

A wide-angle photograph of a city skyline at dusk or night. The sky is a deep blue with some light clouds. Numerous skyscrapers and buildings are illuminated with warm yellow and white lights, their reflections shimmering on the water in the foreground. A multi-lane highway bridge with several support pillars spans across the water, with some traffic visible. The overall scene is a vibrant urban landscape.

Q1 2024 MBM Escalation Update

Navigating the economic forces shaping
escalation in the Australian construction industry

“We expect optimism to be at the forefront of development outlooks with positive building cost escalation forecasts for 2024.....”

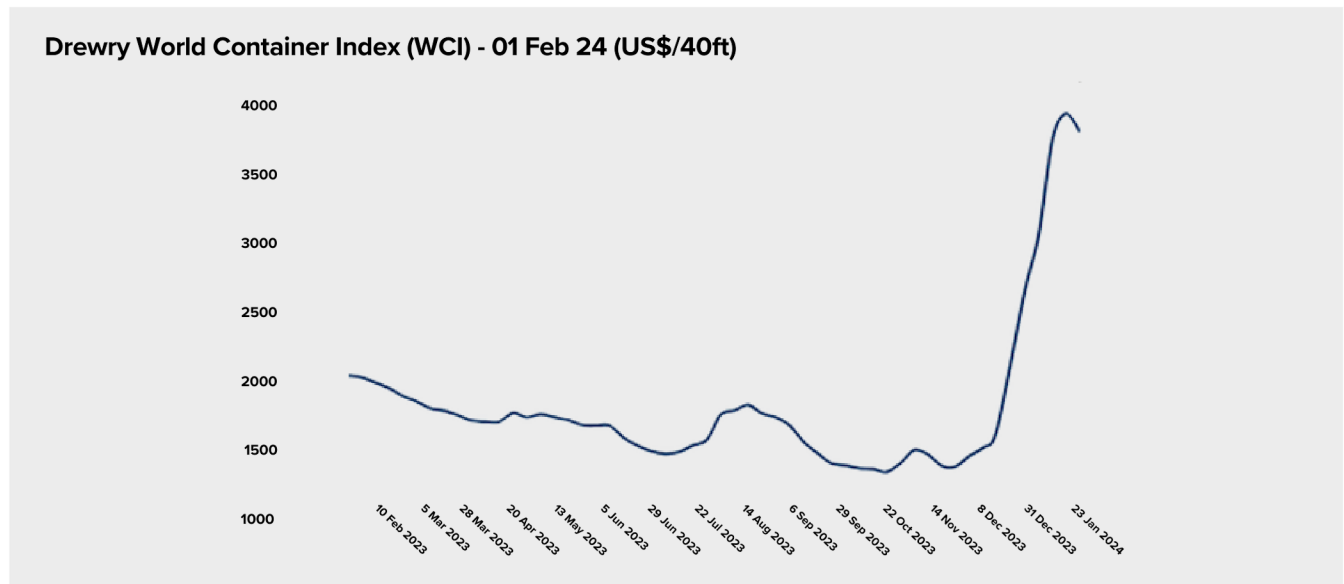
The latest indices published by Australian Bureau of Statistics (ABS) for Q4 2023 show the return of the Building Price Index (BPI) towards normal trends following the easing of the past four quarters. New South Wales, Queensland, and South Australia aligned with MBM's expectations and resulted in a 5.97%, 5.86%, and 4.24% increase respectively for the year. In contrast, Victoria reflected a fourth quarter increase of 5.11% and an overall increase of 8.19% throughout 2023, which differed from MBM's view of the market and actual tenders received over the period.

We expect optimism to be at the forefront of development outlooks, as positive forecasts for building cost escalation in 2024 emerge after three years of surging material and labour costs. According to the RICS Construction Activity Index, Australia's construction market activity maintained stability from Q2 to Q4 2023, albeit relatively low when compared to other APAC markets. Encouragingly, the 12-month market expectation for Private Residential and Private Non-Residential developments are positive and signal a rebound, while public infrastructure is projected to sustain its elevated levels.

