WT PARTNERSHIP

REVIEW OF AUSTRALIAN CONSTRUCTION MARKET CONDITIONS

JULY 2016

WT Partnership (WTP) is an award winning international cost and consultancy organisation for the infrastructure, construction and property industry.

NICK DEEKS - MANAGING DIRECTOR

Every organisation is faced with change and the challenges it creates. At WTP our approach to 'change' is manifest in our 2020 Strategy for Growth based on three pillars;

1. our vision
2. our investment in our people, environment and growth; and
3. business transformation.

Our new agile workspace in Sydney is evidence of our responsiveness to 'change' and our desire to transform our industry. We welcome the opportunity to discuss the impact 'change' is having on your business and how WTP can partner with you to develop solutions.

CRAIG MCHARDY - EXECUTIVE DIRECTOR

The commentary in this report is drawn from each State and Territory and is based on reported statistical data together with local insight into market trends. Our report focuses on three key areas; construction activity, key performing sectors and tender price escalation. However, every project and development has its own nuances and we suggest you contact your local Director for 'real' project specific advice.

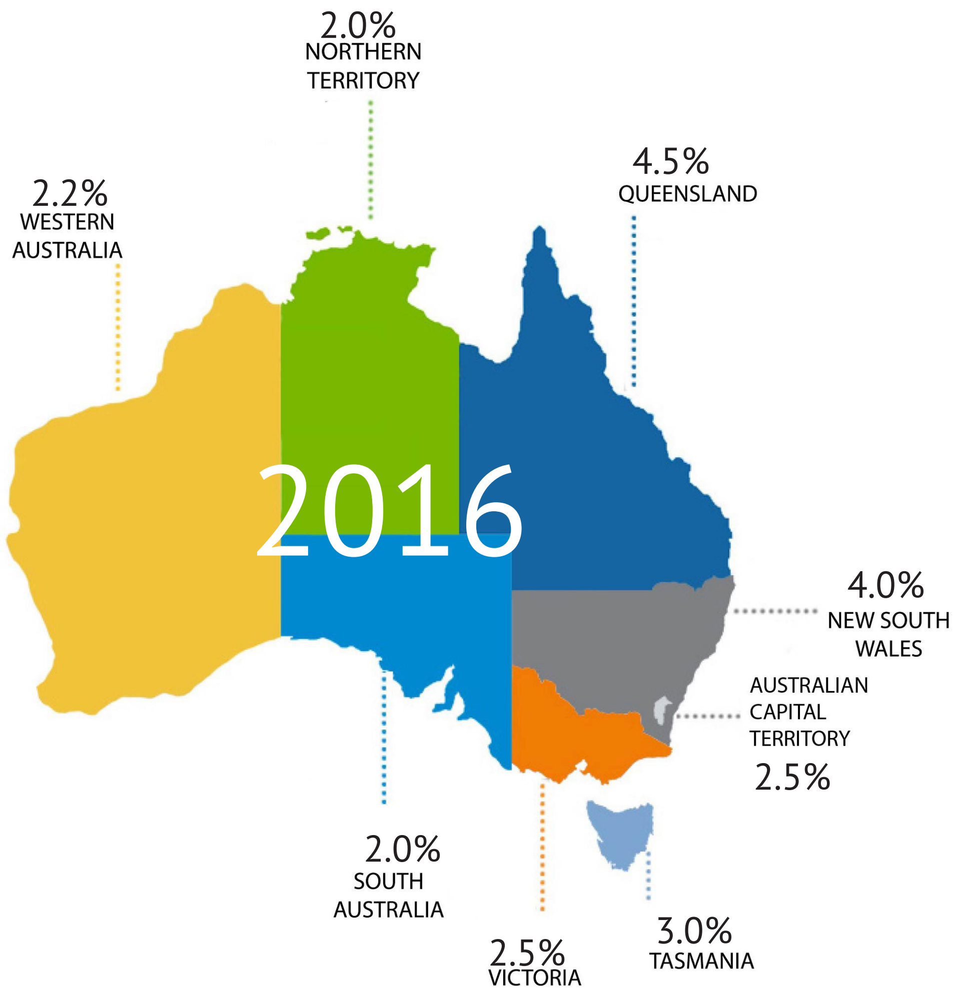
KEITH MERRY - ASSOCIATE DIRECTOR | HEAD OF MARKETING

At WTP we believe better decisions equal better outcomes.
We enable better outcomes by providing accurate, benchmarked, reliable, timely advice to our clients.
To help you achieve better outcomes we encourage you to talk to us about our core business of Cost Management and our Consultancy services; Asset and Building Consulting, Project Delivery, Sustainability, Facilities Management, PPP Technical Advisory and Defence Services. At WTP your vision is our goal.

OVERVIEW

THE OUTLOOK FOR CONSTRUCTION AND INFRASTRUCTURE IS GENERALLY VERY POSITIVE

NATIONAL TENDER PRICE ESCALATION



The timing of our publication sees major political upheaval globally with the ongoing election campaign in the USA, a recent Federal election in Australia and (some say) surprise Brexit vote.

Despite Australia's ties to the UK, the 'Tyranny of Distance' insulates us from the broader Brexit vote's impact. The immediate impact may be directly felt by Australian tourism however the broader impact to our industry is uncertain particularly in these early stages.

Of greater significance locally is the result of the recent Australian Federal election. The Coalition has formed Government, however it remains to be seen how successful the Turnbull Government will be at enacting their proposed policies.

Assuming that they are successful, the outlook for the construction and infrastructure market is generally very positive.

OVERVIEW continued

