

UHERO Annual Hawai'i Construction Forecast:
Construction Downturn Milder than Mainland

by

Carl S. Bonham
UHERO

Paul Brewbaker
Bank of Hawaii

Research assistance by
Heber Moulton and Sean D'Evelyn

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University of Hawaii
Economic Research Organization

2424 Maile Way, Room 542

Honolulu, Hawai'i 96822

(808) 956-7605

uhero@hawaii.edu



**University of
Hawai'i
Economic
Research
Organization**

EXECUTIVE SUMMARY

Key Changes in This Forecast

Compared with our Annual Hawaii Construction Forecast released in September, 2007, we have lowered our home price forecast by about \$17,000 in 2008 and roughly \$62,000 in 2009.

We expect total real permits to decline 8.4% in 2008, 2.6% more rapidly than reported last year.

Hawai'i's construction sector is now on the downward side of the cycle, but slowing continues to be considerably more moderate than in many U.S. mainland markets. The current business cycle slowdown, increased land and construction costs (mostly due to a surge in commodity prices), together with tighter credit conditions present challenges for new construction in the islands. Local non-residential construction and military housing renovation projects are helping to moderate the cyclical downturn.

Compared with our 2007 Annual Construction Forecast, we have reduced our forecast for construction activity, but the changes are relatively small.

- Private new residential construction in Hawai'i is expected to remain on a downward path during 2008 and 2009 before stabilizing and mounting a gradual recovery in 2010. Real residential building permits, which declined 27% in 2006 and 5% in 2007, are expected to fall an additional 20% this year and 6% in 2009.
- We expect the median single-family resale price on O'ahu to decline by 3.6% this year, followed by a larger decline of over 5% in 2009. From a peak of \$639,500 (annual average) in 2007, O'ahu home prices are expected to fall by 9% to \$570,000 by 2010, still a relatively modest drop compared with mainland markets where in some cases prices have fallen by that much in one quarter.
- Even with the forecasted modest decline in median home prices, and relatively attractive mortgage rates, the projected slowing of median household income growth keeps housing affordability from improving very much. The Housing Affordability Index for O'ahu will rise from a low of 56.3 in 2006 to only 73.8 in 2010, so that high housing costs will remain an important problem.
- Nonresidential construction trends reflect the pinch of a softer local economy and fallout from the sub-prime financial crisis. Total nonresidential commitments to build peaked in 2006 at \$2.11 billion and have been falling gradually since then. Real private nonresidential construction commitments are expected to decline from a peak of \$2.11 billion in 2006 to a low of \$1.6 billion in 2010, a cumulative drop of only 24%.
- Despite the jump in energy costs during the first half of 2008, we expect continued deceleration in construction cost inflation over the next several years, with costs rising by 4.9% in 2008 and 4.7% in 2009 and falling to 4.3% by 2010.
- The most comprehensive measures of Hawai'i contracting activity include the contracting job count, total building authorizations (permits), and the general excise and use tax base for contracting (contracting receipts). We expect total real permits of \$4.1 billion this year, measured in 2007 dollars. This represents an 8.4% decline from 2007 activity, a bit more rapid than the 5.8% drop we predicted in our September 2007 Annual Construction Forecast. The decline in permitting is expected to continue in 2009, with total real permits declining nearly 2% before bottoming out in 2010 at roughly \$3.9 billion 2007 dollars.
- In constant-dollars, taxable contracting receipts are expected to decline by a modest 15% from a peak of \$7.86 billion in 2007 to a low of \$6.9 billion in 2011. Total Hawai'i construction spending by this measure

likely peaked during the second quarter of 2007 and is expected to decline this year with single-digit annual decreases continuing from 2008 through 2011.

- In contrast, construction payroll employment for all of 2008 will remain very close to the 2007 average of 39,000 jobs. By 2010, construction employment is expected to decline to 37,000 jobs. The downward adjustment in jobs is moderated by the large volume of ongoing military housing renovation projects.

HAWAI'I CONSTRUCTION FORECAST (SUMMARY)

	2006	2007	2008	2009	2010
Nominal GE Contracting Tax Base (Mil \$)	7,018	7,857	7,937	7,918	7,804
<i>% Change</i>	19.95	11.95	1.02	-0.24	-1.44
GE Contracting Tax Base (Mil 2007\$)	7,573	7,857	7,562	7,206	6,812
<i>% Change</i>	9.16	3.75	-3.75	-4.71	-5.46
Construction Job Count (Thou)	36.53	39.03	39.18	38.05	37.12
<i>% Change</i>	9.33	6.84	0.38	-2.89	-2.44
Construction Income (Mil 2007\$)	3,107	3,322	3,316	3,256	3,208
<i>% Change</i>	3.70	6.93	-0.20	-1.79	-1.49
Honolulu Median Home Price (Thou \$)	632.03	639.42	616.61	584.78	569.45
<i>% Change</i>	7.76	1.17	-3.57	-5.16	-2.62
Honolulu Median Condominium Price (Thou \$)	310.25	324.79	328.08	312.17	293.87
<i>% Change</i>	16.34	4.69	1.01	-4.85	-5.86
Honolulu Housing Affordability Index	56.28	57.52	65.91	69.60	73.79

* Tax base is deflated by Honolulu Construction Cost Index. Income is deflated by Honolulu CPI. Housing affordability index is the ratio of median family income to qualifying income for a loan for the median-priced home (times 100). Additional detail available to subscribers and sponsors.

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