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Post Pandemic Construction Boom

State of Play, Australia Wide

December 2021

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In this update, Slattery provide insights into how the construction market is responding to Government stimulus and the post pandemic construction boom.

What impact has opening up had across the construction market Australia wide?

In this paper we cover:

- Cost escalation
- Key impacts on construction including labour and materials
- Embodied carbon and the impact of ESG requirements
- State by state overview
- Consultant impacts

Introduction – the cost escalation forecast and what it means

With new and on-hold projects coming back after lockdowns and long periods of uncertainty, Slattery is predicting an average 4-5% escalation over the next two years across major markets. Smaller markets will continue to struggle to secure supply chains and sub-contractors, with Tasmania pushing the highest escalation at around 12-15%, Perth over 8% and Brisbane 6%.

The inability to attract labour resources and talent across all facets of the building industry will continue to put pressure on pricing. Increases in steel and copper prices, as well as timber shortages, will also have a big impact in driving costs upwards over the next 6-12 months.

2022 is looking to be an exceptionally busy year with a pipeline of government stimulus projects, international borders opening and overall developer confidence increasing.

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GPT Group
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Hawthorn Park
Deloitte PDS
Architect: Rothelowman

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Overview of the key impacts on the national market

Slattery is delivering work across all Australian states and have observed the following key impacts on materials:

- Plasterboard shortages are a challenge across the nation.
- Shipping container costs have increased to around $25,000 each with logistics issues likely to continue for another 12-18 months.
- Due to China's hardline stance on COVID-19 shutdowns and border control, quality control continues to be an issue for overseas joinery and façade manufacturers. As a result, builders are seeking local alternatives for joinery which are likely to be higher in price because of the increased cost of labour.
- China is facing aluminium and power shortages which is expected to place upward pressure on impacted goods'
- Steel (reinforcement, structural steel members and steel stud) prices are expected to increase again in December.
- Copper prices remain high impacting lighting, AV and cabling supply costs.

Quality of Facades – the impact of refurbishment and replacement

The 2019 BCA Update introduced higher performance requirements and as a result, façade costs are increasing. A lot of projects affected by this change are only now coming to market and the impact is in its infancy.

Not all sectors will be impacted in the same way. For example commercial office and university projects already have high-performance façades, so there will be some impact. However, there will be a bigger impact on 'investor' grade residential apartment projects that typically had single glazed laminated glazing units and now require double glazing throughout.

Embodied carbon – the impact of ESG requirements and Green Star ratings

Increased attention on embodied carbon

Last quarter, Slattery launched its carbon planning service, measuring the embodied carbon in existing and new-build projects. With Environmental Social Governance (ESG) requirements impacting commercial, health, and build-to-rent REITS – we are seeing a considerable increase in demand for the measurement of embodied carbon.

The industry is now turning its attention to addressing embodied carbon, as both the electricity grid decarbonises and operational carbon decreases due to energy-efficient design. The Green Star Design and As-Built rating tool certifications end on 17 December 2021. The new Green Star Buildings rating tool will incorporate mandatory upfront embodied carbon reduction criteria. 4 Star and 5 Star certifications require at least a 10% reduction in the building's upfront embodied carbon, and 6 Star certifications will require at least a 20% reduction.

These criteria will become even more stringent over the next 8 years. By 2030, all Green Star certified buildings will need to have at least a 40% reduction in a building's upfront embodied carbon. NABERS and all levels of government are already looking to incorporate embodied carbon criteria into their RFT submissions.

Embodied carbon – impact on materials

The concrete industry is leading the way, offering several lower carbon concrete alternatives. Embodied carbon reduction is heavily reliant on concrete (based on Slattery's carbon data, 30 – 50% of a building's upfront embodied carbon sits within the structural frame).

Australian manufactured steel is still several years away from producing "green steel" and will rely on the progression/investment in renewable energy and the phasing out of fossil fuel-powered blast furnaces. Lower carbon steel is available internationally (Europe, North America), however, the transportation emissions need to be factored into any embodied carbon measurements.

Cross Laminated Timber (CLT) is a popular choice for residential and commercial developers. If used instead of a reinforced concrete structure, it potentially reduces a project's upfront embodied carbon by 35-40% (excluding sequestration). However, there continue to be supply chain issues with CLT.