Increased demand for office space, the establishment of new office precincts, continued large-scale infrastructure project roll-outs, and the likely re-establishment of the Australian Building and Construction Commission are likely to have a positive impact for the developers of commercial real estate. Changes to superannuation contribution rules are also increasing either direct investment or interest from investment vehicles such as syndicates in this sector.

For private development, the formation of the new Government will provide some stability and impact positively on business and market confidence. However, this good news is tempered by the news that development projects undertaken by 'new developers' will experience greater scrutiny from the big four banks. This appears to be driven by a keenness to minimise failed settlement risk or a slowdown in demand in some regions due to recent legislation changes introducing surcharges and reversing the current exemptions on stamp duty for foreign investors.

Our October 2015 and March 2016 reports noted the continued strong delivery of residential, retail, health and commercial projects in many States with an increasingly strong focus on infrastructure projects, particularly in NSW and VIC. This trend continues with many previously anticipated projects now entering the planning and delivery phase.

Whilst there are fluctuations across varying sectors in different locations, overall the Australian construction market is positive and we do not predict any sharp decline in market sentiment in the short term.

Tier 1 contractors, particularly in Sydney, continue to report challenges in attaining adequate subcontract and supplier tender interest and both the tier 1 and tier 2 contractors are reporting increased trade pricing cost when tender acceptance periods expire.

The weakening Australian dollar continues to have an impact on cost escalation for some overseas sourced elements such as facades, lifts and mechanical and electrical plant. Exchange rate fluctuations are continuing to be heavily qualified in tender submissions for these elements.

Tender price escalation for each State and Territory is tabled on page 14.

NATIONAL ECONOMIC INDICATORS

The Australian Gross Domestic Product (GDP) increased by 1.1% in the March quarter of 2016. The Reserve Bank of Australia (RBA) reported this as the biggest expansion in three years, led by household spending and exports. GDP Growth Rate is expected to be between 0.4% to 0.8% for the next quarters of 2016 with a forecast GDP of 3.0% for 2016.

The Consumer Price Index (CPI) fell by 0.2% in the first quarter of 2016 and then rose by 0.4% in the following quarter. Economic forecasters predict a 0.8% and 0.7% increase in the next two quarters of 2016.

