

RAIL AND ROADS WILL LIFT MAJOR CONSTRUCTION

Major construction value
2015/16: -9.8% p.a.

Major construction value
2016/17(e): +4.6% p.a.

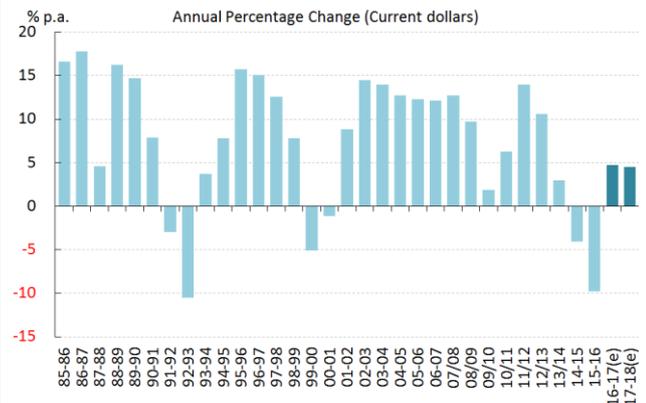
Major construction value
2017/18(e): +4.5%

Major construction jobs
Year to Jun 17: +6.6%

KEY FINDINGS

- The **nation's leading non-residential construction companies** are forecasting a lift in major project work over the course of the 2016/17 and 2017/18 financial years, driven by an upturn in transport infrastructure activity. The pipeline also points to a gradual rise in commercial construction over the next two years and solid levels of apartment construction, albeit slowing from recent peak activity levels in the apartments sector.
- The latest **Australian Industry Group/Australian Constructors Association Construction Outlook survey** indicates that after dropping sharply by 9.8% in 2015/16 (current prices), the total value of major project work is forecast to lift modestly by 4.6% in 2016/17 and a further 4.5% in 2017/18.
- Following a sharp 15% decline in 2015/16, the value of **engineering construction** work is expected to recover by 3.6% in 2016/17 and 3.7% in 2017/18, underpinned by stronger public sector spending on transport infrastructure. Solid growth is also expected in the telecommunications sector in line with rising NBN-related investment, while a rise in revenue from other civil works mainly reflects an expanding project pipeline of bridges and sports complexes.
- Less positively for some parts of engineering construction, reducing resources-related construction (e.g. of LNG facilities) continues to weigh heavily on industry conditions. A substantial further drop is expected in oil and gas sector activity in 2017/18.
- Commercial construction** activity (e.g. offices, retail buildings, warehouses and industrial premises) is expected to recover gradually over the forecast period. After contracting by 3.4% in 2015/16, the value of commercial construction is forecast to rise by 3.5% in 2016/17 followed by a stronger 5.2% expansion in 2017/18. Private sector demand is expected to soften in 2016/17, before stepping up to be the major driver of the sector's growth in 2017/18.
- For **multi-level apartments**, a further increase in turnover of 14.0% is expected in 2016/17. This comes on top of particularly strong growth of 18.6% in 2015/16. Further ahead, a slower pace of growth is expected in 2017/18 (+3.1%) reflecting an imminent peak in activity in the current building cycle, which is concentrated in selected capital cities (mainly Sydney, Melbourne and to a lesser extent, Brisbane).
- Total **employment** in non-residential construction fell in the year to June 2016 in response to the reduction in mining-related work. However, a recovery in employment is expected in 2016/17, as rising infrastructure work leads to an increase in workforce requirements elsewhere.

