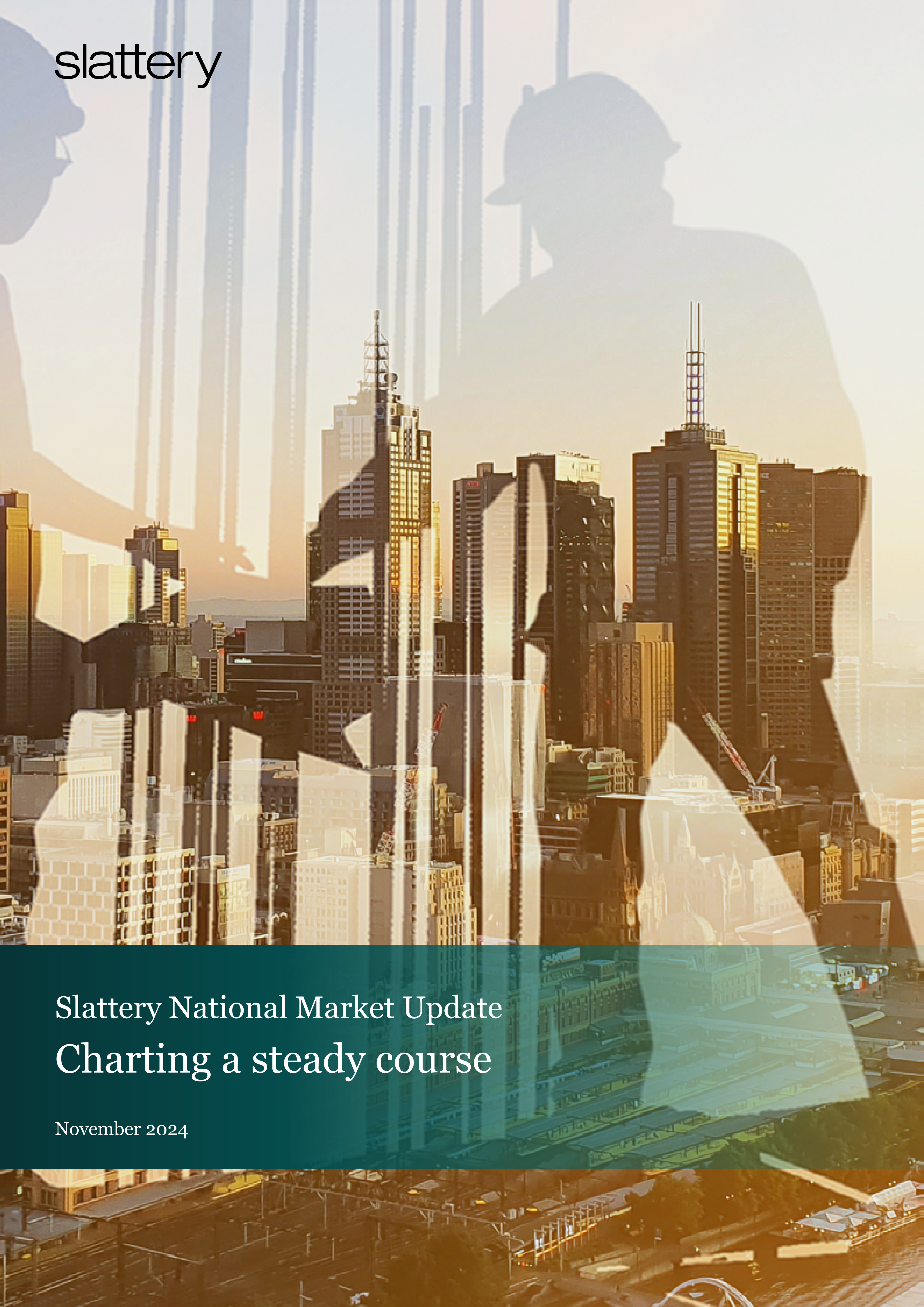

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Slattery National Market Update

