



THE BUILDING BAROMETER **Sample Report**

AN INVALUABLE RISK MANAGEMENT TOOL

The Building Barometer is a monthly report that supplies invaluable insights into the outlook for residential building activity at the national level and provides some regional insights. It contains tried-and-true leading indicator analysis that is accompanied by plain English explanations, and it has a bit of fun along the way.

The report contains our near-term forecasts for the national number of new dwelling consents, focused on the next three quarters and based on tried-and-true leading indicator analysis. And it contains our medium-term forecasts that cover the next two years that are based on rigorous and insightful analysis of the key drivers of residential building, especially interest rates and migration. Our forecasting framework is not only much more reliable than the traditional “black-box” models used by economists, but also helps subscribers better understand what drives residential building activity.

The Building Barometer also delivers analysis of the outlooks for apartment building, and alterations and additions. It provides tables containing historical data for residential building consents and colour-coded charts highlighting the regional winners and losers.

This **Sample Report** explains the contents and analysis within our **Building Barometer** reports. On reading this sample report you will soon realise that this is not another economic report filled with the half-baked ideas of an economist! The quality of our analysis is matched by none and will provide you with a valuable tool in your business risk management strategy.

Of course, forecasting the future is an art not a science, so even armed with the best analytical techniques in the world we will not always get it right. Who knows when “nuclear bombs” might start falling on Chicken Licken’s head. However, we can confidently assert that our track record in our specialist areas is matched by none, while in the event of a major shock we will issue a **Special Report** to help clients negotiate the chaos.



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RESIDENTIAL BUILDING PROSPECTS

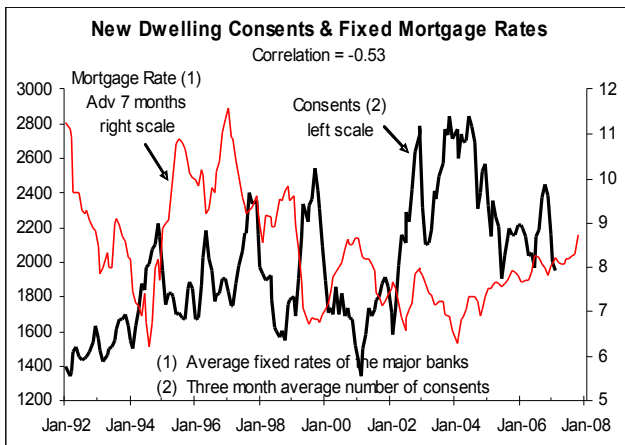
Our leading indicator chart analysis provides superior near-term forecasting ability

Interest rates and migration can explain all of the material increases and falls in the national number of consents for new dwellings. Our leading indicator chart analysis shows you exactly how interest rates and net migration impact on consents. These charts provide a reliable framework for forecasting consents over the next three quarters.

The top chart shows the impact of mortgage interest rates on consents. The **Building Barometer** reports have this chart and the equivalent chart that shows the impact of migration on consents.

The black line in the chart is the monthly number of national consents for new dwellings (the left scale), although we use a three-month average of the monthly numbers to smooth out volatility in the monthly numbers. The red line is an average of the various fixed mortgage rates charged by the major banks (the right scale). A distinct inverse relationship between interest rates and consents is evident in the chart, but interest rates are not the only driver and in the reports we also take into account the impact of migration, as well as the general state of the economy.

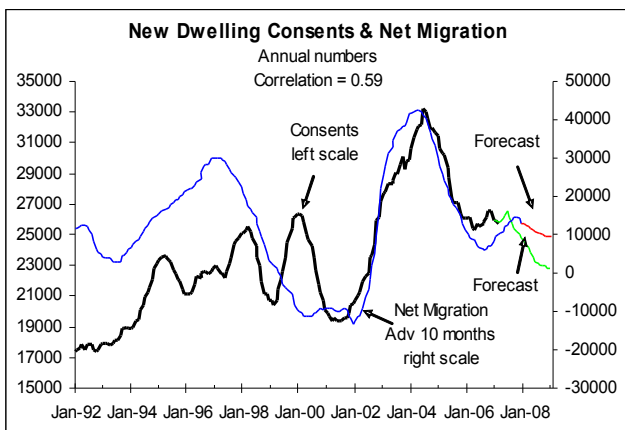
The best fit between the two lines in the top chart is with the red interest rate line advanced or shifted to the right by seven months, which reflects how long it takes for changes in interest rates to impact on consents. As the chart shows, by shifting the interest rate line to the right it provides a lead on what will happen to consents over the next seven months (e.g. the recent rise in interest rates points to a fall in consents roughly seven months hence).