TURNOVER FROM MAJOR CONSTRUCTION WORK



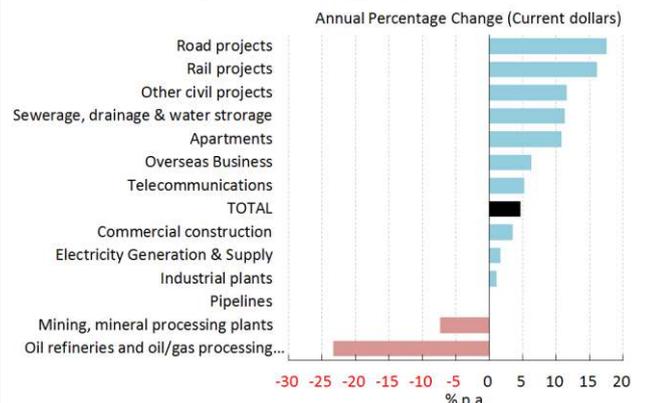
TURNOVER FROM MAJOR CONSTRUCTION WORK: OUTLOOK AT A GLANCE

SECTOR	2015/16 % p.a.	2016/17(e) % p.a.	2017/18(e) % p.a.
Engineering	-15.0	3.6	3.7
Commercial construction	-3.4	3.5	5.2
Multi-level Apartments	18.6	14.0	3.1
Overseas business	7.9	6.3	6.8
Total major construction	-9.8	4.6	4.5

OUTLOOK 2016/17

- The value of turnover from **all major construction work** is expected to recover by 4.6% in 2016/17, following a 9.8% reduction in 2015/16.
- Engineering construction** is expected to rise by 3.6% through the year after falling sharply by 15.0% in 2015/16. The value of **infrastructure-related** engineering work (a sub-set of engineering construction in these data) is expected to rise by 13.5%, driven by strong growth in road (+17.9%) and rail (+16.1%) projects. This is in line with a range of large-scale Government transport projects that are either underway or are in the pipeline.
- In contrast, **resources-related** engineering work will continue to shrink in 2016/17. In particular, the value of work in the oil and gas processing sector is set to fall sharply again in 2016/17 (down by 23.3% after declining by 22.4% in 2015/16) as the LNG projects finish construction. More positively, the drag from reduced mining-related construction (other than oil and gas) is expected to lessen in 2016/17 with a slower fall of 7.3% predicted for revenue from mining projects, following a 31.0% drop in 2015/16.
- The **commercial construction sector** is expected to grow modestly by 3.5% in 2016/17. This outlook is consistent with relatively subdued approvals and commencements evident across various commercial property markets during 2015/16.

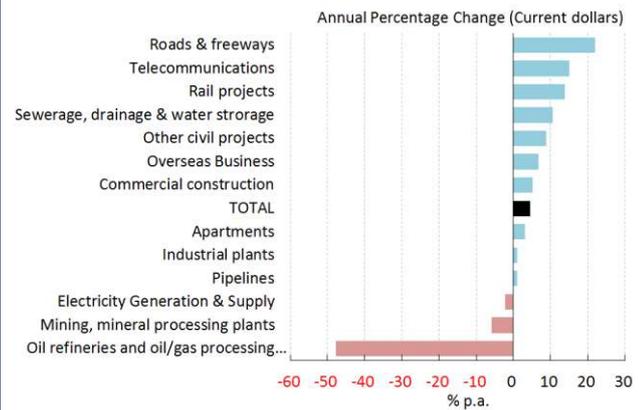
2016/17 FORECASTS



OUTLOOK 2017/18

- Turnover from **all major construction work** is forecast to grow by 4.5% in 2017/18 as public sector capital works programs continue to support higher levels of activity.
- Engineering construction** is expected to grow by a further 3.7% in 2017/18. This reflects the positive contribution to **infrastructure-related engineering** activity from increases in revenue from road (+21.9%) and rail projects (+13.9%) and more robust conditions in the telecommunications sector (+15.0%) as more NBN-related projects move into the construction phase. The outlook is positive for other civil projects also, with strong growth in the sewerage and drainage sector (+10.5%) due to rising demand for services from a bigger population and more housing and commercial properties.
- Resources-related engineering construction** is expected to continue to decline in 2017/18. Weakness is expected to be mainly concentrated in the oil and gas processing sector (-47.8%) while mining-related construction is set to fall at a slower rate of -5.9%.
- Commercial construction** is projected to show a stronger upturn in 2017/18 (+5.2%). Growth is expected to be led by private sector building activity (+6.7%). Public sector building work is expected to be slower (+3.8%) reflecting a thinner project pipeline, and the completion of a number of large public health sector projects.