The RBA stated that inflation had been lower than expected in the March 2016 quarter and was below the RBA's targeted range of 2.0% to 3.0% but remarked that the rate "does not materially distort economic decisions in the community".

The Australian Dollar (AUD) which ranged between United Stated Dollar (USD) $1.11 and USD $0.80 over the last five years continues to decline. As at 1 July 2016 the AUD was trading at USD $0.74 and forecast to decline to USD $0.68 by June 2017.

NATIONAL ECONOMIC INDICATORS

Source: RBA; ABS; Quarterly trend review on GDP, CPI inflation, RBA cash rate.

NATIONAL CONSTRUCTION INDICATORS

The overall value of work done in Building is down by 3% to $47.87 billion in the March quarter with a higher proportional decrease in Engineering Construction consistent with the decline of the mining and resources boom.

It is expected that marginal rises, especially in the residential market which is consistent with Minutes of the Monetary Policy Committee Meeting of the Reserve Bank Board on 3 July 2016, will not be sufficient to offset the contraction in Engineering Construction.

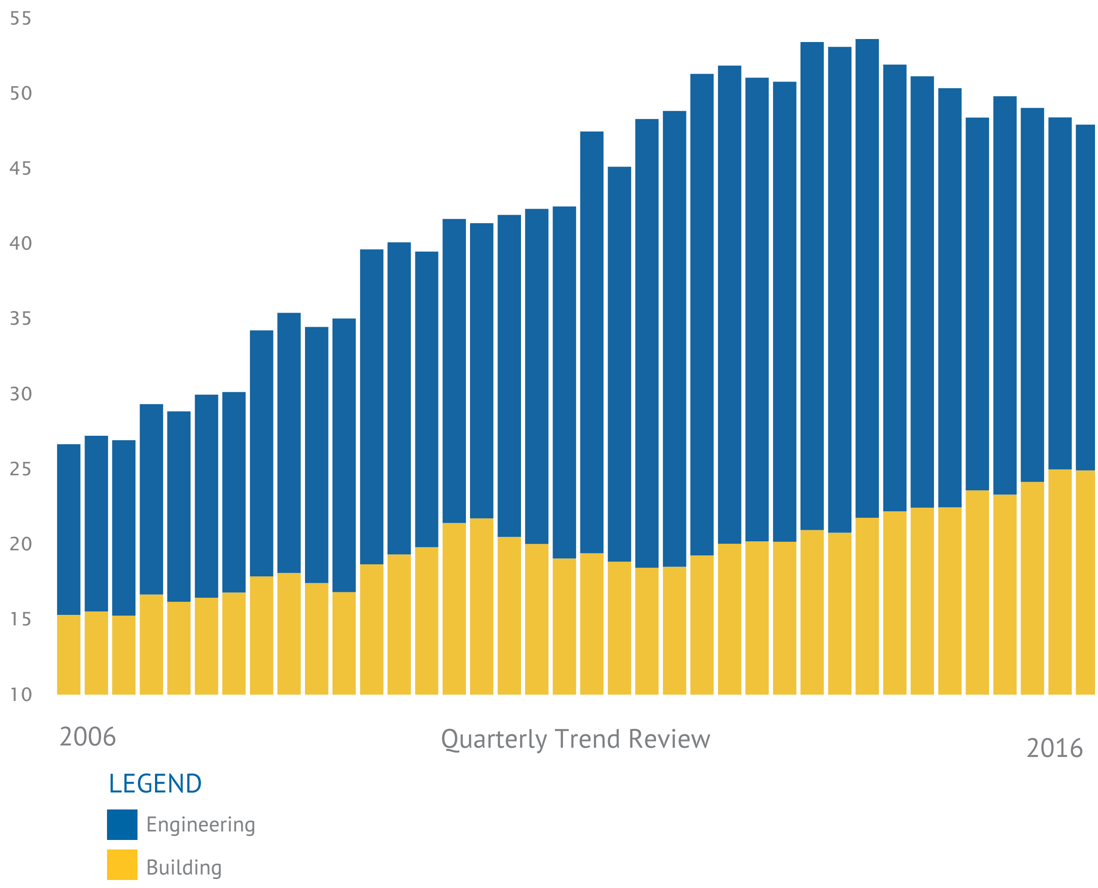
It is expected that this reduction will continue over the next three years despite Federal and State Government initiatives with infrastructure planning.

