Current And Future Market Escalation View – Q1 2023

In Q1 2023 we have seen the Australian construction market start to show a decline, primarily in the private sector, due to high interest rates and construction costs.

The industry continues to face challenges due to labour and material shortages which have led to increased costs and project delays. In contrast, freight costs have returned to pre-covid rates, fuel prices have stabilised, and corrections to electrical equipment, steel and timber products have contributed to a slowdown in construction cost escalation. As highlighted in our update below, construction cost increases are persisting but at a declining rate.

The construction market continues to show a recovery from supply chain disruptions. While materials supply has increased, demand has subsided due to projects being delayed. The global pandemic, which led to shipping and logistics challenges, is officially over and governments are exploring ways to increase the availability of skilled labour through improvements to immigration processing times and a higher intake volume. This will be complimented by the return of overseas students.

In NSW, ongoing enterpise bargaining agreement (EBA) negotiations continue to drive labour costs for new and existing projects - a departure from tradition, where reformed EBA agreements applied to new projects only. Current negotiations will potentially result in a 5-7% increase to labour rates which could substantially contribute to the forecasted annual escalation. The Reserve Bank of Australia's (RBA) target of reducing inflation to 2-3% by April 2024 could be optimistic based on the current rate of 7% - a minimal decrease from the 30-year peak recorded in Q4 2022. Banking sector sentiments indicate further

MBM View on Building Cost Escalation	2022	2023	2024	2025
New South Wales	9.5%	5.0%	3.0%	2.5%
Victoria	7.8%	4.5%	3.0%	3.0%
Queensland	10.9%	4.0%	3.0%	2.5%
South Australia	6.2%	4.0%	2.5%	2.5%
Western Australia	7.4%	5.5%	3.5%	2.5%

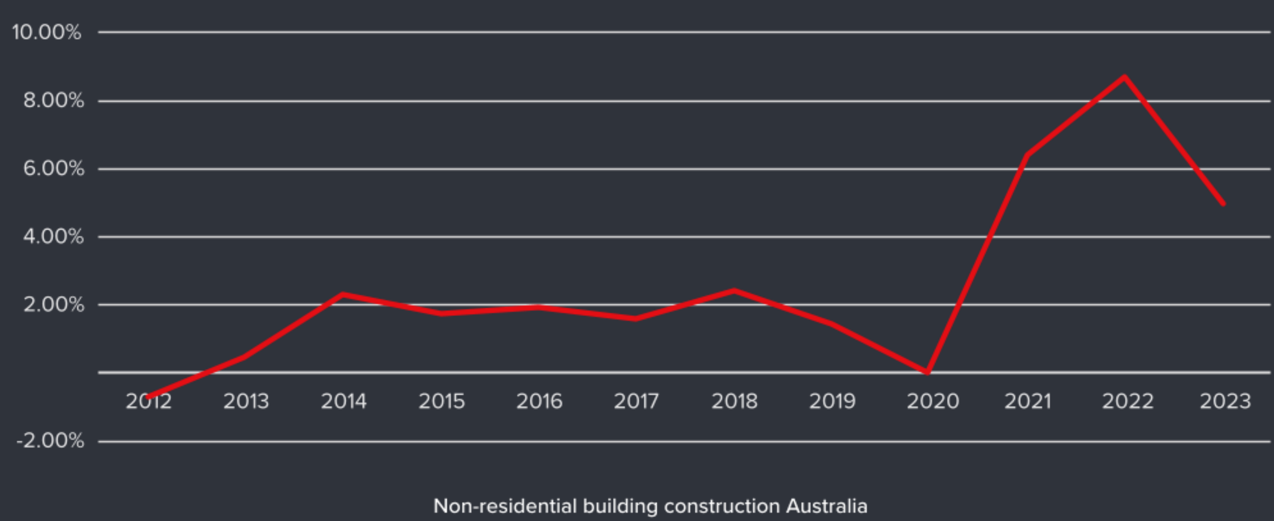
interest rate hikes are on the horizon to facilitate contractions in high inflation. These decisions will continue to put pressure on project feasibilities and create the potential for further delays.

The first quarter of 2023 has seen increases to concrete, clay and ceramic product prices, while reinforcement, steel and timber costs have slightly reduced from major increases over the past two years. Plumbing and electrical trades have contributed to increases due to the rising costs of materials such as copper and plastic. Recent tender returns indicate a strong resurgence of sub-contractors into the tender market. The signal is encouraging for contractors with regard to lump sum tenders on projects which can commence on site within 3 months of submission.

Despite the multidimensional challenges faced by the construction market, optimism remains regarding future growth prospects for the industry. MBM's outlook is consistent with the view that market escalation peaked in Q4 2022 and will continue to reduce throughout 2023. We forecast a stablisation in escalation towards the end of 2023 and into 2024. However, it is predicted that input costs and wage pressures will continue to drive market surges in the short-to-medium term.