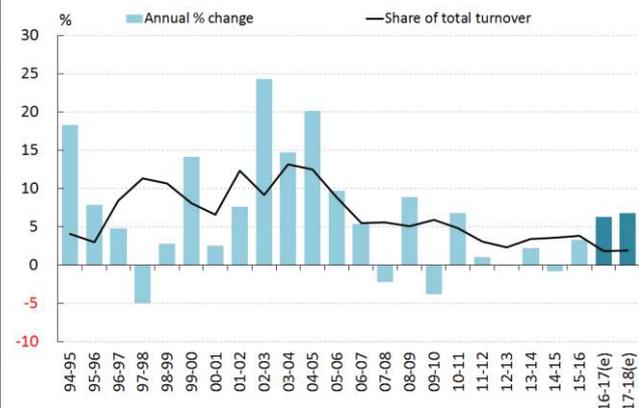
2017/18 FORECASTS



OVERSEAS BUSINESS

- The overseas business of the major construction sector accounted for approximately 2.0% of all major construction revenue in 2015/16, well below the peak of 13.2% twelve years ago in 2003-04.
- Revenue from overseas business increased by 7.9% in 2015/16 (in nominal Australian dollars). The lower Australian dollar is likely to have had a positive influence on this, by raising the local currency value of overseas generated revenue. This growth follows an increase in overseas revenue of 3.6% p.a. in 2014/15.
- The outlook indicates further growth over the next two years, with revenue from overseas business expected to rise by 6.3% in 2016/17 followed by a further increase of 6.8% in 2017/18.

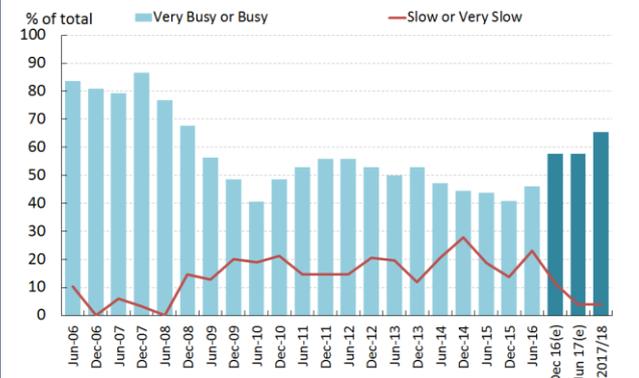
OVERSEAS BUSINESS



LEVELS OF ACTIVITY

- Consistent with the continued contraction in mining investment, less than one-half (46.1%) of respondents reported 'very busy' or 'busy' activity levels during the six months to June 2016. This was up from 40.9% in the previous six-month period but it was still relatively low, compared to results in 2011 and 2012 or further back in 2006 and 2007.
- Over the second half of 2016, activity is expected to recover somewhat, with 57.7% of businesses anticipating 'very busy' or 'busy' conditions. This reflects stronger infrastructure-related construction activity that will partly offset waning resources-related construction activity.
- Activity levels are expected to hold steady at this higher level through the first half of 2017 and to lift further during 2017/18, with 65.4% of respondents expect 'very busy' or 'busy' levels of activity in 2017/18.
- The average level of industrial and construction capacity in use was 86.0% in August/September 2016, a rise of 1.8 percentage points from 84.2% a year earlier. Despite this improvement, the current capacity utilisation rate is still well below the peak of approximately 93% recorded during the mining investment boom in early 2008.