Residential building work rose in 2014-15 to the highest level on record (according to the ABS) with a pipeline of work that will see this record level increase in 2015-16, driven by historically low interest rates. Despite these figures we are seeing indications that this sector will decline in the medium term.

Non-residential building fell by 1.6% in the March 2016 quarter. However at WTP we are seeing increased activity in key sectors including retail, hotel, student accommodation and aged care when the local economic conditions and business fundamentals align.

Total construction activity accounted for approximately 14% of Gross Domestic Product in 2014-15, however with the continued contraction in Engineering Construction from its peak in 2012-13 it is expected that this will decline by 1% in the next 12 months.

VALUE OF CONSTRUCTION WORK DONE IN AUSTRALIA ($BILLION)



NEW SOUTH WALES

The NSW construction industry remains strong despite fluctuations across different sectors within the industry. Tier 1 and 2 contractors confirm that enquiry levels remain high across most sectors.

The buoyant market means that tier 2 players in particular are currently able to be selective in both the clients and projects they're choosing. However, margins remain reasonably tight and from this we conclude that many builders are using the current market to grow their business with new clients or 'landmark projects' rather than growing their profits in the short term.

There is increased interest in the concept of Early Contractor Involvement (ECI) agreements as a step towards an open-book, collaborative approach to project delivery. This procurement model does not result in a cheaper product for the client but often results in a 'smarter' build and provides the client with a greater degree of cost certainty.

Infrastructure is the obvious stand-out performer in the NSW construction market with many high-profile projects in planning and execution at the time of writing.

The commercial office and fit-out sector also remains strong with major tenants moving around the CBD vacating tenancies which need to be upgraded by incoming tenants. In addition, we are seeing areas around Sydney where compulsory acquisitions for future infrastructure/mixed-use developments mean that tenants will be obliged to move on to new premises in the near future.

Regardless of sector and location, the impact of the Enterprise Bargaining Agreements (EBAs) must be considered in the medium to long-term.

The increases in wages and site allowances during the current agreement period account for an additional 2-3% per annum wage increase on EBA sites compared to (average standard Australian wage increases) on non-EBA sites. This may further increase the total construction cost for EBA sites.

Generally commercial /fitout projects are likely to see cost increases in line with our previous forecast of 4% to 5% p.a. for 2016 continuing at the same level throughout 2017 and 2018.

Infrastructure tender escalation will continue to increase at a rate of 4% p.a. in the mid-term with the residential sector continuing to increase at between 4% to 5% p.a. in the foreseeable future.

Overall, for the remainder of 2016 and throughout 2017 we anticipate tender price escalation to increase by 4% p.a. We expect this to increase to an industry-wide rate of 5% p.a. for 2018 - 19 as a number of significant projects across various sectors enter their tender and contracting phases.

LEGEND

- Construction Activity
- Key Performing Sector
- Tender Price Escalation

VICTORIA

The outlook for VIC in the second half of 2016 is strong albeit for different reasons than previously anticipated.

A confluence of State Government and financier's initiatives including reduced plot ratios and building heights; new apartment design guidelines; raising land transfer duty impositions on foreign investors and further tightening of lending protocols for off-shore purchasers all suggest that demand for large volume, single contract apartment towers in Melbourne's CBD and Southbank areas will likely abate in the medium to longer term.

However, the Victorian 'State Taxation and Other Acts Amendment Act 2016' has seen changes in stamp duty requirements which provide exemption for foreign investors from paying the 7% stamp duty surcharge on retirement villages, hotels, motels, serviced apartments and student accommodation on property transactions completed on or after 1 July 2016.

