



UHERO FORECAST PROJECT, PUBLIC SUMMARY
ANNUAL HAWAII CONSTRUCTION FORECAST:

CONSTRUCTION BEGINS TO STABILIZE

SEPTEMBER 24, 2010





UHERO

THE ECONOMIC RESEARCH ORGANIZATION
AT THE UNIVERSITY OF HAWAI'I

UHERO HAWAI'I CONSTRUCTION FORECAST

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EXECUTIVE SUMMARY

Key Changes in this Forecast

We have made a modest upward revision to our construction forecast because of evidence of stabilization in private sector building permits and our anticipation that interest rates will remain low for an extended period.

Real residential permits will rise 4.3% this year, compared with a decline of roughly 4% in our June forecasts; non-residential permits will be roughly unchanged this year, up from a nearly 15% decline seen in our previous forecast.

The near-term impact on aggregate measures of construction activity is limited. The 2010 decline in construction jobs and real income will be approximately one percentage point smaller than in our June forecast. There will be about one percentage point faster growth in 2011.

Hawaii's construction industry continues to seek a bottom to what has been a bruising downturn. Recent months have brought some encouraging news, with permitting numbers beginning to stabilize and employment losses tapering off. The home resale market appears healthier, although this can be explained in part by the now-expired Federal tax credits. At the same time, non-residential permitting remains very weak and focused on just a small number of large projects. Until private demand picks up, the industry will find its most promising support in public sector projects, which are expected to ramp up further in coming months.

- Like much of the country, Hawaii has seen a rally in home resales, with large double-digit gains in all four counties for both condos and single-family homes. This reflects in part improved affordability associated with lower housing prices and historically low mortgage interest rates. However, the now-expired Federal homebuyer tax credits almost certainly played an important role.
- Increased sales have not fully arrested a slow downward trend in home prices, but the decline has tapered off; on Oahu, they have begun to edge up. With a limited supply of housing in the Honolulu market, conditions should support gradual appreciation over the next several years. We expect Honolulu median single-family prices to rise by close to 4% this year and next, with strengthening thereafter. UHERO does not prepare numerical forecasts for the Neighbor Island housing resale market.
- The outlook for residential investment remains difficult, but we have begun to see a slight recovery in permitting activity on the Big Island and Oahu. Prospects for residential building are generally less satisfactory on the Neighbor Islands than on Oahu because of continuing weakness, pockets of overbuilding, and the lack of offshore demand. Total real (inflation-adjusted) statewide residential building permits are expected to post a 4.3% gain for the year as a whole, and they will rise more than 18% in 2011. In 2012 permits will still remain 39% below their 2005 peak.
- Private nonresidential permits and government contracts appear to have leveled off. However, activity has been

concentrated in a relatively small number of large projects, the overwhelming majority of which are on Oahu.

Demand for new private nonresidential projects is being suppressed by high vacancy rates among office, industrial, and specialty/resort retail. Development by big box retailers appears to be the most dependable source of growth for the next few years. Permits for the year as a whole will be roughly unchanged from 2009 levels. Non-residential permits will remain 33% below peak in 2014.

- Government contracts awarded surged 20% in the first half of the year, compared with the same period in 2009, with the awarding of a number of large energy and highway contracts and several University of Hawaii projects across the state. We expect the pace of growth to back off next year, but government infrastructure projects will maintain a level roughly 50% higher than during the 2005-2009 period. As in past reports, we emphasize that our government construction forecasts do not incorporate estimates of the impact of Oahu rail transit.
- The statewide construction job count has stabilized but will show a 3.6% decline for this year as a whole; it will expand by just under 2% in 2011. Real construction labor income will decline 2.6% this year, turning to 3.2% growth in 2011. More significant job and income growth will not resume until the next industry upswing is well underway in 2013. The real General Excise and Use contracting tax base will decline by 16% this year and will stabilize in 2011.
- In Hawaii as in the nation as a whole, there remains a high level of foreclosure activity and a potentially vast overhang of troubled mortgages that could ultimately wind up in foreclosure. How this *shadow inventory* impacts housing markets (and construction) will depend on the pace of economic improvement but also on how rapidly financial institutions act to move troubled properties off their books. Other vulnerabilities include the reliance on a small number of large public projects and external risks associated with weakening U.S. and global recoveries.

HAWAII CONSTRUCTION FORECAST (SUMMARY)

	2008	2009	2010	2011	2012
GE Contracting Tax Base (Mil 2009\$)	8,098	6,642	5,585	5,743	6,639
% Change	-3.7	-18.0	-15.9	2.8	15.6
Nominal GE Contracting Tax Base (Mil \$)	7,987	6,642	5,574	5,904	7,031
% Change	1.7	-16.8	-16.1	5.9	19.1
Construction Job Count (Thou)	37.9	31.5	30.3	30.9	31.1
% Change	-3.2	-16.9	-3.6	1.9	0.6
Construction Income (Mil 2009\$)	3,332	2,756	2,686	2,773	2,854
% Change	-7.1	-17.3	-2.5	3.2	2.9
Honolulu Median Home Price (Thou \$)	619.3	573.4	598.5	622.5	652.1
% Change	-3.1	-7.4	4.4	4.0	4.8
Honolulu Median Condominium Price (Thou \$)	323.4	303.7	306.8	323.6	338.3
% Change	-0.4	-6.1	1.0	5.5	4.6
Honolulu Housing Affordability Index	64.5	79.4	81.5	79.1	74.4
% Change	12.1	23.1	2.8	-3.0	-6.0

* Note: Source is UHERO. Figures for 2010-2012 are forecasts. Tax base is deflated by Honolulu Index. Income is deflated by Honolulu CPI. Housing affordability index is the ratio of median family income to income for a loan for the median-priced home (times 100). Additional detail available to subscribers and sponsors.

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