Charting a steady course

November 2024

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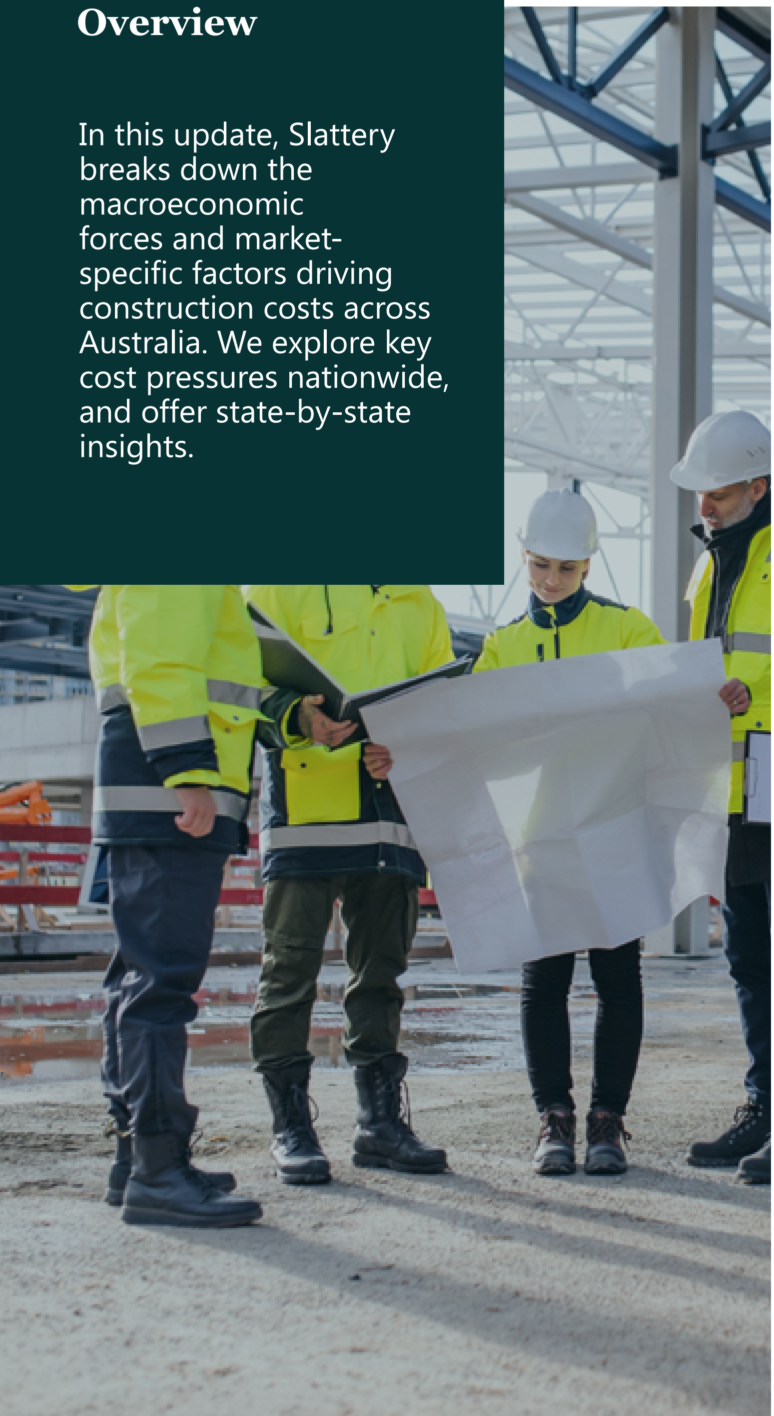
Charting a steady course

Australia's construction sector shows resilience, with growth opportunities on the horizon despite global uncertainties. Industry players must remain vigilant, navigating complex cost pressures and evolving market demands to secure long-term stability.

