

DECLINE IN MAJOR CONSTRUCTION TO CONTINUE INTO 2016

Major construction value
2014: -3.6% p.a.

Major construction value
2015: -4.3% p.a.

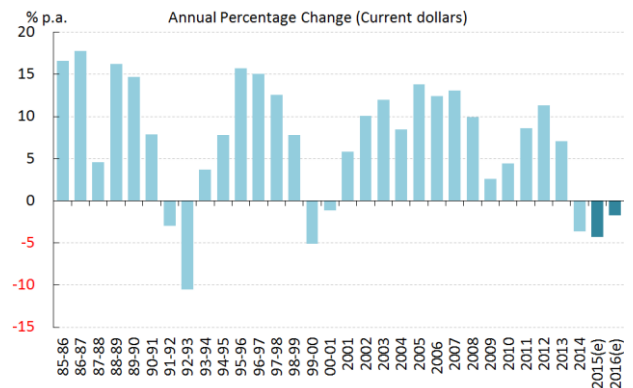
Major construction value
2016: -1.7%

Major construction jobs
Feb to Dec 15: -1.0%

KEY FINDINGS

- Following the downturn experienced in major project work in 2014, the **nation's leading construction companies** are forecasting continued declines in engineering and non-residential building activity in 2015 and 2016. This is largely on the back of further falls in mining-related construction and patchy conditions across key infrastructure project categories. Commercial construction is expected to remain subdued reflecting on-going weakness in the sector's project pipeline.
- However, there are bright spots for the industry's outlook. Revenue from road and rail projects is expected to pick-up solidly in 2016 in line with Federal and State Government plans for a number of major transport projects. The outlook is also positive for multi-level apartment building developments while telecommunications work is expected to be broadly sustained at current levels of activity over the next two years.
- The latest **Australian Industry Group/Australian Constructors Association Construction Outlook survey** reveals that following a fall of 3.6% in calendar year 2014 (current prices), the value of turnover from major construction work is expected to decline at a steeper rate of 4.3% in 2015 followed by a further fall of 1.7% in 2016.
- Employment in non-residential construction is also forecast to decline in 2015, largely in response to the winding back in mining-related work. A smaller pipeline of new projects, completions and the deferral of some existing projects will see falls in employment weigh more heavily on employees engaged on-site and sub-contracted trades. Non-residential construction employment is expected to recover somewhat in 2016.
- Engineering construction** is forecast to decline by 7.6% in 2015 and a further 3.6% in 2016, reflecting deteriorating conditions across a range of key project categories. The winding down in mining-related construction will be the major drag on activity, although notable falls are also expected in the heavy industrial resource based sectors. This includes oil and gas processing which is expected to experience a marked downturn in 2016. Recent falls in utilities investment is driving expectations for steeper declines over the next two years in electricity generation and water supply projects.
- Commercial construction** is expected to remain constrained by the continuation of subdued overall approvals in this sector. Following flat conditions in 2014, the total value of commercial construction work is expected to increase by just 1.3% 2015 and 1.5% in 2016.
- For **multi-level apartment developments**, solid growth of 14.5% is expected in 2015 followed by a 4.1% rise in 2016. This reflects strong growth in apartment building approvals in recent months in Sydney, Melbourne and many other locations around Australia.

TURNOVER FROM CONSTRUCTION WORK



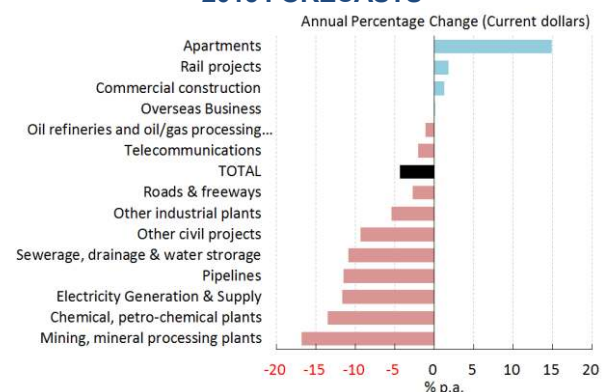
TURNOVER FROM CONSTRUCTION WORK: OUTLOOK AT A GLANCE

| SECTOR | 2014 % p.a. | 2015 % p.a. | 2016 % p.a. |
|---------------------------|----------------|----------------|----------------|
| Engineering | -5.4 | -7.6 | -3.6 |
| Commercial construction | 0.0 | 1.3 | 1.5 |
| Apartments | 7.1 | 14.9 | 4.1 |
| Overseas business | -1.1 | 0.1 | 0.2 |
| Total construction | -3.6 | -4.3 | -1.7 |