The last two quarters of 2023 saw the stabilisation of material prices and the alleviation of supply chain constraints. Key materials such as reinforcement steel, structural steel, and timber exhibited constancy, while certain elements, notably concrete, remained subject to volatility. Importantly, Australia's reliance on import materials, such as glazing, aluminium, steel, lighting, and equipment raises concerns of potential price escalations.

The risk of supply chain disruptions in early 2024 stems from the ongoing conflict in the Middle East and creates the potential for substantial increases in shipping costs and consequently, program delays. As illustrated below, the Drewry World Container Index (WCI) has recorded a significant 150% surge in the past two months from December 2023 to February 2024.

Source: Drewry Supply Chain Advisors, 1 February 2024
<https://www.drewry.co.uk/supply-chain-advisors/supply-chain-expertise/world-container-index-assessed-by-drewry>



“MBM anticipates a subdued landscape in the Australian construction market during the initial phase of 2024, with projects expected to continue grappling with inflationary pressures, elevated interest rates, and ongoing labour shortages.”

Turning to labour trends, Enterprise Bargaining Agreements (EBAs) remain a key driving factor in current building cost escalation trends with many agreements up for renewal and rates in excess of the current Consumer Price Index (CPI). In Q4 2023, skilled labour continued to be an escalation cost driving factor. While government infrastructure projects are vital to the economy, public projects are attracting much of the skilled labour due to the competitive salaries on offer - to the detriment of the commercial sector.

In addition to absorbing much of the available labour, public projects secure highly reputable contractors over private developers. The demand for labour is demonstrated in the latest unemployment figures and skilled shortage lists as published by Jobs and Skills Australia with key occupations in the construction industry remaining on the lists. Consequently, private sector organisations are being forced to hire and train inexperienced labour market participants, resulting in inefficiencies, lower productivity, and longer program durations.

The labour shortage affecting the private and commercial sector is expected to continue over upcoming years across most states. Queensland, with its huge infrastructure pipeline planned to take place over the next 8 years, will propel the imbalance between public and private sector labour availability namely due to the Capacity Expansion Program investment of a \$10bn Health program, \$5bn Corrections program, and a \$3bn Education program followed by the 2032 Olympics Games. Trades that overlap heavily between the private sector and infrastructure projects are susceptible to higher price volatility due to supply and demand issues with the available pool of resources being put under severe strain.

In the face of economic uncertainties, experts do not foresee a decline in construction costs, but rather slowing rates of escalation in most states. The viewpoint is shaped by a myriad of macro, micro, and industry-specific factors, collectively exerting a complex influence on the economic environment. Anticipated contributors to construction escalation include as shipping costs, fuel prices, building approvals, labor market dynamics, and public expenditure.

With the latest published twelve month CPI index of 4.1% for the December 2023 quarter and only 0.6% over Q4 2023, cash rate cuts seem increasingly likely towards the second half of 2024 and could lead to relief for the Australian construction industry. Additionally, the reduction in building approvals, as published by the ABS, could lead to a shortfall in new projects resulting in lower cost escalation due to increased capacity and competition in the construction sector.

MBM anticipates a subdued landscape in the Australian construction market during the initial phase of 2024, with projects expected to continue grappling with inflationary pressures, elevated interest rates, and ongoing labour shortages. Although major public developments, particularly in transport and health, persist as key industry drivers, a resurgence in private sector projects is foreseen as the year advances. The renewed activity is expected to create a more predictable escalation trajectory in alignment with a reduction in CPI towards long-term averages. In turn, development trends are poised to enhance certainty surrounding project financing costs.