We feel that the incentives provided by this amendment may offset the predicted decline in the high rise residential market in the CBD.

There is continuing momentum in the infrastructure market with major rail upgrade initiatives and road and civil projects more than making up for a reduction in the previously buoyant residential market for the tier 1 and 2 contractors.

Tier 1 contractors report a dip in demand for tenders, however tier 2 and 3 contractors remain busy with metropolitan residential projects.

Campus-style developments and smaller residential towers continue to be considered away from the CBD; some of these are of significant value but their nature and scale lend themselves to a broader head-contractor and sub-contractor market.

With regard to senior living and aged care, the outlook is positive with clear demand for facilities of all types. However, we note that developer discussions are increasingly focusing on the provision of care in vertical and higher density accommodation in the inner suburb locations.

This is consistent with seniors looking to transition into 'lifestyle' accommodation within 10km of the family home and closer to amenities. The demand that we are seeing in this sector is consistent with independent forecasters.

The renegotiation of the EBA in March 2016 is resulting in a direct increase to the cost of construction labour, however there is competitive tendering on key projects especially where tier 1 contractors are able to absorb increased labour costs particularly on iconic projects.

There are marginal changes to our previous publication and we now anticipate tender escalation in the order of 2.5% for the balance of 2016, 2.3% in 2017 and 2.25% in 2018.

QUEENSLAND

The QLD outlook for the remainder of 2016 appears positive despite the national fall in total building and construction activity, with the short-term upturn in residential building works.

However we note that the Queensland Government has recently reversed its policy of attracting foreign investment in the residential market by increasing stamp duty for foreign buyers by 3% despite this being one of the regions strongest sectors.

Queensland Government expenditure sees a $4.39 billion capital programme in the Transport and Main Roads portfolio which continues funding for a number of previously announced projects.

The Gold Coast region's activity is driven by works for the Commonwealth Games in 2018, whilst in the Northern parts of the state, Townsville is still static with few major projects underway.

The residential sector is active with tower cranes visible on the horizon in Brisbane. However, financier and construction pricing pressures are likely to result in a decline in new residential projects in the medium-term.

The Brisbane CBD office market is steady, whilst the Sunshine Coast and Gold Coast office markets continue to decline. Subsequent to the increase in commercial office vacancies, landlords are investing, re-fitting and refurbishing older stock in order to attract new tenants.

In addition, the owners of older commercial office buildings are responding to market demand and are set to convert their assets to hotel or student accommodation. The latter, has become viable driven by reduced Headworks Charges in the Brisbane CBD region.

The multi-storey residential sector is seeing labour shortages across a number of trades including tiling, partitioning, painting and formwork.

This has resulted in increased costs of up to 20% over the last 18 months (on EBA sites). The currently proposed EBA agreement looks set to increase wages by an additional 1-2% per annum over the next four years. Currently, EBA projects are approximately 10% more expensive than non-EBA projects within QLD.

Across the state, different areas are seeing different levels of cost pressures. The Gold Coast is seeing escalation above the state average due to the 2018 Commonwealth Games.

We forecast escalation to remain at 4.5% for the balance of the 2016 with 4% to 5% p.a. over the following 2 years given the sustained strength in the SE QLD market.

WESTERN AUSTRALIA

The WA market continues to show signs of excess capacity in both the main and sub-contractor markets.

As we move into the second half of the year we expect conditions to improve in a number of sectors, while other sectors continue to see little or no growth. As suggested in our previous report, this re-balancing of the local construction market appears to benefit tier 1 contractors more so than tier 2 or tier 3 contractors.

While competitive tenders are being noted across all project sizes, it would appear from tenders returned by tier 2 and tier 3 contractors that this section of the market has become very competitive with supply outstripping demand.

We expect this trend to continue for the balance of the year, and most likely extend into Q2 2017 before the local construction market begins to balance itself.