OUTLOOK 2015

- The total value of turnover from construction work is forecast to decline by 4.3% (current dollars) in 2015 following a fall of 3.6% in 2014.
- Within the **engineering sector**, mining-related construction is expected to decline by 16.8% in 2015 as the pipeline of new projects shrinks and current projects are completed. Reduced resources investment is also driving a decline of 3.2% in heavy industrial resource-based construction. However, a 1.1% reduction in work generated from oil and gas processing projects suggests that this sector will continue to hold-up reasonably well in 2015.
- The total value of infrastructure work (a sub-set of engineering construction in these data) is expected to contract by 4.9% in 2015 following a 7.6% decline in 2014. The value of other civil projects such as bridges/tunnels & harbour works is forecast to decline by 9.3% while power and water and waste infrastructure projects are expected to decline by 11.0% to 11.6% p.a.. A pause prior to the next round of major transport projects will see road construction fall by 2.7% in 2015.
- The value of **commercial construction** work is expected to record subdued growth of 1.3%. Various major projects are underway, but soft economic conditions and subdued investor sentiment appear to be weighing down firm commitments to new commercial developments such as offices, retail developments and related facilities.

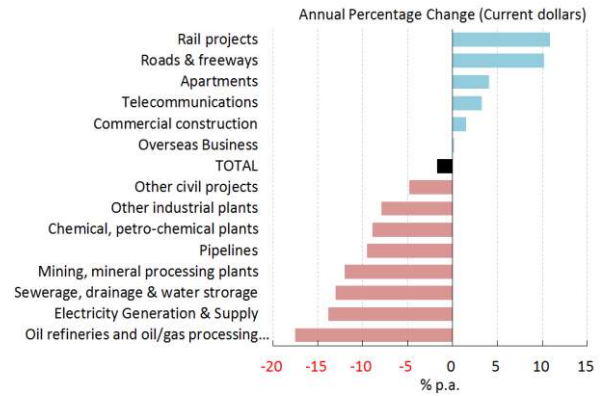
2015 FORECASTS



OUTLOOK 2016

- Turnover from major construction projects is forecast to decline further in 2016, although at a slower rate of 1.7% as public sector capital works programs support a higher overall level of infrastructure activity.
- Engineering construction** is expected to decline by 3.6% driven by a sharp decline of 12.0% in mining construction work. The outlook also remains negative across the heavy industrial sectors. In particular, the value of work in the oil and gas processing sector is set to fall by 17.5% in 2016 as current projects move to completion.
- Within the engineering construction sector, the value of infrastructure work is expected to grow by 2.0% during the year. The next phase of strong investment in urban transport infrastructure is reflected in solid projected rises in revenue from both road (10.2%) and rail projects (10.9%). A return to growth of 3.3% is also projected in telecommunications infrastructure in 2016. Growth in these large infrastructure categories will offset the declines anticipated in other civil projects (-4.8%), pipelines (-9.5%), sewerage, drainage & water supply (-13.0%) and electricity, generation & supply (-13.8%) projects.
- Commercial construction** is projected to grow by just 1.5% in 2016. A modest improvement in private sector building activity (+3.5%) will be supported by projects in the retail, warehousing and accommodation sectors. Public sector building work is expected to be flat reflecting a thin project pipeline and public sector funding constraints.