MBM view on Building Cost Escalation					
	2023	2024	2025	2026	2027
NSW	6.0%	3.0%	2.5%	3.0%	2.5%
VIC	6.0%	5.0%	4.0%	3.0%	2.5%
QLD	6.5%	6.0%	6.0%	4.5%	4.5%
SA	4.0%	4.0%	4.0%	3.0%	2.5%
WA	5.5%	3.5%	2.5%	2.0%	2.5%

3.9%

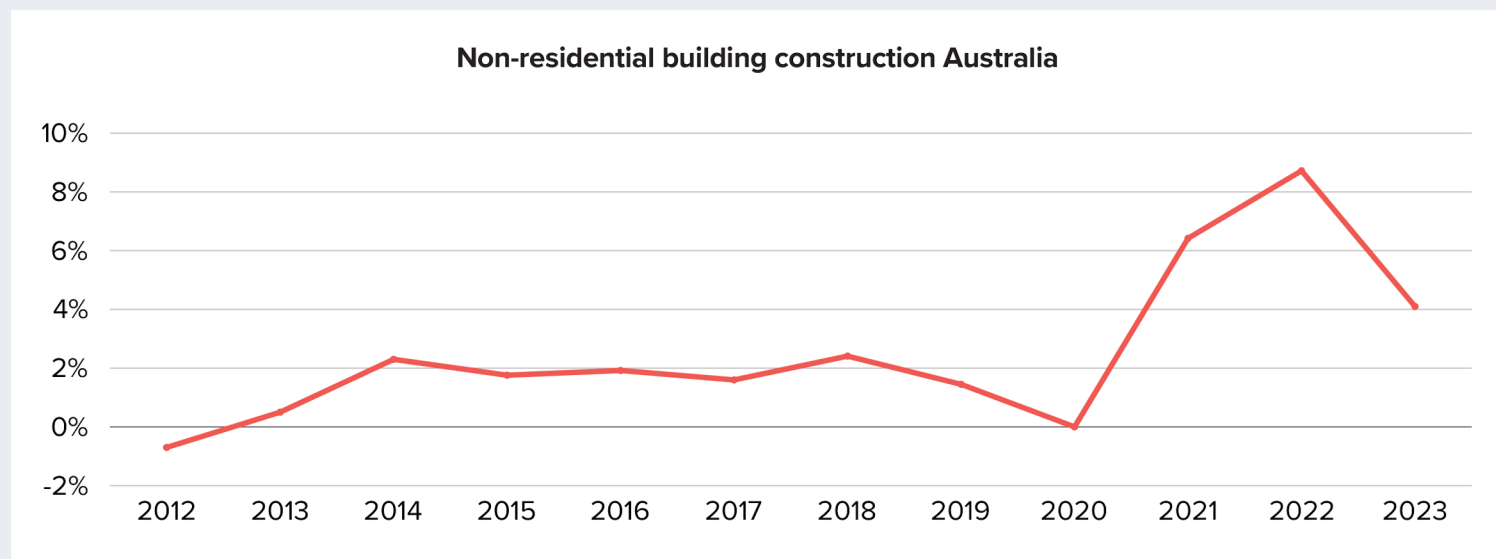
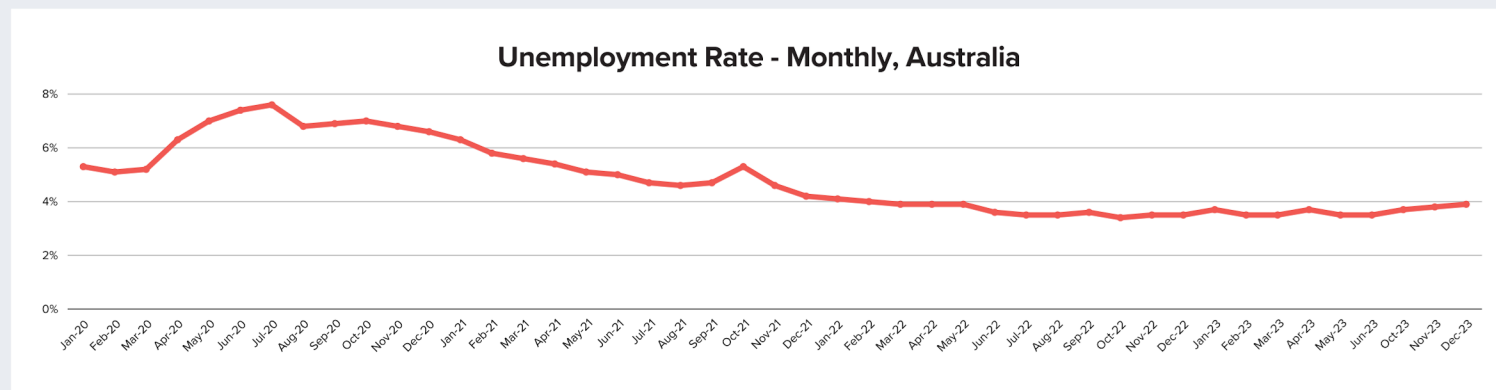
The seasonally adjusted unemployment rate in Australia experienced a marginal uptick, rising from 3.8% in November to 3.9% in December. The change aligned with a reduction of 65,000 individuals categorised as employed, with indications that the figures may be influenced by the seasonal nature of employment during the Christmas period.