The retail sector is a major growth area in WA. Given the magnitude of the various projects underway or in planning we are of the opinion that the retail sector will be a major contributor to the local construction market for the next 4 to 5 years.

The hospitality sector is performing well with a number of new build and hotel refurbishment projects underway.

The high rise residential sector is still active with both local and overseas developers continuing to invest. However, this sector is very dependent on the ability of individual developers to attract overseas interest.

Civic infrastructure continues to perform well, with the new Perth Stadium under construction and the New Museum for WA currently in negotiation with the preferred tenderer.

The infrastructure sector continues to perform well with a number of substantial road and rail projects currently under construction and planned over 2016-2020. The Defence sector is also looking strong and due to various economic and geopolitical factors should become a growth area over the next 3 to 5 years.

Our overall outlook for the WA market is neutral for the medium term. The decline of the resources sector is now being felt in the "real" local economy. While the full implications of this have yet to be borne out, a degree of stability is starting to materialise.

Subject to substantial international economic shocks, we would expect the local construction market to balance its excess capacity by Q2 2017.

Based on tenders received over the first half of 2016 we are reducing our escalation forecast from 2.4% to 2.2% over the balance of 2016, with 2% for 2017, and 1.8% for 2018.

SOUTH AUSTRALIA

Large State Government infrastructure projects remain the key employer for tier 1 contractors and trade contractors. However the tier 2 and 3 contractor market remains extremely competitive.

Earlier rumours of a delay for completion of the Royal Adelaide Hospital have proven to be correct; several revised completion dates have been announced in the local media but there is currently no confirmed date.

The State Government has indicated legal action is being considered against the PPP consortium for delays; the building arm being Hansen Yuncken CBP Contractors Joint Venture.

Aged care, seniors living, student accommodation and high density apartment projects continue to be the major sectors of strength in an otherwise quiet market.

Aldi's expansion into South Australia continues to spur local retail centre owners into redevelopment works to expand existing facilities to cater for their stores plus take the opportunity to upgrade facades, and amenities.

The new $250 million Calvary Private Hospital suffered delays to construction commencement. The contract has now been awarded and early works have commenced.

Mid-tier contractors are hungry for new work and favourable pricing continues to be seen for developers.

We forecast escalation to be a maximum of 2.0% for the second half of 2016, with 2.5% p.a. for 2017 and 3% for 2018.

AUSTRALIAN CAPITAL TERRITORY

Since our last report, the views of property owners, developers, agents, managers, and consultants indicate an increase in business confidence and sentiment for the Australian Capital Territory.

Residential, office, retirement living, and hotel/tourism capital growth expectations have all increased from previous months. Aside from NSW and Tasmania, the ACT is the only other jurisdiction recording a positive government performance index.

This is especially important in light of slight decreases in expected forward work schedules, and economic growth for both the ACT and the nation.

The recently posted ACT Budget clearly illustrates the property industry's critical role in the economic growth within the region.

The budget captured both the achievements and the challenges facing the industry.

Historically the largest construction activity in the ACT has been the residential sector, however leading indicators suggest that this will reduce with numbers of new dwellings to fall over the next 12 months.

ACT has a number of major projects such as the ACT Law Courts and the Light Rail works forecast to dominate the construction industry.

Works continue on Parliament House but there was no big budget announcement for the Canberra Hospital.

The 'City to the Lake' project will develop the West Basin as a premium waterfront leisure, sport, commercial and residential precinct with provision within the ACT Budget for a feasibility study into the provision of swimming and aquatic facilities in Central Canberra.

Local tier 2 contractors continue to report that the 'trade' market is keen for work with numerous subcontractors responding to requests for pricing on most projects.

Given the improvement in confidence levels, we have maintained our forecast for tender price escalation in the order of 2.0% to 2.5% until the end of 2016 with 3.0% in 2017 and 3.0% p.a. in 2018.