Image credit:
32 Smith Street, Parramatta
Architect: Fender Katsalidis

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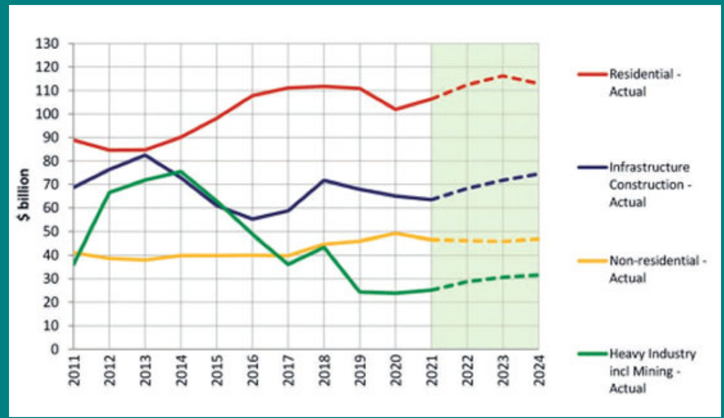
Volume of work expected

According to the November Australian Construction Industry Forecast (ACIF), construction relating to infrastructure will continue to have the strongest pipeline and is expected to increase by 7.5% in 2022, continuing for the next 3-4 years. Residential construction has two more strong years before it will taper off.

Non-residential construction is expected to slow down. While there will be stronger spending in health and aged care, this is not expected to counteract the decrease in retail, commercial, and accommodation which may take some time to recover to pre-pandemic levels.

Overall, a strong recovery is expected. The Global GDP has now risen above pre-pandemic levels providing a positive outlook.



Graph One

Australian Building and Construction Work Done
($ billion, 2018-19 prices) via: ACIF CFC

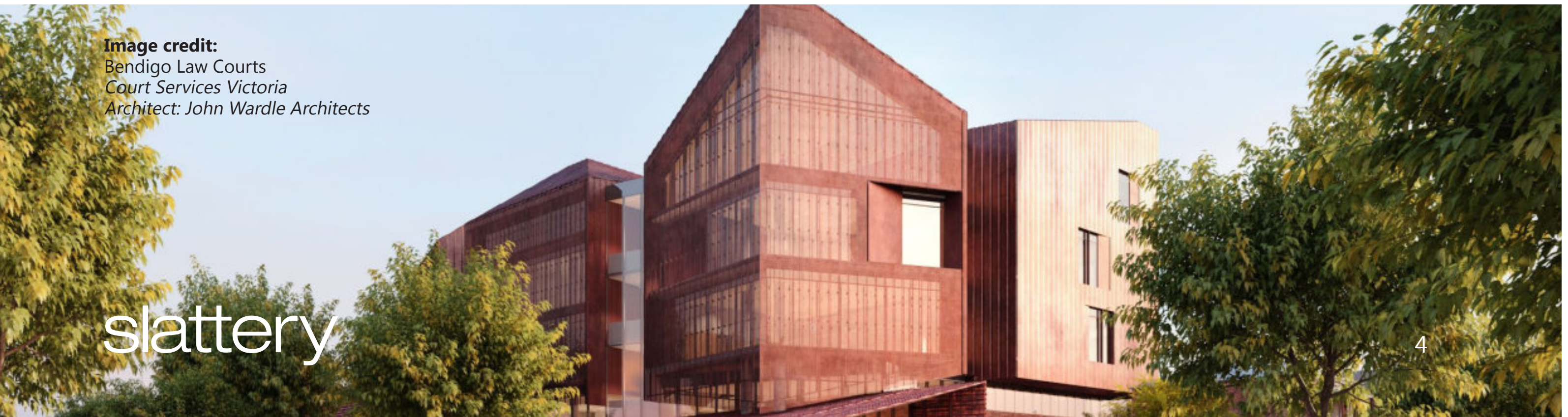
The forecast

Slattery is currently forecasting an average of 4-5% per annum for the next three years in Australia's major markets with significant variances in our smaller and more remote cities. While many impacts show a common thread across the individual states, there are significant local variations that should be considered in each State.

The biggest impact will be on long-term projects. Budgets may have been set years ago but have only recently been given the go-ahead. It is important to review the price for nuance and robustness. It is not simply a matter of updating for cost escalation.

Graph Two

Cost escalation forecast



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Bendigo Law Courts
Court Services Victoria
Architect: John Wardle Architects

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State by State Focus - Common Trends

Many impacts are common nationally, however each state is facing its own local impacts, opportunities and challenges.

Victoria

- With Victoria, and in particular Melbourne, are emerging from another year punctuated by lengthy lockdowns. Many consultants and contractors are anecdotally reporting that they are busy with either projects that went on hold because of COVID-19, or new opportunities that were germinated over lockdowns.
- Whilst there are a number of projects progressing in design or coming to tender over the next period, there are fewer projects in the $150M+ category. This is likely to mean that larger contractors and their supply chains will be competitive for any projects of that magnitude.
- Victoria is challenged with the same material and commodity supply issues that face the rest of Australia. Plasterboard, steel (structural, reinforcement, sheet), aluminium, timber, and curtain walling are all pushing prices up and well above historical benchmark levels.
- The demand for construction materials is being fueled by the competing tensions of a boom in the domestic building versus a significant increase in post lockdown commercial construction. Until manufacturing capacity can catch up, the supply of key materials will likely be an issue through much of 2022.
- Previously, contractors and their supply chains were squeezing their margins to offset material price increases and to remain competitive. For the most part, this is no longer the case and margins are slowly increasing to pre-pandemic levels.
- Escalation is forecast to be 4-5% on average.