New South Wales

has exhibited a notable increase of 1.36% in Q4 2023. For the year, growth for non-residential building constructions was reported at 5.97%. These figures underscore NSW's role as a vibrant hub for non-residential construction.

Surprisingly, Victoria

reported a 5.11% increase for the preceding quarter and an 8.19% rise for the year. Queensland recorded a minimal increase in construction costs during the fourth quarter, signaling an easing of economic factors.



Advisory Outlook

MBM’s outlook is that the continued slowing of the labour market during the early part of 2024 will continue to see increased Facilities Management and Asset Management costs in the short term.

The unemployment and underemployment rates remained relatively stable from October to December 2023. However, notable increases in vacancy numbers were observed in five states – Tasmania, New South Wales, South Australia, Western Australia, and Queensland. The persistent trend of rising unemployment since November 2022 combined with elevated underemployment rates, a deceleration in employment, and a decline in hours worked suggests a potential prolonged slowdown in the labour market.

In regional and remote areas, a notable labour shortage of Technicians and Trade Workers is occurring. As service delivery organisations compete for limited resources, potential cost escalations may occur beyond CPI for reactive, planned, and statutory maintenance. The slight decline in full-time employment and rise in part-time employment - constituting 30.8% of total employment - showcases the attractiveness of part-time roles in the Facilities Management (FM) sector to employees.