TASMANIA

Hobart is currently a hive of activity with unprecedented total value of capital works currently underway including;

- $100M + Parliament Square - new hotel development
- $65M UTAS NRAS apartments
- $90M UTAS performing arts centre in Hobart
- $100M Myer building and Hotel
- Vibe Hotel Argyle Street
- MAC 01 Hotel
- Macquarie Street Hotel - Fragrance Group
- $690M Royal Hobart Hospital Development

Also mooted are further hotel developments within and outside of Hobart such as Federal Hotels Port Arthur Resort.

Future activity is also expected for the railyard site near the waterfront, civil works are expected to commence on the Airport runway extension and roadworks will commence on the main road link between Hobart and Launceston.

Activity in the North of the state is not so buoyant and the North West sector has even less activity.

Other than the hotel sector the aged care market is also increasing with a number of developments in the pipeline.

Construction activity is increasing. Trade rates remain competitive with many costs being held in check as a result of being tendered on large projects in a subdued market over 12 months ago. However we anticipate that new projects coming on line in 2016 to 2018 will see increases in trade pricing as a result of the buoyant market.

Labour shortages will continue to have an impact on project costs in the short term with some local contractors going into administration and labour potentially being sourced from other regions.

We forecast escalation to be steady at 3% for the balance of 2016, increasing to 4% for each of 2017 and 2018.

NORTHERN TERRITORY

The Northern Territory is expected to benefit from increased exports in the 2016/2017 financial year particularly in the liquefied natural gas (LNG) sector. The resources sector will continue to be one of the main economic drivers for the region. The local economy will stabilise and return to long term growth norms assisted by the circa $1.78 billion infrastructure spend.

However, it would appear that while public sector expenditure will be significant, it will not fully fill the void left by the reduction in private sector expenditure. The effects of this reduction will be further amplified with the completion of “Ichthy’s LNG” which involves $30 billion investment in an 889 km gas pipeline and on-shore processing facility.

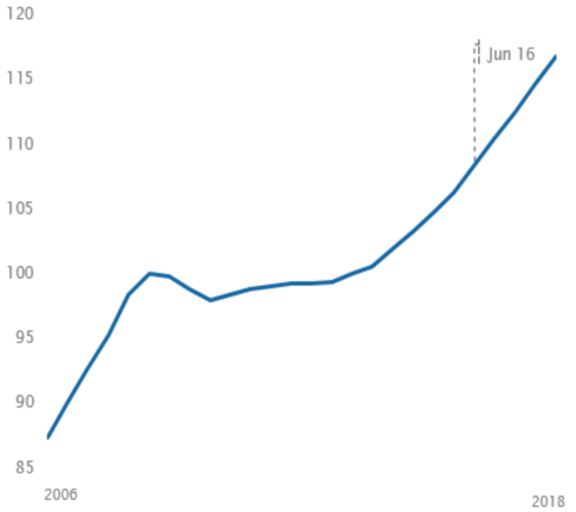
While resources, infrastructure and Defence are expected to be the main contributors to the local construction market, we expect to see a slight increase in both the hospitality and retail sectors.

Other sectors which previously had seen significant growth, such as the residential sector, are expected to decline over the next 12 months. This is due to both the supply of new homes catching up with and outstripping demand and very low population growth in the region. We are of the opinion that private investment in large scale residential projects will be limited for the foreseeable future.

Overall our outlook for the NT construction market is steady for the next 12 months. We anticipate tenders to be very competitive over 2016/2017 within Darwin and indeed state wide. We are of the opinion that escalation will be 1.5% to 2% over 2016, 2% p.a. in 2017 and 1.9% in 2018.