Overview

In this update, Slattery breaks down the macroeconomic forces and market-specific factors driving construction costs across Australia. We explore key cost pressures nationwide, and offer state-by-state insights.



The forecast

Slattery forecasts that construction escalation rates in Australia's major markets will rise by an average of 4-6% per annum through the remainder of 2024 and into 2025.

This national average doesn't apply uniformly to all projects, materials or locations. Given the unpredictability of cost escalation, we advise clients to actively review their projects and portfolios, anticipate market shifts, and implement strategic mitigation plans.

City	2024	2025 forecast
Sydney	4-5%	4-5%
Melbourne	4-5%	4-5%
Brisbane	4-6%	4-6%
Adelaide	4-5%	4.5-5.5%
Hobart	6%	6%
Perth	4.5-5.5%	4.5-5.5%

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National overview

Australia's building and construction industry is the second-largest contributor to the nation's economic growth and delivers nearly one in 10 jobs. However, the sector continues to be plagued by persistent challenges, especially labour shortages, regulatory red tape and supply chain disruptions, which influence costs. We provide a roundup of the most pressing factors for the industry below.

Global outlook

The global economic outlook remains uncertain, weighed down by conflicts in Ukraine and the Middle East, China's prolonged downturn and elections impacting half the world's population, including in the world's biggest economy, the United States. The International Monetary Fund (IMF) October 2024 Global Financial Stability Report warned that many countries may be underestimating rising geopolitical risks. Notably, U.S. President-elect Donald Trump's proposed tariff hikes could fuel inflation, while his tax cut plans risk deepening the US deficit. Meanwhile, the crisis in the Middle East could impact logistics and supply chains.

Inflation and interest rates

The Reserve Bank of Australia kept the cash rate steady at 4.35% when it met on Melbourne Cup Day. While headline inflation is down, underlying inflation of 3.5% is still outside the RBA's target band. Later in the week, the US Federal Reserve cut interest rates by a quarter of a percentage point following Trump's victory, with policymakers noting that inflation continues to move in the right direction. The IMF has raised Australia's 2025 inflation forecast from 2.8% to 3.6%, predicting it will be one of only two advanced economies, alongside Slovakia, with inflation above 3% next year.

Consumer sentiment

Consumer indices are showing a slight uptick in sentiment in the second half of 2024. While the cost of living remains the biggest driver of consumer stress, according to NAB, the Westpac–Melbourne Institute Consumer Sentiment Index jumped 6.2% in October – the most encouraging sign since the RBA began its rate hikes two and a half years ago.

Construction insolvencies

According to the Australian Securities & Investments Commission, 964 construction businesses entered administration between June and October 2024, averaging eight per day. This marks an increase from 814 during the same period in 2023 and 636 in 2022.

Labour and skills

Australia has one of the world's strongest jobs markets. More than 64,000 new jobs were created in September, according to the Australian Bureau of Statistics (ABS). The unemployment rate remains steady at 4.1%, where it has hovered for the past six months. Job vacancies fell by 5.2% in the three months to August 2024. The Wage Price Index rose by 4.1% over the year to June 2024.

Commencements of new apprenticeships in construction trades decreased by 11.8% for the year ending March 2024, and completions by 10.2%, according to the National Centre for Vocational Education Research (NCVER). "Low apprentice numbers reflect a shortage of skilled workers across all trades, and until we're able to address the challenges facing the future of the workforce, we won't be able to increase building activity," noted Master Builders Australia CEO Denita Wawn in October.

Productivity

Construction labour productivity – the ratio of output to hours worked – fell by 4% in the June quarter, following a 2% decline in the previous quarter, according to the Productivity Commission. The Australian Government's National Construction Industry Forum convened for the first time in October. This forum brings together representatives from government, business and unions to develop a new "blueprint" aimed at breaking Australia's productivity deadlock.