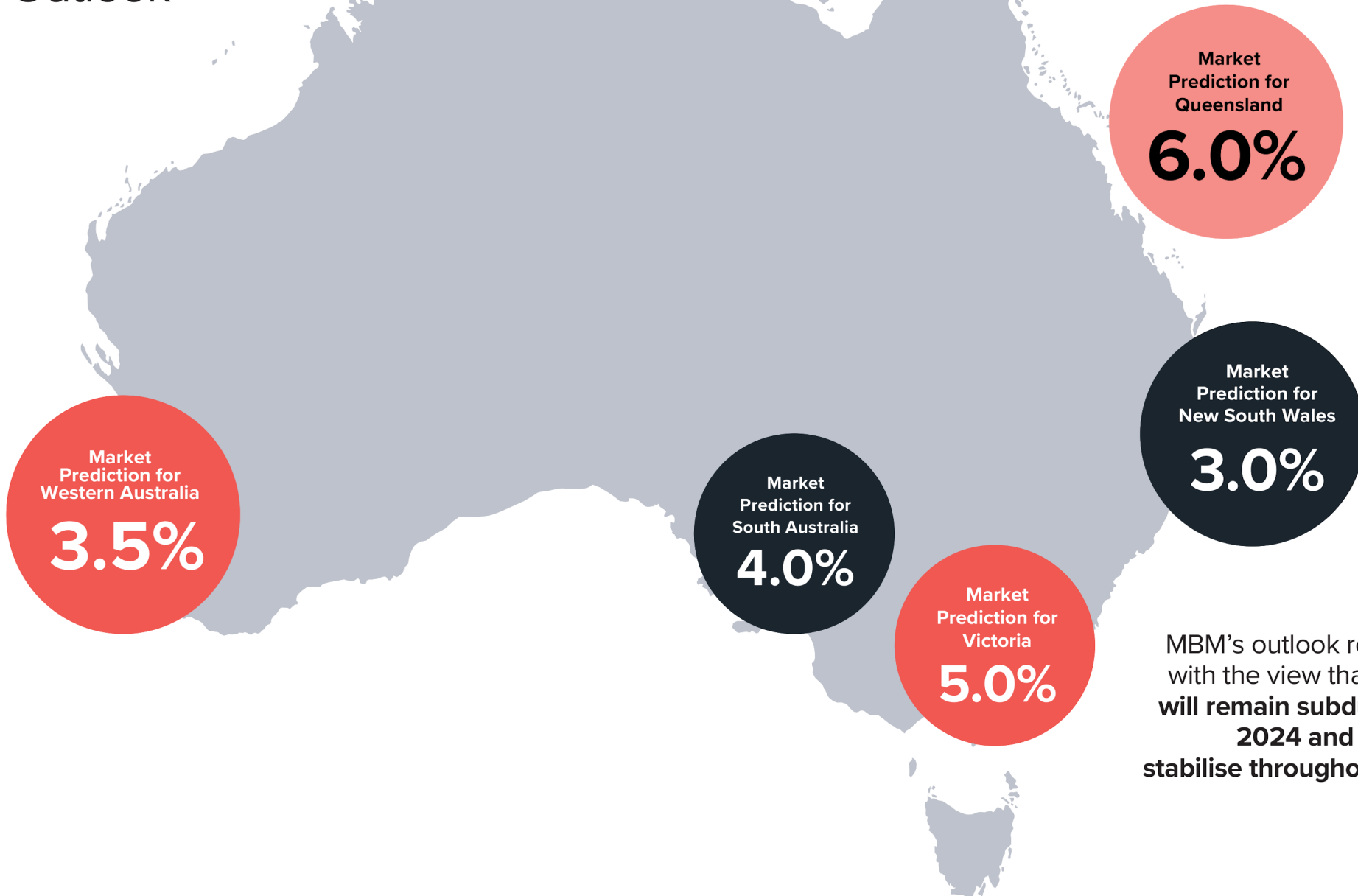
The seasonally adjusted Wage Price Index (WPI) increased by 1.3% for the quarter and 4.0% over the year. Although below the modern award and national minimum wage increases (4.5% to 5.5%), this signifies that facilities and asset management companies may seek adjustments outside the contract cycle to offset impacts on their profit margins. Contracts that are in the early stages of the contract term are unlikely to see significant change. Contracts that are in the mid-to-late stages may see service providers seeking out-of-cycle cost adjustments to reduce pressure on profit margins.

All sector WPI, quarterly and annual movement (%) seasonally adjusted (a)



Although the trends indicate a stronger labour market, it is likely that the continued slowing of the labour market will continue to see increased FM and Asset Management in the short term.

2024 Escalation Outlook



MBM’s outlook remains as is with the view that escalation will remain subdued in early 2024 and continue to stabilise throughout the year.

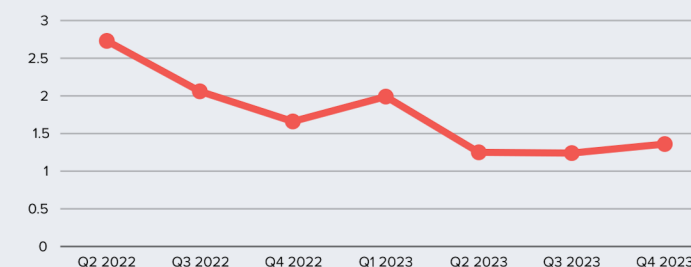
ABS Data for New South Wales



Non-Residential Building Construction Change Per Annum

▼	-1.48%	2020
▲	8.02%	2021
▲	8.89%	2022
▲	5.97%	2023

Non-Residential Building Construction Change Per Quarter



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%	
Q2 2023	155.3	1.11%		145.4		1.25%	
Q3 2023	157.4	1.35%		147.2		1.24%	
Q4 2023	159.3	1.21%	6.13%	149.2		1.36%	5.97%