We also check other leading indicators to see if the near-term outlook for consents predicted by interest rates and migration is unfolding. For example, while it takes seven months on average for changes in mortgage interest rates to impact on consent numbers it only takes three months on average for interest rates to impact on existing house sales. This is because there is a much longer planning lag in preparing to take out a consent (e.g. finding a section, getting plans drawn up) than there is in buying an existing house. Consequently, movements in existing house sales generally provide us with around four months forewarning of changes in consent numbers.

Our medium-term forecasts are well-founded on interest rate and migration prospects

It is not uncommon for economists to forecast falling residential building consents on the back of predictions of falling interest rates. This will sound strange, even unbelievable, but one of the things we supply in the **Building Barometer** reports is a critique of what the economists are predicting for residential building activity, and these critiques frequently reveal that the economists are up to such silly things.



Our predictions for residential consents over the next three quarters are founded on our reliable leading indicator charts, but to predict further into the future we have to input our views on the outlook for interest rates and net migration.

The chart shows the impact of annual net migration (the blue line and right scale) on the annual number of consents for new dwellings (the black line and left scale). The best fit is with net migration advanced or shifted to the right by ten months. The upturn in net migration over most of the last ten months will have a favourable impact on consents over the next ten months, although the interest rate impact also needs to be taken into account.

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The bottom chart on the previous page shows how our predictions for net migration (the red line) feed into our predictions for annual consent numbers over the next two years (the green line). However, our forecasts for consents are also shaped by our interest rate forecasts and our assessment of how other factors will impact on residential building activity (e.g. the state of the labour market, whether there have been too many or too few spec houses built).

The **Building Barometer** reports contain a table of our two-year-ahead forecasts for the annual number of new dwelling consents (see below), and a summary of our analysis of interest rates prospects. The full analysis of interest rate prospects is contained in our **Interesting Times** reports (visit our website – www.sra.co.nz for a sample). The **Building Barometer** reports also contain our leading indicator analysis of the outlook for both immigration and emigration. This analysis greatly assists us in feeding better quality predictions for net migration into our residential building forecasts.

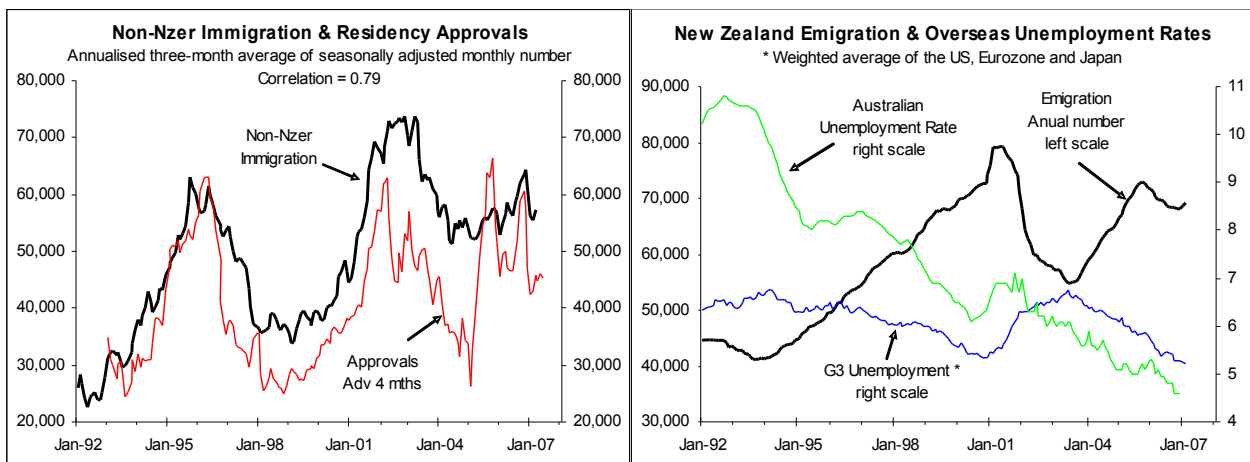
Annual Consents for New Dwellings

	Number	Ann % change
Mar-04	31,823	12.4
Jun-04	33,251	14.4
Sep-04	31,864	5.7
Dec-04	31,423	5.0
Mar-05	30,255	-4.9
Jun-05	27,444	-17.5
Sep-05	27,092	-15.0
Dec-05	26,023	-17.2
Mar-06	25,406	-16.0
Jun-06	25,563	-6.9
Sep-06	26,101	-3.7
Dec-06	25,952	-0.3
Mar-07 F	25,799	1.5
Jun-07 F	26,519	3.7
Sep-07 F	25,392	-2.7
Dec-07 F	24,750	-4.6
Mar-08 F	24,150	-6.4
Jun-08 F	23,250	-12.3
Sep-08 F	22,950	-9.6
Dec-08 F	22,800	-7.9