National overview *cont.*

Materials

Master Builders Australia estimates that construction costs have increased by 40% and build times have blown out by up to 47% over the last five years. Material costs, particularly for structural materials like steel and timber, have stabilised to offer builders some relief. However, energy-intensive materials such as concrete and insulation continue to rise with increasing energy prices. Price increases for materials are closely tied to market activity levels, with annual escalation rates gradually returning to the historical escalation range of 3-4% per annum.

Sustainability

Mandatory climate reporting will take effect from 1 January 2025, starting with the companies with more than $500 million in consolidated revenue. Most of these companies already have robust reporting procedures in place. The second tranche, those with $200 million or more in consolidated revenue, will be phased in from 1 July 2026. This is when the impact will begin to be felt in the market, driving increased transparency and accountability along the length of the construction supply chain.

Industry stakeholders are also eagerly awaiting the release of the NABERS Embodied carbon tool, with pilot projects currently underway. NABERS has noted that the tool is "already being referenced in policy" such as the NSW Sustainable Buildings SEPP and the Australian Government's Environmentally Sustainable Procurement (ESP) Policy and Reporting Framework.

> "In times of uncertainty, the construction industry is rising to the challenge. By tackling costs with strategic foresight and a commitment to innovation and collaboration, we can navigate the complexities ahead and lay a sustainable foundation for Australia's growth."
>
> **David Martin,** CEO, Slattery

Commercial

- **Office:** Australia's CBD office vacancy rate stood at 13.6% in July 2024, and non-CBD vacancy at 17.2%, per the Property Council's latest Office Market Report. Vacancy rates, combined with higher borrowing costs, continue to flow through to office asset values, which have lost 21% in Sydney and 27% in Melbourne over the last two years, according to Macquarie analysts. Tenants are increasingly gravitating toward better-quality assets, with Premium and A-grade properties in high demand. As B and C grade assets become obsolete, there is a growing opportunity for adaptive reuse and innovation. JLL's Asia Pacific Capital Tracker shows strong interest in office and logistics assets from overseas investors.
- **Industrial:** "Warehouse investors are starting to open up their wallets again," says CBRE and more than $5 billion was invested into income-producing industrial and logistics real estate nationally during the September quarter. National rental growth remains strong at about 9% year-on-year.
- **Retail:** Investor sentiment in retail property is improving as foot traffic returns, and global capital is on the hunt for assets. One sign of the times is the Queensland Investment Corporation's plans to sell the Westpoint shopping centre in Sydney's Blacktown for a reported $900 million. This represents the largest standalone retail property transaction in Australian history.

Residential

Australia is falling short of its target of 1.2 million new homes by 2029, indicated in the latest ABS housing completions data. While dwelling completions rose by 7.3% in the June quarter, delivering 44,853 dwellings, this figure remains well below the 60,000 homes needed each quarter over the next five years. Dwelling commencements declined by 1.1%, contributing to an ongoing undersupply of housing that is dampening industry confidence.

According to the September Procore/Property Council Survey, 43% of respondents chose housing supply and affordability as the most pressing concern for the federal government, and 42% considered this the most critical issue for state governments.

- **Apartments:** The apartment market continues to be challenged by pre-sale requirements for financing and the need for a larger skilled labour force. KPMG analysis indicates that 82% of Sydney dwellings currently on hold are apartments and townhouses.
- **Build-to-rent:** As build-to-sell apartment developments fail to stack up, developers continue to look for alternatives. Build-to-rent is one promising avenue. Among projects to watch is the $1.5 billion Timberyards in Sydney's Marrickville, spearheaded by the co-founders of Scape Australia, the nation's largest student accommodation provider. This ambitious project aims to deliver up to 1,000 apartments, including 100 affordable units.

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National overview *cont.*

- **Purpose-built student accommodation:** The student accommodation sector is also gaining attention, with CBRE estimating that Australia will add 19,000 new beds between 2024 and 2027, representing an 18% increase over current volumes.

Infrastructure

Governments are shifting priorities, reshaping the infrastructure landscape nationwide.