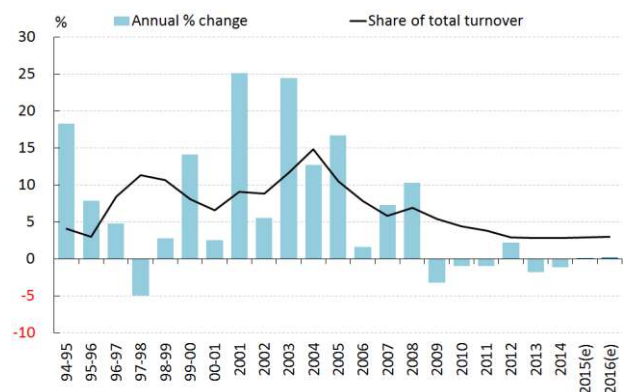
2016 FORECASTS



OVERSEAS BUSINESS

- The overseas business of construction businesses accounted for approximately 3.0% of all construction revenue in 2014, a share which is well below the plus 10% peak years of 2003 to 2005
- Revenue from overseas business fell by 1.1% p.a. in 2014 reflecting a relatively subdued uptake of off-shore projects among respondents. This follows a decline in overseas revenue of 1.8% p.a. in 2013. The strong Australian dollar is likely to have impacted negatively on the local currency value of overseas generated revenue.
- Revenue from overseas business is expected to remain constant through 2015 and 2016, in nominal Australian dollar terms.

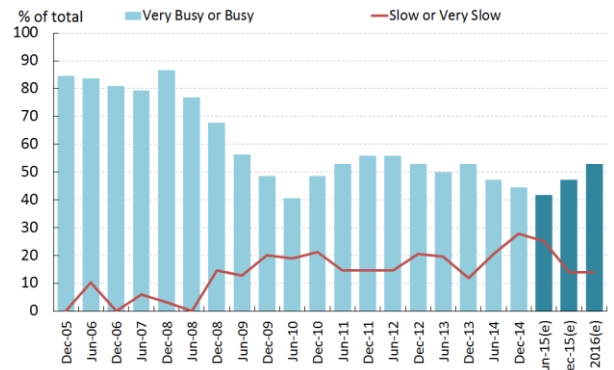
OVERSEAS BUSINESS



LEVELS OF ACTIVITY

- Levels of activity have softened in line with the deterioration in resources and infrastructure project work. Less than one-half (44.4%) of respondents reported very busy or busy activity levels in the six months to December 2014, down from 47.1% in the previous six months period.
- During the first half of 2015, a further reduction in activity is expected with the proportion of businesses anticipating very busy/busy conditions falling to 41.7%.
- For the second half of 2015 activity is projected to strengthen with 47.2% expecting very busy/busy conditions. Continued improvement is expected through 2016 (52.7% expecting to be very busy/busy) as declining mining related construction is moderated by a lift in other key project areas including the next wave of major urban transport projects.
- The average level of industrial/construction capacity in use was 78.9% in February 2015, a fall of 3.9 percentage points from the reading (82.8%) six months earlier.
- The current level of capacity utilisation is the lowest recorded in five years, and is well down on the peak levels of approximately 90.0% recorded in late 2007 and early 2008.

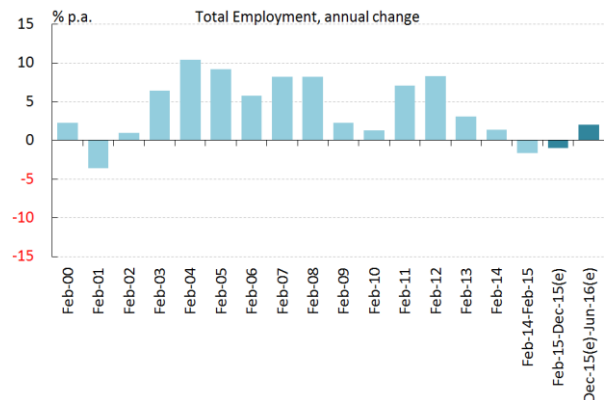
LEVELS OF ACTIVITY



EMPLOYMENT

- Labour market results from the latest survey reveal that employment in non-residential construction is deteriorating in line with the overall weakening in project demand.
- Employment in non-residential construction was reported to have contracted by 1.6% in the year to February 2015 following growth of 1.4% during the previous 12 months. Reduced investment demand and the completion of various major projects has seen reductions in employment concentrated on employees principally engaged on-site (-2.6%) and sub-contract tradesmen (-1.0%). Off-site employment remained broadly unchanged during the twelve months to February 2015.
- Employment is expected to continue to contract over the remainder of 2015. The number of on-site employees and sub-contract tradesmen are forecast to fall by 1.4% and 1.0% respectively. In contrast, off-site employment is expected to rise marginally by 0.6%.
- Thereafter to June 2016, non-residential construction employment is expected to recover, rising by 2.0%. Reflecting the influence of rising infrastructure work, a pick-up is forecast across all employment categories. Growth will be led by a 2.2% increase in the number of on-site employees followed by a 1.9% rise in sub-contract tradesmen and a 1.5% increase in off-site employees.