New South Wales

- Increasing material prices continue to push tenders up like other states, with supply chain shortages of timber and façades starting to cause program delays on larger projects.
- Labour shortages continue despite the easing of restrictions. Skills shortages across most trades, management, and professions, continue to drive up wages and preliminaries.
- Margins are still under pressure on small to medium value projects with builders trying to fill order books to maintain cashflow; but with material and labour prices continuing to rise, liquidity continues to be a concern.
- With larger stimulus projects starting to come online, there appears to be less pressure on margin for higher-value projects. Recent increases in material and labour prices are being passed on in tender returns.
- Build to Rent interest remains high with several site acquisitions and project announcements. Build to Sell products are now gaining more traction after a lull.
- Escalation is forecast to be approximately 4-5% next year.

Queensland

- Tenders in Queensland are currently extremely volatile with limited trade coverage and large differences between prices received. This is made worse with the summer holiday period and a large volume of tenders coming to market.
- Supply chain issues continue to be a challenge with all trades reporting difficulties in obtaining materials on time.
- Supply chain networks are predicted to return to normal in mid-2022 with price volatility levelling over time.
- The construction market is buoyant, especially in areas such as the Gold Coast and Sunshine Coast where migration is driving residential development.
- The housing sector, driven by migration and stimulus, will enable other sectors, such as retail, industrial, followed by schools and health. Health is a focus for state government with hospitals preparing for possible longer-term COVID-19 implications.
- The labour force is also an issue with several trades reporting difficulties in finding people to deliver the volume of work currently on the books and forecast for next year.
- Developers are trying to source non-EBA contractors due to the reduced price point difference. However, the non-EBA trade prices are also increasing with demand.
- Contractors with an EBA are currently looking at a reduced site allowance agreement for projects under $50m, which has been implemented to enable more competitiveness in this space. This will potentially increase the pool of contractors who can work in this price bracket.
- The Brisbane Olympics in 2032, is a very welcome boon that will drive investment and federal funding over several years.
- As of January 1, new legislation under the Building Industry Fairness Act mandates the establishment of project trust accounts on private projects over $10m. It is anticipated the administration of this facility will increase contractor overheads and result in preliminaries cost increases. These rules require developers to pay retention into a trust account, which could affect development cash flow.
- Escalation is forecast to be 5-6% next year.

Continued on the following page.

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State by State Focus - Common Trends

Western Australia

- General building escalation in Perth is running at approximately 8-8.5% year on year, however, the cost of 'selling' the risk to contractors is between 12-15%.
- Steel (reinforcement and structural), glass and concrete remain unpredictable with suppliers refusing to hold pricing beyond that month or even guarantee supply beyond the month. Labour intensive (form & pour, partitioning, etc) and services trades are not able or willing to commit to forward work which is keeping their pricing high, especially outside metropolitan areas.
- The main pressure release will be vaccine-related border opening, first nationally then later internationally, and resources that can then be brought in. Realistically that will be at the end of quarter three 2022 at the earliest. It is estimated that will 'settle' the increases at circa 5% but not in the short term.
  - Labour availability is expected to ease as the ability to gain resources from the east coast increases in line with vaccination uptake. Without this intrastate resourcing, the WA market will face an increasing strain on labour availability.
- As with other locations, nationally and internationally, the availability of key materials has required creative redesign and engineering of projects across WA. Exacerbated by its remoteness, Perth is increasingly suffering from availability leading to price stress.
  - The Residential sector is seeing a focus on suburban housing, utilizing government incentives which have slowed the uptake in apartments. Build to Rent is finally starting to make an impact with significant schemes in their infancy. The new stock of social and affordable accommodation is slow to come to fruition.
- Riverside CBD projects, particularly in Elizabeth Quay, are contributing to a strong commercial sector at present. Once these are completed it will lead to an inevitable slowdown as the backfill space is slowly absorbed.
- Impacting the Tier 2 contracting community is the significant gulf between the government's high value and high projects, such as Metronet and Edith Cowan University (ECU), and their smaller projects. The ECU EOI for contractors closes soon and represents a significant stage in the Perth City Link. Post restrictions, the Southwest tourism sector is expected to grow, generating a pipeline of investment in the Busselton / Margaret River area.
- Should Scarborough and Pluto Train 2 developments proceed, it will further stretch resources in the Pilbara but it will enhance WA's international position in the LNG export market. With iron ore remaining at circa US$100/T, continued development and labour shortages will put pressure on production costs.
- A large gulf has opened between Tier 1 contractors and a crowded Tier 2 field. As a result, Tier 1 capacity is at its limit, while many Tier 2 contractors have incomplete order books and competition is still strong in the Perth metropolitan market. Regionally, the ability to resource projects outside the metropolitan area remains a concern for contractors.