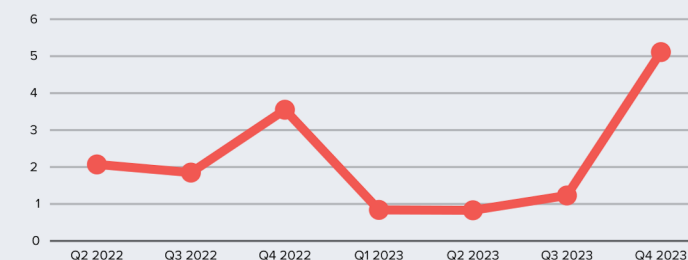
ABS Data for Victoria



Non-Residential Building Construction Change Per Annum

▲	1.61%	2020
▲	1.87%	2021
▲	9.62%	2022
▲	8.19%	2023

Non-Residential Building Construction Change Per Quarter



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%	
Q2 2023	134.5	0.98%		121.7		0.83%	
Q3 2023	135.6	0.82%		123.2		1.23%	
Q4 2023	140.5	3.61%	5.48%	129.5		5.11%	8.19%

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

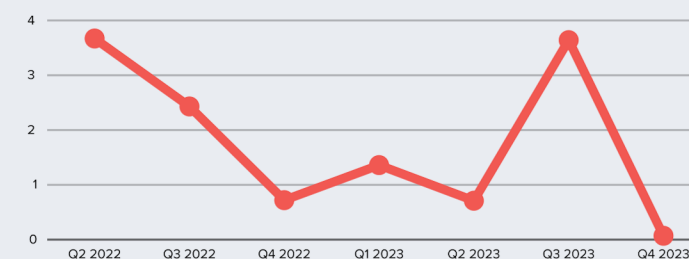
ABS Data for Queensland



Non-Residential Building Construction Change Per Annum

▲	0.51%	2020
▲	8.81%	2021
▲	8.96%	2022
▲	5.86%	2023

Non-Residential Building Construction Change Per Quarter



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%	
Q2 2023	153.8	0.92%		142.8		0.71%	
Q3 2023	157.2	2.21%		148.0		3.64%	
Q4 2023	157.4	0.13%	4.10%	148.1		0.07%	5.86%

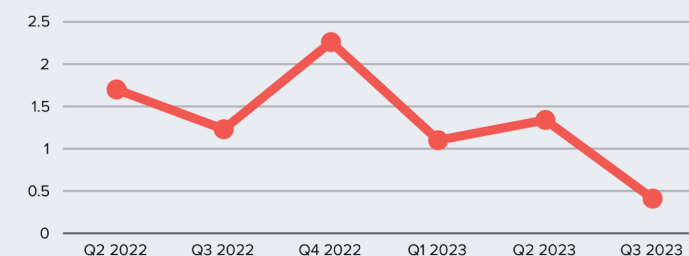
ABS Data for South Australia



Non-Residential Building Construction Change Per Annum

▼	-2.82%	2020
▲	3.19%	2021
▲	6.99%	2022
▲	4.24%	2023

Non-Residential Building Construction Change Per Quarter



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%	
Q2 2023	133.8	1.83%		120.7		1.34%	
Q3 2023	134.8	0.75%		121.2		0.41%	
Q4 2023	136.7	1.41%	5.80%	122.8		1.32%	4.24%