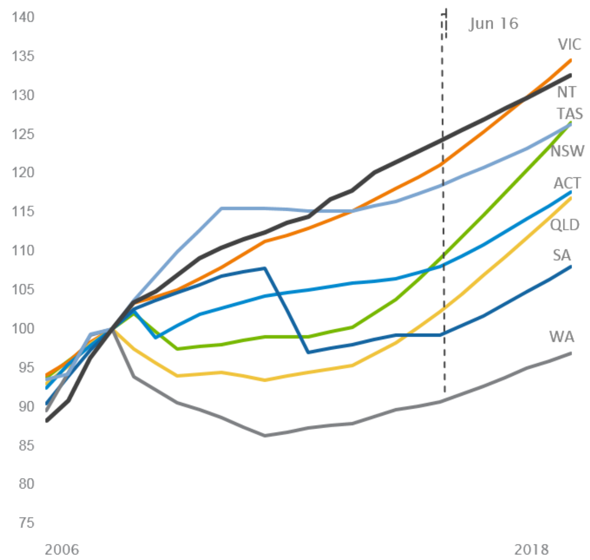
TENDER PRICE ESCALATION FORECASTS

WTP TENDER PRICE ESCALATION FORECAST AUSTRALIAN AVERAGE



The above graph index is set at 100 for September 2008. Recorded data and forecasts are based on tenders for large building construction projects (value $20 million to $300 million).

WTP TENDER PRICE ESCALATION FORECAST STATE BY STATE



The above graph does not reflect the relative cost differential between the different States.

WTP TENDER PRICE ESCALATION

		NSW	VIC	QLD	WA	SA	ACT	TAS	NT
Actual	2006	4.6%	4.2%	5.9%	12.0%	6.3%	6.3%	5.9%	9.1%
	2007	4.6%	4.5%	5.5%	10.9%	7.6%	6.0%	5.1%	7.4%
	2008	4.0%	5.1%	-0.7%	-2.8%	5.4%	4.6%	5.2%	3.5%
	2009	-4.4%	1.6%	-3.6%	-5.7%	2.0%	-1.9%	4.7%	3.3%
	2010	0.6%	2.8%	0.5%	-2.1%	2.0%	2.3%	4.1%	1.8%
	2011	1.0%	3.0%	-1.0%	-2.7%	1.0%	1.5%	0.2%	1.7%
	2012	0.0%	1.5%	1.0%	-1.6%	-10.0%	0.8%	-2.9%	3.0%
	2013	1.3%	2.0%	1.0%	0.6%	1.0%	0.8%	0.0%	3.1%
	2014	3.5%	2.5%	3.0%	2.0%	1.3%	0.5%	1.0%	2.2%
	2015	5.0%	3.0%	4.0%	1.4%	0.0%	1.5%	1.8%	2.2%
Forecast	2016	4.0%	2.5%	4.5%	2.2%	2.0%	2.5%	3.0%	2.0%
	2017	4.0%	2.3%	4.5%	2.0%	2.5%	3.0%	4.0%	2.0%
	2018	5.0%	2.2%	4.5%	1.8%	3.0%	3.0%	4.0%	1.9%

The above indices reflect capital city CBD and metropolitan construction costs.

WT PARTNERSHIP

WT PARTNERSHIP IS AN AWARD WINNING INTERNATIONAL COST AND CONSULTANCY PRACTICE.

Our expertise covers the building, construction and infrastructure sectors, as well as consultancy services that assist with the acquisition, operation and divestment of assets.

WTP draws on the collective experience, knowledge and capability of our professional staff in locations throughout Australasia, Asia, North America, Canada and Europe to provide our clients with the right advice on all aspects of cost, value and risk to help them achieve optimum commercial outcomes.

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NOTE ON APPLYING TENDER PRICE INDICES

A number of project specifics should be considered when reviewing tender price escalation forecasts including, but not limited to, the procurement route, size, complexity, location and risk. Equally, the keenness of tenderers is important in terms of pricing and this will be driven by issues such as local market dynamics, workloads, hotspots and realisable margins. With the current uncertainties in the local, national and international arenas, it is important to continually monitor the market and review escalation allowances. Clearly, it is very difficult to predict future escalation over the next few years therefore the advice is offered for guidance purposes only.