As mega transport projects wind down, the energy sector is stepping up. The next phase of the federal Capacity Investment Scheme has doubled in size in response to demand, with the next round of tenders calling for 10 gigawatts of wind, solar and battery storage. The renewables transition is well and truly underway. In October, the electricity grid reached a milestone with a 75.2% share of renewables. However, transitioning from transport to energy projects presents challenges for industry participants as they look to pivot skills, capabilities and locations.

- **Victoria:** While projects are gradually tapering and some major projects have been deferred, infrastructure spending remains above the 10-year average. Tunnelling for the Suburban Rail Loop (SRL) is set to begin in 2026, although the project's long-term future is likely to be decided at the state election in 2026.
- **New South Wales:** The tap on transport projects hasn't just slowed – it's been turned off. Major projects like Sydney Metro remain in delivery but planning decisions for other projects have stalled. The focus is shifting to regional rail, with the NSW Government developing a strategy for an upgraded network. Water infrastructure is also front and centre, with Sydney Water set to invest $34 billion over the next decade.
- **Queensland:** The Sunshine State is poised for Australia's "next big build". The Olympic Games and major infrastructure projects are drawing significant investment, and skilled trades are relocating to participate in this boom. Among the projects to watch is the Sunshine Coast Rail. Stage 1, projected to cost $5.5 to $7 billion, which is slated for completion by 2032.

State by state trends

Australia's construction costs are shaped by local challenges and constraints. Our state-by-state analysis highlights the key cost drivers in each market where Slattery and its partners operate.

Jump ahead to:

New South Wales

Queensland

South Australia

Tasmania

Victoria

Western Australia

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New South Wales

Sentiment is slowly returning to positive territory in NSW. Clients, particularly in the residential space, are revisiting projects that had been shelved for several years. This renewed interest extends to the education sector, with universities dusting off old feasibility studies and school projects returning to the market after a year of inactivity. Key factors influencing the local market include:

Government activity

The NSW Infrastructure Pipeline is currently dominated by education and healthcare projects, alongside transport. The health infrastructure pipeline, for instance, stands at $13.8 billion over the next four years.

Urban renewal

The State Significant Rezoning Policy, published September, is expected to provide a faster pathway for large and complex rezoning proposals to deliver more social and affordable housing. Several sites have been identified, including Blackwattle Bay and Bays West.

Big build

The contract for Australia's largest social housing project, a $4 billion redevelopment in Sydney's Waterloo South, was awarded in August. This transformative project aims to reshape perceptions of social housing, delivering 3,000 new social, affordable homes, alongside retail and public open spaces.

Residential backlog

The build-to-sell model continues to face significant challenges. Builders remain hesitant due to extended liability, and a limited number of contractors are willing to take on projects exceeding $150 million. Larger head contractors are selectively stepping back, leaving Tier 3 builders to move into Tier 2 territory. This raises concerns about their ability to deliver and remain solvent.

Housing supply

With affordable housing an ongoing hot topic, the NSW Productivity Commission's recent report into housing supply challenges provides some hope with its recommendations, though its call for reductions in solar access requirements and minimum apartment sizes has sparked significant industry debate.

Labour squeeze

Negotiations for the latest round of Enterprise Bargaining Agreements (EBAs) has concluded, providing some stability for the next five years. However, a large portion of the residential market remains outside these agreements. Labour supply issues currently stem more from market demand than union pressures.

Summary: The Property Council's latest sentiment survey finds the state's property industry is "tentatively positive" and there is certainly a greater degree of certainty in NSW construction. But caution is the key word. We expect a 4-5% per annum cost escalation across NSW, holding steady at that rate over 2025, before stabilising at the traditional rate of 3–4% per annum.

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Queensland

Queensland's construction market is currently experiencing significant fluctuations. While public sector work continues at pace, private sector projects are facing considerable challenges in getting off the ground, primarily due to high costs and a persistent shortage of skilled labour. Several key market movements to watch include:

New government

Several large projects received the green light just before the caretaker period, and the implications of the new Crisafulli Government will take time to materialise. Any regulatory changes affecting the construction industry will impact how projects are managed and executed.

