

# Quarterly Escalation in Conversation

## Webinar FAQs

### **What is the difference between escalation and inflation, in definition?**

Inflation is based on the Consumer Price Index which is determined through a basket of household goods and services over a period of time whereas escalation is purely related to the construction industry and the building cost inputs (materials, labour, preliminaries etc.). The indices that the Australian Bureau of Statistics publish for building price index is based on a price bill of quantities which is issued to various contractors to price over a period of time to reflect differences in pricing for various trades. This is used to determine building cost escalation over various periods of time.

### **Is it appropriate to ask what is driving contractors to struggle and go under?**

This is very relevant and good to understand when evaluating risk on future projects. The main factors driving insolvencies are the past two years of difficult trading conditions which included COVID, inclement weather conditions, unforeseen material escalation, supply chain issues etc. This has essentially put massive strain on contractors who signed up to fixed price contracts over this period. These contractors would have essentially priced 2-3 percent per annum escalation over the contracts whereas actual escalation was closer to the 8-10 percent per annum. Under the condition of contract there would be no entitlement to compensation for this and the result has been main contractors margins being diminished to almost nil over this period and in certain cases resulted in contractor insolvencies.

### **Is it worth undertaking financial checks of MC prior to tender?**

Definitely very beneficial to the project to undertake financial checks as early as before tender process. This can ensure tenders are not received from ultimately "disqualified contractors" and possibly resulting in only one/two valid tenders which may affect the competitiveness of the tender process and ultimately obtaining the best price.

### **Do you foresee the limited amount of top tier builders in the residential space will cause more escalation than 2.5-3% per year in NSW?**

Yes, the residential market remains one of the highest risk sectors to be in resulting in a reluctance from many top tier builders. The result of this will be less competition within the tenders, higher risk (contingencies) and margins being priced into tenders and ultimately drive higher rates of escalation. The 2.5-3% would cover labour and materials escalation however for residential developments an additional 1.5-2.5% , depending on project size, should be considered for the above-mentioned reasons.

### **Has your escalation forecast considered the generally required increase in union endorsed EBA subcontractors? ie 5-6% pa wage growth!**

Yes definitely one of our main considerations. It is one of the main factors driving escalation in 2024 and has been the major influence in the % increases on the second half of 2023 when EBAs were beginning to be signed or main contractors became aware of the 5-6%pa wage growth coming into effect and started pricing this into their tenders. IF you refer to our Q3 2023 report we mentioned that the result of the EBAs on large projects where EBA contractors are required, creates a floor of 2% pa based on labour roughly making up 40-50% of the contract sum (depending on sector).