1)]	3.9%	-1.2%	4.9%
House prices[(2)]	-4.8%	3.8%	3.5%
Unemployment rate[(3)]	3.9%	4.9%	4.8%
Net migration[(4)]	110,244	25,107	25,349

(1) Year-end % change (2) Three-month annual % change
(3) Quarterly level, seasonally adjusted (4) Annual total
Data source: Statistics NZ, Infometrics forecasts

Recent data suggests the Reserve Bank is successfully engineering a soft landing for the New Zealand economy. Inflation slowed from 6.0% to 5.6%pa in the September quarter, despite a 17% jump in petrol prices over the quarter. The labour market is finally showing definite signs of easing, with lower job numbers and the unemployment rate climbing to a two-year high of 3.9%. Yet economic growth in June was reasonably positive, at 0.9% for the quarter, even if that figure was partly a bounce-back from March's result that was negatively affected by weather. Most forecasters do not expect the official cash rate to be lifted beyond its current level of 5.5%, but financial markets remain concerned about the potential for inflation to hang around for longer, both internationally and domestically. As a result, longer-term wholesale interest rates have continued to trend upwards, suggesting that any cuts to the official cash rate might not occur until late 2024. Until then, economic growth is likely to remain patchy, with the positive effects of high migration counterbalanced by downward pressure on export prices and the continued squeeze on household budgets.

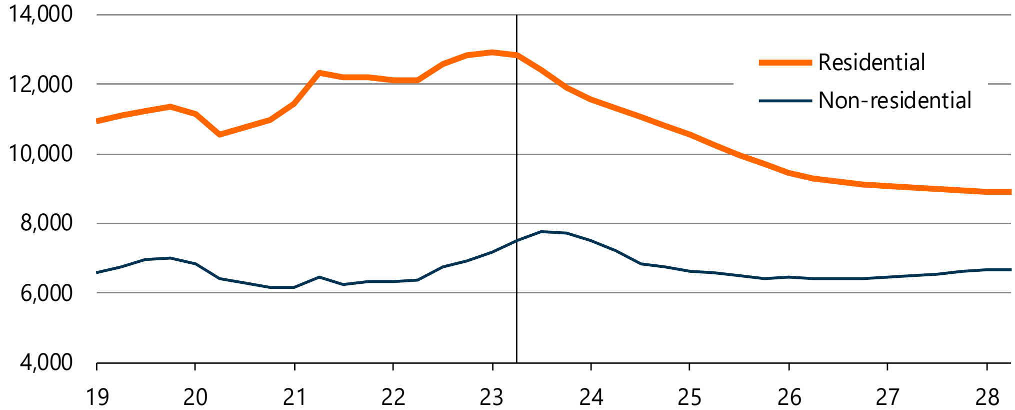
Construction downturn to gather speed during 2024

Residential consent numbers in the September quarter were down 31% from a year earlier, the fastest rate of decline since 2009. The fall in standalone house numbers that has been underway since the start of 2022 is being joined by increasingly sharp declines in attached dwelling consents, although townhouse consents are still only down 14% from a year ago. We forecast that total consent numbers will fall from 40,408 in the year to September to around 34,000pa at the end of 2024.

Residential work put in place has started to ease, but the 7.6% decline in quarterly activity levels since September last year is still modest compared to the fall in consents. Building materials firms are generally reporting solid sales levels, with the backlog of consents awaiting completion keeping demand relatively buoyant. However, by the end of 2025, annual work put in place is forecast to be down 25% from its peak in early 2023.

After adjusting for building cost inflation, the volume of non-residential consents is now falling for the first time in 2½ years. Non-residential work put in place is forecast to peak by the end of 2023, with higher interest rates and weaker economic growth weighing on private sector investment. Lower levels of storage and accommodation building will contribute to the forecast decline in activity during 2024, and public sector activity is also set to pull back from its current highs.

Building work put in place
Annual running totals, 2009/10 $m



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New government policies will affect construction, but only slowly

The voters' choice of a National-led government at last month's election is likely to see a range of policy changes affecting the construction industry. Noting that the coalition arrangements and policy priorities between National, ACT, and NZ First have yet to be thrashed out, we profile several possible changes that could have implications for construction activity.

The most significant policy change in the near-term is likely to be the reversal of the financial restrictions placed on residential property investors by Labour in 2021. These expected changes include the reintroduction of tax deductibility for mortgage interest, reduction in the bright-line test from 10 years to two years, and the likely removal of several restrictions around tenancies and rent reviews. Even ahead of these election, the prospect of these changes has reportedly boosted investor interest in housing, pushing up sales volumes and contributing to the moderate increase in house prices over the last few months. Alongside the effects of strong net migration, this increased demand from investors is likely to drive a continued upturn in the housing market throughout 2024.

This pick-up in the housing market might normally be expected to flow through into increased demand for new homes. However, the implied removal of the tax wedge for investors between new and existing homes could see a shift in investor demand back towards existing homes outweigh the positive effects for residential construction. We believe that demand over the last two years for new townhouses and terraced housing, in particular, has been higher than normal due to the incentives that have steered investors towards new builds.

With an eye on housing affordability, National is also keen to improve the supply of housing through various regulatory changes. Having removed its support for the Medium Density Residential Standards, National is now focused on reducing zoning restrictions and streamlining the resource consent process. It campaigned on repealing Labour's replacements for the Resource Management Act, the National and Built Environments Act and the Spatial Planning Act, and is now focused on preparing its own legislation to reduce the impediments preventing new developments from going ahead.

National will also aim to facilitate growth in the housing stock by providing additional funding options for infrastructure. The limited ability to fund or construct necessary infrastructure has been seen as a key factor limiting the supply of new housing and contributing to higher land and house prices. The presence of NZ First in the governing arrangements could result in an increased proportion of funding available for projects outside the main urban areas.

A perceived lack of delivery associated with flagship policies under Labour is also likely to focus the new government to ensure progress on major new infrastructure projects. National's emphasis on roading is likely to change the mix of infrastructure activity, although public transport and rail will remain significant parts of the overall infrastructure picture. We expect increased levels of infrastructure activity, both relative to current levels and previous forecasts, from 2025 onwards.

Further change is expected in the vocational education and training area, continuing the upheaval of the last few years. National campaigned on reversing the creation of Te Pūkenga and returning to regionally administered polytechnics, and ACT is looking to abolish the Workforce Development Councils. Encouragingly for the construction industry, National has pledged to continue to support building and construction apprenticeships. Whether this support extends to any extension of the Apprenticeship Boost scheme, which is currently in place until the end of 2024, remains to be seen.

In summary, we expect more favourable conditions for residential and infrastructure activity over the medium term. However, weaker economic conditions remain the key determinant of our forecasts of activity during 2024 and 2025, particularly for residential construction. It will take time for regulatory changes facilitating more residential development to pass through Parliament, and even longer for those changes to translate into actual increases in construction activity. For the supply of new housing in particular, it is likely to be 2026 before the new government's policies start to affect consents.