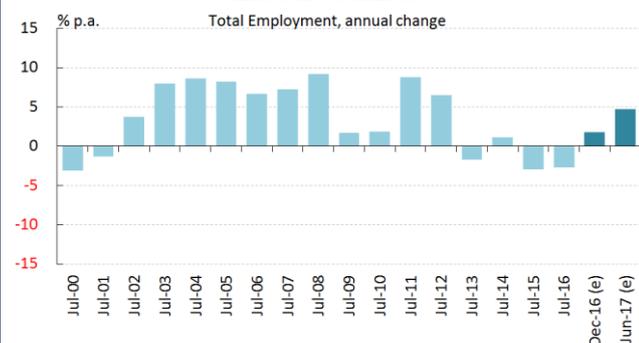
LEVELS OF ACTIVITY



EMPLOYMENT

- Reflecting the drop in major project activity in 2015/16, employment in major construction contracted by 2.7% in the year to July 2016 following a decline of 2.9% during the previous 12 months. Due to cutbacks in resources investment and project completions or deferrals, reductions in employment over this period were concentrated in sub-contract tradesmen (-2.7%) and employees principally engaged on-site (-2.9%). Off-site employment fell at a slower rate of 1.4% during the twelve months to July 2016.
- For 2016/17, a strengthening recovery in workforce resourcing requirements is expected to build up through the year, in response to rising infrastructure-related work.
- Over the second half of 2016, increases are forecast in the industry's two major employment categories: on-site (+3.5%) and sub-contract tradesmen (+2.3%). These rises are expected to outweigh a further decline in off-site employment (-6.4%).
- Further ahead, in the six months to June 2017, total employment is expected to increase at a stronger rate of 4.7%. Growth will be mainly boosted by a 6.2% increase in the number of on-site employees, with the numbers of off-site workers and sub-contractors lifting by 2.7% and 3.3% respectively in this six-month period.

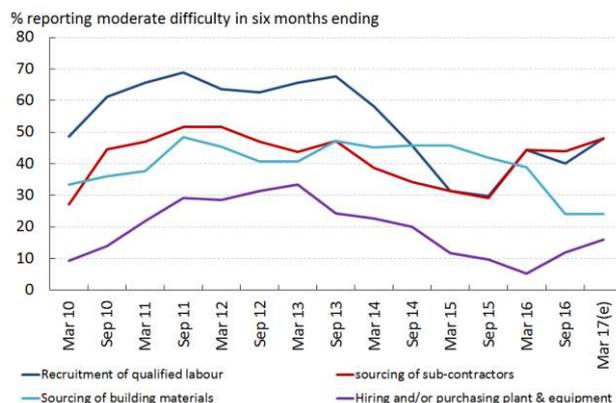
EMPLOYMENT



SUPPLY CONSTRAINTS

- **Labour shortages** are re-emerging in 2016 as major infrastructure works come on stream. A relatively high 40.0% of respondents reported either 'major' or 'moderate' difficulty in recruiting skilled labour in the six months to September 2016, down only slightly from a relatively elevated 44.4% in the previous six months. Sourcing sub-contractors also remained a key concern in the six months to September 2016, with 44.4% citing 'major' or 'moderate' difficulty, unchanged from the proportion citing this level of concern in the previous six months.
- Looking ahead, over the six months to March 2017, more businesses expect difficulty with recruiting skilled labour (48.0% expect major or moderate difficulty) and sourcing sub-contractors (48% expect major or moderate difficulty).
- Sourcing **building materials** was of less concern for the industry in the six months to September 2016, with 24.0% of respondents reporting 'major' or 'moderate' difficulty, down from 38.9% six months earlier.
- However, a higher proportion of businesses (12.0%) reported 'major' or 'moderate' difficulty with hiring and purchasing equipment (up from 5.3% six months earlier).
- For capital supplies, more businesses expect major or moderate difficulties with hiring and purchasing equipment (16.0%) over the six months to March 2017. The same proportion expect difficulties with sourcing building materials (24.0%).