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

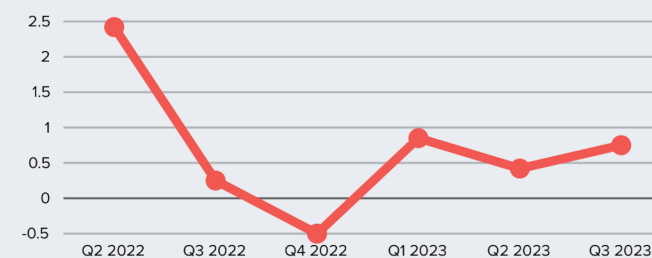
ABS Data for Western Australia



Non-Residential Building Construction Change Per Annum

▲	0.51%	2020
▲	14.18%	2021
▲	4.97%	2022
▲	3.13%	2023

Non-Residential Building Construction Change Per Quarter



Building Construction – Western Australia				Non-Residential Building Construction – Western Australia			
		% Change per Quarter	% Change per Year			% Change per Quarter	% Change per Year
Q2 2020	103.6	0.68%		98.2		0.00%	
Q3 2020	105.1	1.45%		98.2		0.00%	
Q4 2020	106.8	1.62%	4.30%	98.7		0.51%	0.51%
Q1 2021	110.1	3.09%		100.6		1.93%	
Q2 2021	113.5	3.09%		103.7		3.08%	
Q3 2021	116.1	2.29%		107.1		3.28%	
Q4 2021	122.3	5.34%	14.51%	112.7		5.23%	14.18%
Q1 2022	128.5	5.07%		115.8		2.75%	
Q2 2022	132.1	2.80%		118.6		2.42%	
Q3 2022	133.6	1.14%		118.9		0.25%	
Q4 2022	133.9	0.22%	9.48%	118.3		-0.50%	4.97%
Q1 2023	134.6	0.52%		119.3		0.85%	
Q2 2023	134.7	0.07%		119.8		0.42%	
Q3 2023	137.1	1.78%		120.7		0.75%	
Q4 2023	141.8	3.43%	5.90%	122.0		1.08%	3.13%

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

MBM's Escalation in Conversation

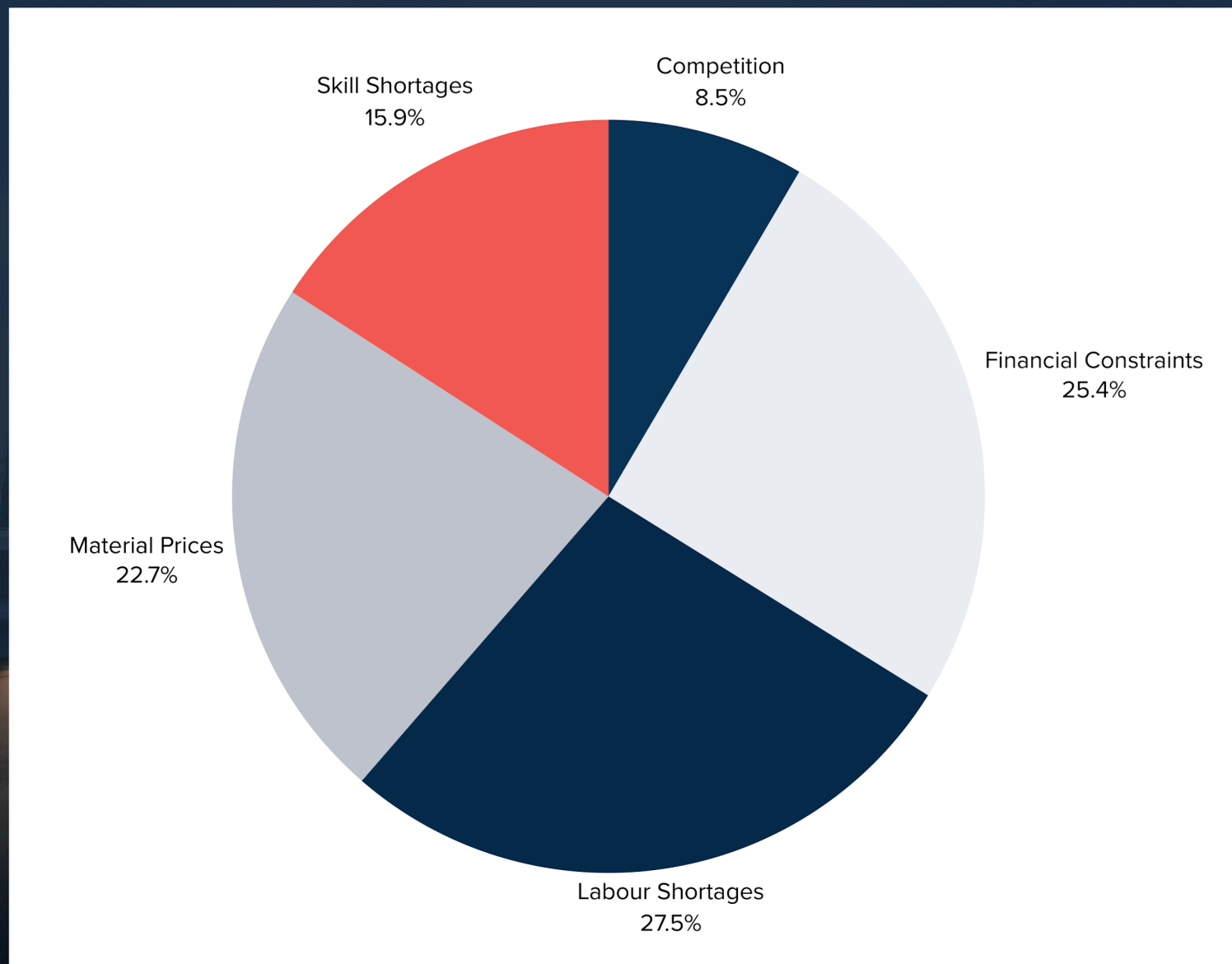
Market escalation webinar
14 February 2024