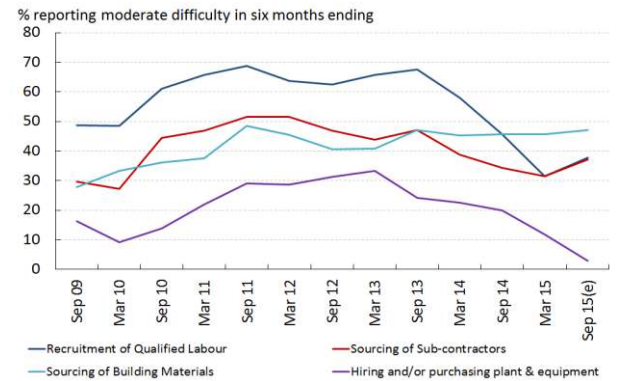
EMPLOYMENT



SUPPLY CONSTRAINTS

- In line with the contraction in major project activity and weaker workforce demand, labour supply constraints have continued to moderate. 31.4% of respondents reported either major or moderate difficulty in the recruitment of skilled labour in the six months to March 2015, but this was down from 45.7% in the previous six months. Sourcing of sub-contractors was also of less concern as a supply constraint in the six months to March 2015, with 31.4% citing major or moderate difficulty (down from 34.3%).
- Sourcing building materials is the most widespread supply constraint currently facing the industry. In total, 45.7% of respondents reported major or moderate difficulty in the sourcing of building materials, unchanged from six months ago.
- Fewer businesses (11.8%) reported major or moderate difficulty in the hiring and purchasing of equipment (20.0% six months ago).
- Over the six months to September 2015, the proportion of businesses expecting difficulty in recruiting skilled labour (37.1% major or moderate) and sub-contractors (37.1%) is expected to increase. For capital supplies, difficulties in the sourcing of building materials will remain particularly widespread (47.1%), but a lower proportion of businesses expect difficulties in the hiring and purchasing of equipment (2.9%).

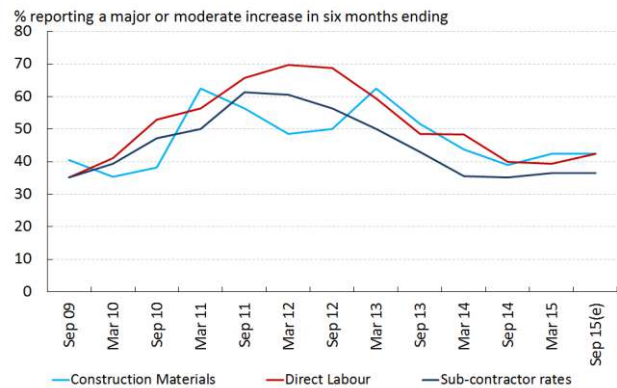
SUPPLY CONSTRAINTS: LABOUR AND CAPITAL



INPUT COSTS

- Despite softer market conditions, labour and construction material costs remain a source of pressure for infrastructure and building projects.
- Consistent with the widespread constraints faced in sourcing building materials, a relatively high 42.4% of businesses cited major or moderate increases in material costs in the six months to March 2015, up from 38.9% citing this level of difficulty six months ago. Contributing to this increase was the impact of the lower Australian dollar which has increased the costs of imported materials in Australian dollar terms.
- Labour cost pressures were broadly unchanged levels over the past six months. In total, 39.4% of respondents reported major or moderate increases in direct labour costs (compared to 40.0% in the previous six months period) while 36.4% reported major or moderate increases for subcontractor rates (compared to 35.1% previously). This reflects the impact on wages growth still flowing from existing EBA's and the difficulties that still exist for a number of businesses in filling skilled vacancies.
- The outlook points to broadly unchanged cost pressures in coming months. Over the six months to September 2015, the proportion of businesses anticipating major or moderate increases is forecast to rise slightly to 42.4% for direct labour costs and remain steady at for construction materials (42.4%) and sub-contractor rates (36.4%).