Stadium squabbles

The 2032 Brisbane Olympics became a pivotal issue in the recent election, with plans to either replace the ageing Gabba or upgrade the Queensland Sports and Athletics Centre attracting ire. Newly elected Premier David Crisafulli has announced a 100-day review of Olympic venues, which maintains the option for a Gabba revamp while definitively ruling out the construction of a new stadium.

Labour squeeze

The shortage of trades persists. Queensland's public infrastructure pipeline was 38,000 people short in October 2024, according to Infrastructure Australia's Public Infrastructure Workforce Supply Dashboard. This labour squeeze has significant implications for project timelines and costs.

EBAs

CFMEU Queensland secured a substantial 26% increase over five years in June. This increase has now been factored into project costs, resulting in an immediate 2% rise that impacts overall budget projections across the industry.

Subcontractor dynamics

At the smaller end of the market, builders are observing a greater appetite from subcontractors. Workplace fitouts are particularly competitive, creating opportunities for smaller firms. However, larger projects still struggle with a lack of depth in resources, leading to inefficiencies and potential delays.

Productivity pitfalls

Conservative pricing strategies among builders reflect ongoing productivity concerns. Subcontractors, who traditionally accepted some risk related to weather, must now also factor in disruptions caused by unions, persistent supply chain issues, and the impact of extreme weather events due to climate change. This has led to a more cautious approach to pricing and project management.

Summary: Despite cost escalation hovering at around 4-6% per annum, this figure masks the reality that expenses are trending upward. The current market capacity may be short-lived, as billions of dollars in public infrastructure projects are set to break ground.

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South Australia

South Australia's construction market remains robust, with diverse activity across multiple sectors. Tier 1 contractors are particularly busy, managing a substantial volume of both public and private projects. While Tier 2 contractors are also finding opportunities, a noticeable divide exists between the two tiers regarding workload and cost pressures. Key market movements include:

State of states

South Australia has secured the top spot in the economic performance rankings in the latest CommSec State of the States report for the third consecutive quarter, bolstered by a strong job market and thriving construction activity.

Sentiment up

Confidence in the local market has surged by 9% over the past quarter, as indicated by the Procore/Property Council Industry Sentiment Survey, with forward work expectations surpassing historical averages.

Key projects

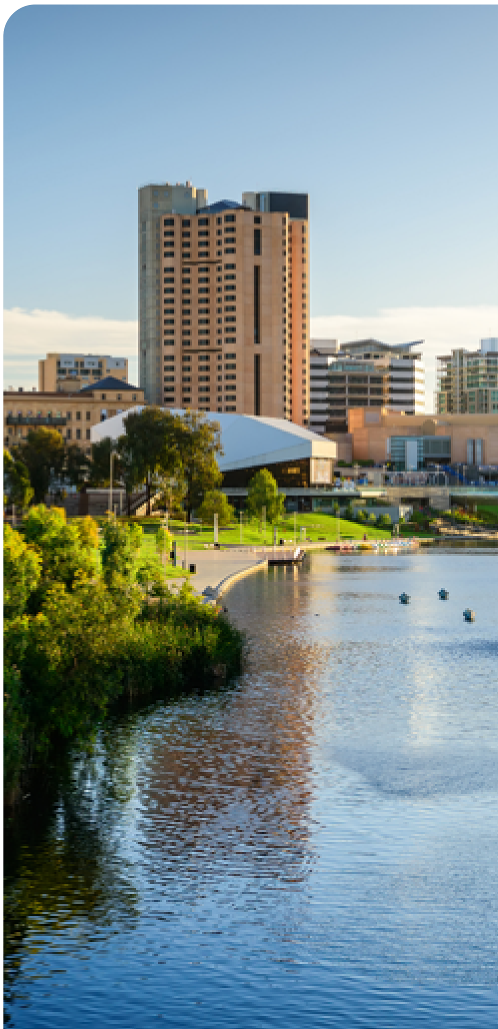
The Department for Infrastructure and Transport boasts a healthy pipeline of projects, including the $3.2 billion Women's and Children's Hospital. Recent announcements include $250 million for schools, $92 million for a new netball centre, and expansions of corrective service facilities.