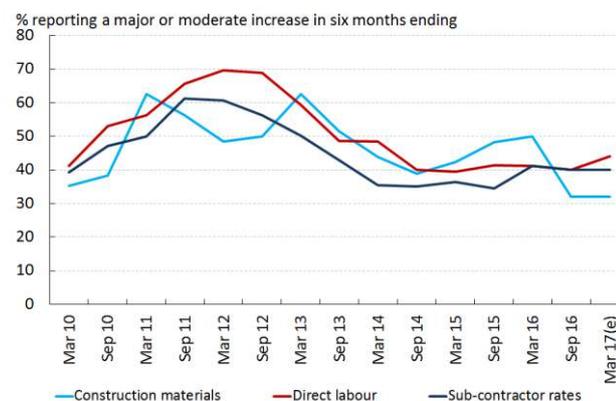
SUPPLY CONSTRAINTS: LABOUR AND CAPITAL



INPUT COSTS

- **Labour costs** remain a source of pressure for the construction of infrastructure and building projects. Upward pressures on direct labour costs are expected to be sustained as large infrastructure projects move from the planning pipeline into the construction phase and contractors increasingly compete for the same pool of skilled labour.
- Over the six months to September 2016, 40.0% of respondents reported 'major' or 'moderate' increases in sub-contractor labour rates while 40.0% also reported 'major' or 'moderate' increases for direct labour rates. These proportions were down slightly from 41.2% reporting 'major' or 'moderate' rises for both direct labour and sub-contractor rates six months earlier.
- Looking ahead, in the six months to March 2017, a higher proportion of businesses expect 'major' or 'moderate' increases in direct labour costs (44.0% major or moderate increase). About the same proportion of businesses (40.0%) expect 'major' or 'moderate' pressure on sub-contractor rates in the six months to March 2017 as they did in the six months to September 2016.
- Reports of increases in **construction material costs** remain relatively widespread in 2016, but these rises have eased off to some extent, with 32.0% of businesses reporting 'major' or 'moderate' increases in the cost of materials in the six months to September 2016. This compares with 50.0% citing 'major' or 'moderate' increases six months earlier. The continuing decline in mining investment activity compared with a year ago appears to have taken some of the heat out of demand for and therefore the cost of construction materials.
- Looking ahead, the same proportion of businesses (32.0%) expect 'major' or 'moderate' rises in the cost of construction materials in the six months to March 2017 as they did in the six months to September 2016.

INPUT COSTS



Value of turnover in construction work	Share of turnover, 2015/16	2015/16	2016/17(e)	2017/18(e)
	% of total	% change p.a.	% change p.a.	% change p.a.
Engineering Construction*	60.9	-15.0	3.6	3.7
(A) Infrastructure	37.2	-5.4	13.5	14.0
Utilities Infrastructure	4.7	-1.3	7.4	5.6
- Electricity generation and gas supply	1.9	-11.2	1.7	-2.3
- Sewerage, drainage and water storage	2.8	6.7	11.3	10.5
Transport infrastructure	21.5	-8.5	16.9	17.4
- Roads and freeways	9.2	-9.5	17.9	21.9
- Rail projects	12.3	-7.7	16.1	13.9
Telecommunications infrastructure	3.5	14.6	5.3	15.0
Other civil projects	7.2	-7.1	11.6	8.9
Pipelines	0.3	17.8	0.0	1.0
(B) Mining & mineral processing construction	13.6	-31.0	-7.3	-5.9
(C) Heavy Industrial construction	10.1	-11.1	-25.5	-10.1
Oil refineries and gas processing facilities	7.9	-22.4	-23.3	-47.8
Industrial plants	2.2	-11.1	1.1	1.4
Commercial construction	30.6	-3.4	3.5	5.2
Private sector	14.9	3.4	1.7	6.7
Public sector	15.7	-9.0	5.2	3.8
Multi-Apartment Complexes	6.0	18.6	14.0	3.1
Overseas Business	1.9	7.9	6.3	6.8
Other	0.6	-7.0	59.6	33.9
Total value of turnover in construction work	100.0	-9.8	4.6	4.5

* Infrastructure, Mining and Industrial Construction

Outlook

Employment	Share of employment, July 2016 % of total	July 15 – July 16 % change	Exp. July 16 – Dec 16 % change	Exp. Dec 16 – Jun 17 % change	Exp. July 16 – Jun 17 % change
On-site employees	48.2	-2.9	3.5	6.2	9.9
Off-site employees	12.0	-1.4	-6.4	2.7	-3.9
Sub-contract labour	39.8	-2.7	2.3	3.3	5.7
Total employment	100.0	-2.7	1.8	4.7	6.6

Level of activity	Very busy	Busy	Moderate	Slow	Very slow
	% of companies				
Six months to Dec 2015, actual	13.6	27.3	45.5	9.1	4.5
Six months to Jun 2016, actual	19.2	26.9	30.8	15.4	7.7
Six months to Dec 2016, expected	26.9	30.8	30.8	7.7	3.8
Six months to Jun 2017, expected	23.1	34.6	38.5	0.0	3.8
Expected 2017/18 (financial year)	19.2	46.2	30.8	0.0	3.8

WHAT IS THE CONSTRUCTION OUTLOOK REPORT?

The Australian Industry Group Construction Outlook survey was conducted in August/September 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 62,000 persons with combined turnover of around \$23 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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