INPUT COSTS



| Value of turnover in construction work | Share of turnover, 2014 | | 2014 | 2015(f) | 2016(f) |
|---|-------------------------|------------|---------------|---------------|---------------|
| | % of total | % of total | % change p.a. | % change p.a. | % change p.a. |
| Engineering Construction* | 67.6 | | -5.4 | -7.6 | -3.6 |
| (A) Infrastructure | 41.3 | | -7.6 | -4.9 | 2.0 |
| Utilities Infrastructure | 6.3 | | -13.9 | -11.3 | -13.4 |
| - Electricity generation and gas supply | 3.2 | | -3.4 | -11.6 | -13.8 |
| - Sewerage, drainage and water storage | 3.1 | | -22.6 | -11.0 | -13.0 |
| Transport infrastructure | 19.9 | | -7.7 | -0.3 | 10.6 |
| - Roads and freeways | 9.2 | | -7.6 | -2.7 | 10.2 |
| - Rail projects | 10.7 | | -7.7 | 1.8 | 10.9 |
| Telecommunications infrastructure | 3.2 | | -3.1 | -2.0 | 3.3 |
| Other civil projects | 8.7 | | -5.5 | -9.3 | -4.8 |
| Pipelines | 3.2 | | -3.0 | -11.5 | -9.5 |
| (B) Mining & mineral processing construction | 17.0 | | -2.8 | -16.8 | -12.0 |
| (C) Heavy Industrial construction | 9.3 | | -0.2 | -3.2 | -14.6 |
| Chemical, petrochemical plants | 0.9 | | -4.4 | -13.5 | -8.9 |
| Oil refineries and gas processing facilities | 6.3 | | 0.1 | -1.1 | -17.5 |
| Other industrial plants | 2.1 | | 0.5 | -5.4 | -7.9 |
| Commercial construction | 26.1 | | 0.0 | 1.3 | 1.5 |
| Private sector | 11.7 | | 2.3 | 2.5 | 3.5 |
| Public sector | 14.4 | | -1.7 | 0.3 | -0.1 |
| Multi-Apartment Complexes | 3.2 | | 7.1 | 14.9 | 4.1 |
| Overseas Business | 2.8 | | -1.1 | 0.1 | 0.2 |
| Other | 0.3 | | 0.3 | 3.2 | 2.0 |
| Total value of turnover in construction work | 100.0 | | -3.6 | -4.3 | -1.7 |

* Infrastructure, Mining and Industrial Construction

| Employment | Share of employment, Feb 2015 | | Feb 14 – Feb 15 | Exp. Feb 15 – Dec 15 | Exp. Dec 15 – Jun 16 |
|-------------------------|-------------------------------|------------|-----------------|----------------------|----------------------|
| | % of total | % of total | % change | % change | % change |
| On-site employees | 45.9 | | -2.6 | -1.4 | 2.2 |
| Off-site employees | 10.5 | | -0.1 | 0.6 | 1.5 |
| Sub-contract labour | 43.6 | | -1.0 | -1.0 | 1.9 |
| Total employment | 100.0 | | -1.6 | -1.0 | 2.0 |

| Level of activity | Very busy | Busy | Moderate | Slow | Very slow |
|---------------------------------|----------------|----------------|----------------|----------------|----------------|
| | % of companies | % of companies | % of companies | % of companies | % of companies |
| Six months to Jun 2014 | 11.8 | 35.3 | 32.4 | 14.7 | 5.8 |
| Six months to Dec 2014 | 8.3 | 36.1 | 27.8 | 16.7 | 11.1 |
| Expected six months to Jun 2015 | 11.1 | 30.6 | 33.3 | 22.2 | 2.8 |
| Expected six months to Dec 2015 | 11.1 | 36.1 | 38.9 | 13.9 | 0.0 |
| Expected 2016 (year) | 11.1 | 41.7 | 33.3 | 11.1 | 2.8 |

WHAT IS THE CONSTRUCTION OUTLOOK REPORT?

The Australian Industry Group Construction Outlook survey was conducted in February/ March in conjunction with the Australian Constructors Association (ACA), the peak industry body representing the nation's major construction contractors. The survey covered the responses of 100 companies employing approximately 55,000 persons with combined turnover of almost \$25 billion.

SPONSOR STATEMENT

The Australian Constructors Association (ACA) is delighted to be associated with the Australian Industry Group as the major sponsor of one of the most authoritative surveys of Australian construction activity. The survey, which is conducted on a bi-annual basis, provides an excellent barometer on the state of the engineering and non-residential building sectors – on a national and key market basis. We look forward to our continuing association with the survey and its development as the most credible source of information on construction industry activity.

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