City shaping

Multi-million-dollar investments in the Lot Fourteen and BioMed City innovation districts are driving growth in emerging industries. The Adelaide Economic Development Agency continues to monitor a significant list of private developments. Current projects under construction include the $400 million Market Square, $250 million Eighty Eight O'Connell, and the $200 million Victoria Tower.

Office demand

Although the city's headline office vacancy rate remains elevated, declining from 19.3% to 17.5% in the first half of 2024, demand for office space in the Adelaide CBD is nearly 600% above the historic average.



Summary: With new tenders hitting the market, expectations are high for strong activity in 2025. Consequently, we have revised our cost escalation range from 4-5% per annum to 4.5-5.5% per annum, indicating that while costs remain manageable, they are on an upward trajectory.

Tasmania

The outlook for Tasmania's construction market is cautiously optimistic, buoyed by a robust pipeline of public infrastructure projects and increasing interest from private developers. However, there are some underlying concerns, particularly with rising state debt projected to reach $8.5 billion in four years, which could lead to project reprioritisation. Key factors influencing the Tasmanian market include:

Infrastructure spend

The state budget, which passed in October, commits $5.1 billion to infrastructure over the next four years. Bridgewater Bridge, Tasmania's largest ever transport project with a $786 million price tag, is expected to open to traffic by the end of 2025.

Airport take-off

Launceston Airport signed a multi-year, multi-million-dollar deal for a major expansion in August, including upgrades to retail, food and lounge facilities. Described as the largest tender process in the airport's history, the project will accommodate over 1.75 million passengers by 2030, positioning the airport for future growth.

Stadium costs climb

Macquarie Point stadium is now forecast to cost $775 million – $60 million higher than originally estimated – due to potential escalations in fees, materials and labour. Despite this, the Rockliff Government will cap its contribution at $375 million. The project will undergo a 12-month assessment by the state's planning commission, followed by parliamentary approval. An unsolicited offer (Stadium 2.0) for delivery as a Public Private Partnership is currently under government review.

Housing headaches

Homes Tasmania has outlined its strategy to meet the target of 10,000 new social and affordable homes by 2032. The agency expects to carry $1.8 billion in borrowings by 2032 to support the initiative. But media reports suggest less than a third of the total will be social housing and more than 1,000 parcels of vacant land will be counted as 'homes'.

Labour shortages

Construction costs in Tasmania remain above the national average, largely due to a shortage of skilled labour and reluctance from interstate contractors, particularly specialists in mechanical and electrical trades, to enter the market. Breaking into the Tasmanian market is inherently difficult – it's a relationship-driven, long-term game.

Price perceptions

There's a prevailing perception, particularly from interstate contractors, that building in Tasmania is 30% more expensive than elsewhere. This belief is exaggerated, and experienced local players can often trim unnecessary costs and offer more competitive pricing.

Summary: The heat has left the market, with prices contracting as the gap between low and high bids narrows. Subcontractors are increasingly bidding on projects, a sign that their workload is easing. We anticipate easier pricing conditions over the next 12 months, as the industry awaits the next wave of large-scale projects. In response, we have adjusted our forecasts to a softer 6% per annum growth for the next 12-18 months, with slower escalation expected thereafter.

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Victoria

Victoria's construction market remains sluggish as public sector projects wind down and private developers struggle to find viable opportunities. Construction costs have plateaued, with revenues and income streams stagnant. Melbourne has hit the bottom of the trench and anticipated interest rate cuts could be a ladder out. Key local market shifts this quarter include::

Stamp duty concessions

The Victorian Government will cut stamp duty on off-the-plan apartments, units and townhouses for 12 months, saving purchasers of a $620,000 apartment around $28,000. This one-year, $55 million relief aims to accelerate home building and ease housing pressures. Stamp duty generated $8.7 billion in FY2022-23, 27% of state revenue.