Source: Statistics New Zealand (www.snz.govt.nz)
F Strategic Risk Analysis Limited forecasts

THE OUTLOOK FOR MIGRATION

The **Building Barometer** reports analysis the outlook for immigration and emigration. Key to the major cycles in immigration is what the government does with new residency approvals, with cycles in foreign immigrants swamping cycles in Kiwis returning from doing their OE. Key to emigration is the state of the Australian and international labour market.



The left chart above shows that the best fit between the number of new residency approvals for immigrants (the red line) and immigration numbers of non-Kiwis is with the approvals line being advanced or shifted to the right by four months. This chart will generally give us a warning four months prior to major changes in immigration, while the immigration numbers give us another ten month lead on consents. When we

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combine the leading indicator charts and analysis we use we can have an informed view on the outlook for residential building – as opposed to the half-baked views often expressed by economists and other commentators – for more than the next year.

The right chart on the previous page shows that when the unemployment rate falls in Australia and in the major countries then more people generally leave New Zealand on a permanent or long-term basis (largely reflecting Kiwis heading overseas to do OE). While when the unemployment rate rises overseas New Zealand’s emigration numbers generally fall. The **Building Barometer** reports have leading indicators of global growth which give advance warnings of prospects for the global labour market, which in turn gives a lead on major emigration cycles.

THE RESIDENTIAL SECTION MARKET

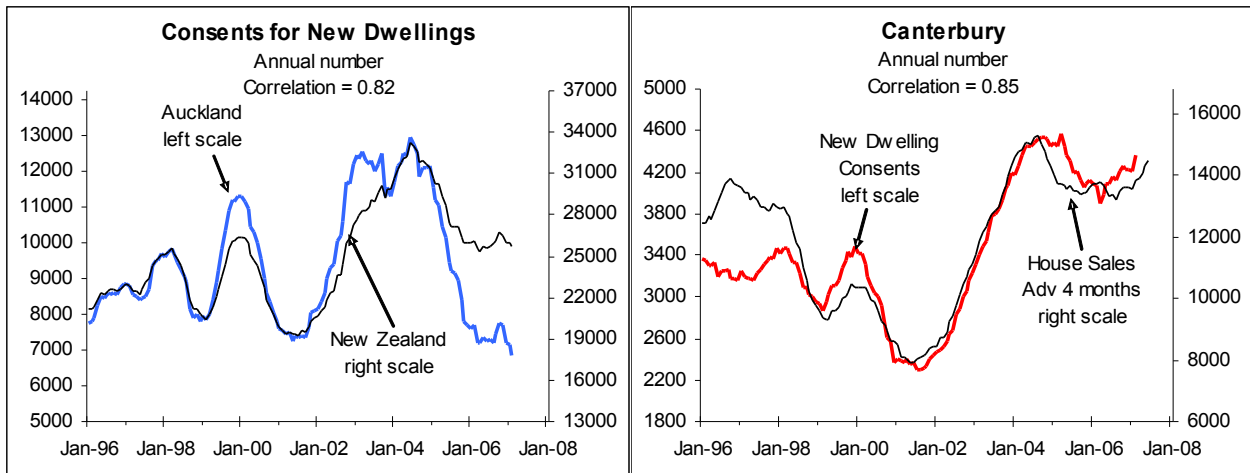
The same analysis we use to predict the near-term outlook for residential building activity is used to predict the near-term outlook for national section sales and section prices. We also look at the affordability of sections relative to existing houses and relative to income levels.

APARTMENTS, ALTERATIONS & ADDITIONS AND FLOOR AREA

Leading indicator charts show the impact of interest rates and immigration on apartment consent numbers. We look at the states of the rental market for apartments and the secondary market for apartment sales in the major centres to help assess construction prospects for apartments. We also assess the outlook for alteration and additions, as well as for the average size of houses being built.

REGIONAL CONSENTS

The **Building Barometer** contains regional charts that show, in easy to see regional colours, how consents for each region are travelling relative to the national market. There are also charts for each region showing consents relative to existing house sales in the first instance and secondly consents relative to section sales. Examples of the charts are shown below. The report contains tables showing a regional breakdown of consents and various other breakdowns of the national consent numbers.



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