Industry Poll Results

In our inaugural quarterly escalation webinar, *Escalation in Conversation*, we conducted a poll to gather collective industry feedback on the factors which most impacted projects in Q3/Q4 2023.

The poll results revealed that labour shortages were the primary challenge posed to construction projects. Approximately 27.5% of respondents identified this as the most significant impact on projects during the previous quarter.

In close second, financial constraints created barriers to the success of developments, followed by changes in material prices. The poll results align with the economic factor analyses presented in our Q1 2024 Quarterly Escalation Update, and assist to measure the accuracy of tangible changes in project impacts.



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Our expertise ranges from quantity surveying, building consultancy, tax depreciation & asset services, asset management and facilities management advisory, infrastructure, and expert witness advice.

Our Escalation Experts

<p>DAVID MADDEN Founding Director dm@mbmpl.com.au</p>	<p>KENNY TOPLIS Executive Construction Economist kenny.toplis@mbmpl.com.au</p>	<p>JUSTIN NOAKES Director – Advisory justin.noakes@mbmpl.com.au</p>	

Adelaide

Level 5
60 Waymouth Street
Adelaide SA 5000
08 8223 3038
sa@mbmpl.com.au

Brisbane

Suite 12.1 Level 12
100 Creek Street
Brisbane QLD 4000
07 3234 4000
qld@mbmpl.com.au

Canberra

Level 1
68 Northbourne Avenue
Canberra ACT 2600
02 6152 0996
act@mbmpl.com.au

Melbourne

Level 6
500 Collins Street
Melbourne VIC 3000
03 9603 5200
vic@mbmpl.com.au

Parramatta

Suite 1A Level 8
111 Phillip Street
Parramatta NSW 2150
02 9270 1000
nsw@mbmpl.com.au

Perth

Level 32
152 St Georges Terrace
Perth WA 6000
08 9322 1795
wa@mbmpl.com.au

Sydney

Level 5
1 Chifley Square
Sydney NSW 2000
02 9270 1000
nsw@mbmpl.com.au