New building watchdog

The Victorian Building Authority will be replaced by a more powerful regulator following a damning report on its handling of homeowner complaints regarding defects. The new watchdog will have the authority to compel builders to rectify issues even after homeowners have moved in.

Commercial vacanices

Melbourne's CBD office vacancy rate of 18% is driving innovation in adaptive reuse, timber construction and modularisation, with these techniques promising to boost productivity and sustainability.

Labour dynamics

Labour costs are set to rise by 5% per annum over the next four years due to EBAs. The CFMEU's current administration could lead to reforms, but it remains to be seen if these changes will improve labour competitiveness.

Capital attraction

Melbourne remains an attractive destination for capital investment, although investors are cautious. JLL notes that Melbourne leads the nation's build-to-rent market with 58% of the pipeline, and the industrial market remains "exceptionally tight" with below 2% vacancy. Office transaction volumes also rebounded in the third quarter, according to Cushman & Wakefield.

Summary: Looking ahead, we expect cost escalation of 4-5% per annum, with labour accounting for 3% of the increase. This forecast remains consistent with previous estimates, reflecting a market cautiously adapting to evolving challenges.

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Western Australia

It may be "business as usual" for Western Australia's construction sector, but labour costs and shortfalls in housing continue to pose significant challenges. Here are some key local factors shaping the WA market:

City shaping projects

New megaprojects continue to take shape, including $5 billion at Perth Airport to develop a new terminal, runway and airport hotel. The $3.8 billion megaproject at Burswood Point promises to become one of the largest urban development projects undertaken in Australia. Meanwhile, the WA Government's $43.9 billion asset investment program includes a current $8.7 billion pipeline of public works projects.

Procurement plus

In October, the Cook Government announced a new initiative to attract major investment in state infrastructure projects through a new Bid Contribution Policy for Non-Residential Major Projects, aimed at increasing market capacity and competition. Eligible contractors can receive up to $750,000 to offset bid costs for government non-residential projects valued over $100 million, including hospitals, correctional facilities and cultural buildings.

Defence spending

Defence spending is advancing rapidly, highlighted by the Albanese Government's mid-October announcement of its intention to establish a defence precinct at Western Australia's Henderson shipyard. This initiative promises to underpin tens of billions of dollars in defence capabilities over the next two decades and is projected to support around 10,000 jobs.

Housing horizons

Launched in mid-October, the new WA Housing Strategy aims to connect 150,000 households to homes by 2030, and targeting a 6% net increase in social housing. While this strategy promises to energise residential construction, just 3,957 homes were built in the June quarter, according to ABS statistics. To meet the National Housing Accord target, Western Australia must produce at least 6,540 new homes each quarter, highlighting a significant challenge ahead.

Economic powerhouse

WA emerged as the second strongest performer in the latest CommSec State of the States report which assessed eight key indicators: economic growth, retail spending, equipment investment, unemployment, construction work completed, population growth, housing finance, and dwelling commencements.

Summary: While Western Australia's construction market is strong, it continues to face cost challenges related to skilled labour. We therefore maintain our cost escalation forecast at 4.5-5.5% per annum for the remainder of 2024 and into 2025.

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Slattery is a property and construction advisory firm specialising in quantity surveying, cost management, carbon planning and project control measures. We're at the forefront of providing knowledge and insights to the industry.

If you would like further information or to discuss anything in this Market Update, please reach out to:

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Meeanjin	**nipaluna**	**Naarm**	**Boorloo**	**Warrang**

Thank you to **Travis Swigart, Managing Director** from **Chris Sale Consulting** for contributing to this construction market update with on-the-ground knowledge of the market in South Australia.

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