Despite the multidimensional challenges faced by the construction market, optimism remains regarding future growth prospects for the industry.

Historic Construction Escalation in Australia



Source: https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/producer-price-indexes-australia/latest-release#construction

ABS Data for various states

New South Wales	Building construction New South Wales			Non-residential building construction New South Wales		
		% Change per Quarter	% Change per Year		% Change per Quarter	% Change per Year
Q2 2020	125.8	-0.32%		120.4	-0.17%	
Q3 2020	125.9	0.08%		120.7	0.25%	
Q4 2020	**125.4**	**-0.40%**	**-0.79%**	**119.7**	**-0.83%**	**-1.48%**
Q1 2021	125.3	-0.08%		119.7	0.00%	
Q2 2021	129.1	3.03%		123.7	3.34%	
Q3 2021	130.8	1.32%		124.2	0.40%	
Q4 2021	**135.5**	**3.59%**	**8.05%**	**129.3**	**4.11%**	**8.02%**
Q1 2022	139.1	2.66%		132.1	2.17%	
Q2 2022	144.0	3.52%		135.7	2.73%	
Q3 2022	147.9	2.71%		138.5	2.06%	
Q4 2022	**150.1**	**1.49%**	**10.77%**	**140.8**	**1.66%**	**8.89%**
Q1 2023	153.6	**2.33%**		143.6	**1.99%**	

Victoria	Building construction Victoria			Non-residential building construction Victoria		
		% Change per Quarter	% Change per Year		% Change per Quarter	% Change per Year
Q2 2020	112.8	0.36%		106.4	0.85%	
Q3 2020	113.1	0.27%		106.4	0.00%	
Q4 2020	**114.1**	**0.88%**	**1.69%**	**107.2**	**0.75%**	**1.61%**
Q1 2021	114.7	0.53%		107.3	0.09%	
Q2 2021	115.6	0.78%		108.2	0.84%	
Q3 2021	116.7	0.95%		108.5	0.28%	
Q4 2021	**118.1**	**1.20%**	**3.51%**	**109.2**	**0.65%**	**1.87%**
Q1 2022	121.3	2.71%		111.2	1.83%	
Q2 2022	126.3	4.12%		113.5	2.07%	
Q3 2022	129.8	2.77%		115.6	1.85%	
Q4 2022	**133.2**	**2.62%**	**12.79%**	**119.7**	**3.55%**	**9.62%**
Q1 2023	133.2	**0.00%**		120.7	**0.84%**	

Queensland	Building construction Queensland			Non-residential building construction Queensland		
		% Change per Quarter	% Change per Year		% Change per Quarter	% Change per Year
Q2 2020	120.1	0.17%		117.4	0.00%	
Q3 2020	119.4	-0.58%		116.5	-0.77%	
Q4 2020	**121.2**	**1.51%**	**0.58%**	**118.0**	**1.29%**	**0.51%**
Q1 2021	122.2	0.83%		118.8	0.68%	
Q2 2021	124.4	1.80%		120.8	1.68%	
Q3 2021	130.8	5.14%		126.5	4.72%	
Q4 2021	**135.6**	**3.67%**	**11.88%**	**128.4**	**1.50%**	**8.81%**
Q1 2022	139.7	3.02%		130.8	1.87%	
Q2 2022	146.1	4.58%		135.6	3.67%	
Q3 2022	150.1	2.74%		138.9	2.43%	
Q4 2022	**151.2**	**0.73%**	**11.50%**	**139.9**	**0.72%**	**8.96%**
Q1 2023	152.4	**0.79%**		141.8	**1.36%**	

South Australia	Building construction South Australia			Non-residential building construction South Australia		
		% Change per Quarter	% Change per Year		% Change per Quarter	% Change per Year
Q2 2020	109.6	-0.18%		110.0	0.00%	
Q3 2020	107.5	-1.92%		106.9	-2.82%	
Q4 2020	**107.9**	**0.37%**	**-1.37%**	**106.7**	**-0.19%**	**-2.82%**
Q1 2021	109.4	1.39%		107.6	0.84%	
Q2 2021	110.7	1.19%		108.7	1.02%	
Q3 2021	112.6	1.72%		109.3	0.55%	
Q4 2021	**115.8**	**2.84%**	**7.32%**	**110.1**	**0.73%**	**3.19%**
Q1 2022	118.7	2.50%		111.9	1.63%	
Q2 2022	122.2	2.95%		113.8	1.70%	
Q3 2022	126.5	3.52%		115.2	1.23%	
Q4 2022	**129.2**	**2.13%**	**11.57%**	**117.8**	**2.26%**	**6.99%**
Q1 2023	131.4	**1.70%**		119.1	**1.10%**	

Source: https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/producer-price-indexes-australia/latest-release#construction
Table 30 Contribution to input to the house construction industry index, weighted average of six state capital cities, index points

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