Tasmania

- Several large-scale projects by the University of Tasmania in the north of the state will continue to absorb a large percentage of market capacity through to the end of 2023. The roll-out of their program in the south of the state in early 2022 will then begin to put increased pressure on the southern market.
- Housing demand across all sectors is increasing with migration from VIC and NSW. With the State & Federal Government first home buyer grants being maintained, additional pressure and resultant price increases are forecast to continue for at least 24 months.
- Supply issues on steel and LVL timber products (as is also experienced in other states).
- Labour shortages will continue to be experienced with previous reliance on labour from other states not being possible due to national demand as well as ongoing uncertainty on COVID-19 travel restrictions. The labour shortages are impacting all trades with contractors competing for labour resulting in reasonable wage increases. It is anticipated that this will increase throughout 2022.
- State government stimulus measures including a Headworks Holiday and the Building Project Support Program will trigger marginal projects placing increased pressure on an already extended market.
- Rumours of 30% cost increases over the last year continue to circulate. These levels are limited to small scale refurbishment projects (largely residential) and are driven more by opportunistic pricing rather than bona fide market drivers.

South Australia

- Similar to the rest of the nation, the market is very busy with material shortages being reported against most trades but particularly insulation, steel, timber, and plasterboard.
- These material shortages are resulting in program issues as well as an upward cost pressure. These challenges are being felt across both the residential and commercial building sectors.
- State Government capital works are at an all-time high with a new Women's and Children's hospital, a redevelopment of the Queen Elizabeth hospital, a potential new stadium, a sports institute, and significant works at Flinders University.
- The education sector is busy with spending across a program of projects. There are also large defence projects that are due to come to tender in the short term.
- The private sector is also buoyant with North Adelaide and Port Adelaide being hot spots for medium density residential.
- Escalation is predicted to be at least 4% per annum.

Consultant Impacts

- Consulting firms who have a strong government and infrastructure pipeline are now back to pre-pandemic staffing levels and yet still require more staff. Some larger firms are starting to turn work away. These firms have been declining work – preferencing high-profit and strong pipeline clients.
- Those firms with little government or infrastructure work are still playing catch-up and have been submitting hyper competitive fees to obtain an entry into the strong government pipeline.
- Staff attraction and retention is a problem for all firms and Government agencies. Staff are leaving almost as quickly as firms are hiring and the skills shortage/lack of migration is affecting the talent pool.
- Consultants are seeing more confidence from commercial and residential developers. Coupled with the already strong pipeline we are seeing from the Government stimulus, 2022 is looking to have a high volume of work across the board. Works ramping up include airports, rail and road infrastructure, station precincts, industrial (logistics and storage), build-to-rent and retail anchored mixed-use.

Image Credit:
Ashurst Workplace
Aspect Furniture
Architect: Bates Smart

If you would like further information or to discuss anything in this Construction Market Update, please reach out to any of our key state contacts below.

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Image credit:
UTAS Cradle Coast
Architect: John Wardle Architects

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Image Credit:
Slattery Sydney Collection

About Slattery and our collaborators

Slattery is a property and construction advisory firm specialising in quantity surveying, cost management, and early-phase project advisory, with an outstanding history spanning more than 40 years.

We work hand-in-hand with governments, institutions, and organisations as well as planners, developers, architects, and design teams on a broad range of property and construction projects.

A commitment to excellence and innovation, and an ability to become an integral part of the project team has earned Slattery the trust and respect of clients and project teams alike. Slattery adds value by taking control and ownership of the cost management process from the outset. We understand the importance to drive innovation and productivity.

We invite you to explore our knowledge sharing further at www.slattery.com.au/thought-leadership

Thank you to **Peter O'Donoghue from Exsto Management** and **Chris Sale from Chris Sale Consulting** for contributing to this Construction Market Update with on the ground knowledge of the market in Tasmania and South Australia respectively.

Slattery Carbon Planning

Slattery is proud to be the first Quantity Surveying firm in Australia to launch a Carbon Planning service.

This new service is available in conjunction with Cost Planning to assist our clients in achieving their Net Zero and sustainability targets. The focus of the carbon plan will address and educate clients on the embodied carbon of their current and future developments.

Read more about Slattery's Carbon Planning offering at www.slattery.com.au/carbon-planning

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