REVIEW OF AUSTRALIAN CONSTRUCTION MARKET CONDITIONS

JULY 2013

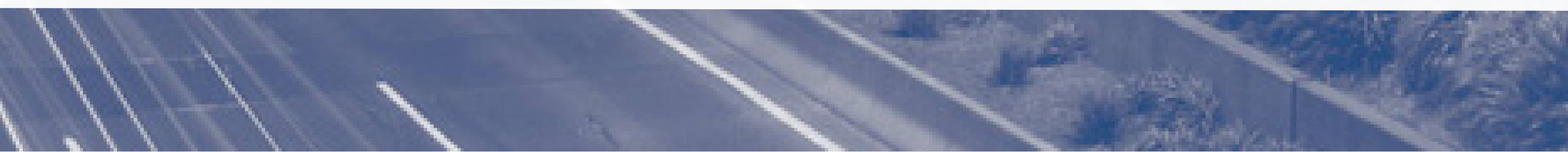
Each of our offices reports subdued construction activity and continued aggressive tendering amid worsening conditions in the mining and resource sector. Public spending is down and previous signs of emerging confidence in the private sector is tempered with uncertainty and caution with little expectation of improvement until after the Federal election.

Increases in materials and labour costs are largely being absorbed by competitive tendering with builders pricing at low or even zero margins. As foreshadowed in our March report, there may be further upward pressure on labour costs as a consequence of the changes in January of this year to the *Building Code 2013 (Federal Code)* under the *Fair Work (Building Industry) Act 2012 (Cth)* as it relates to enterprise bargaining agreements. The Federal Court ruled in favour of the CFMEU in a matter against the State of Victoria on 17 May 2013. The CFMEU will be pressing tier 1 and 2 builders to incorporate the same or similar conditions in their EBAs. Until such time as both Federal and State Government guidelines and policies are in harmony the impacts will not be fully understood.

The value of the Australian Dollar (AUD) against the US Dollar (USD) has reduced by more than 10% since our last report making exports more attractive and imports (priced in USD) less so. The drop against the Chinese Yuan will also increase the costs of materials and products such as curtain walling, fabricated structural steel, joinery, stone and tiling which have been increasingly imported from China as domestic products became less affordable. The cost of lifts, travelators, sanitary ware, kitchen appliances and other construction components imported from Europe and America will also be affected.

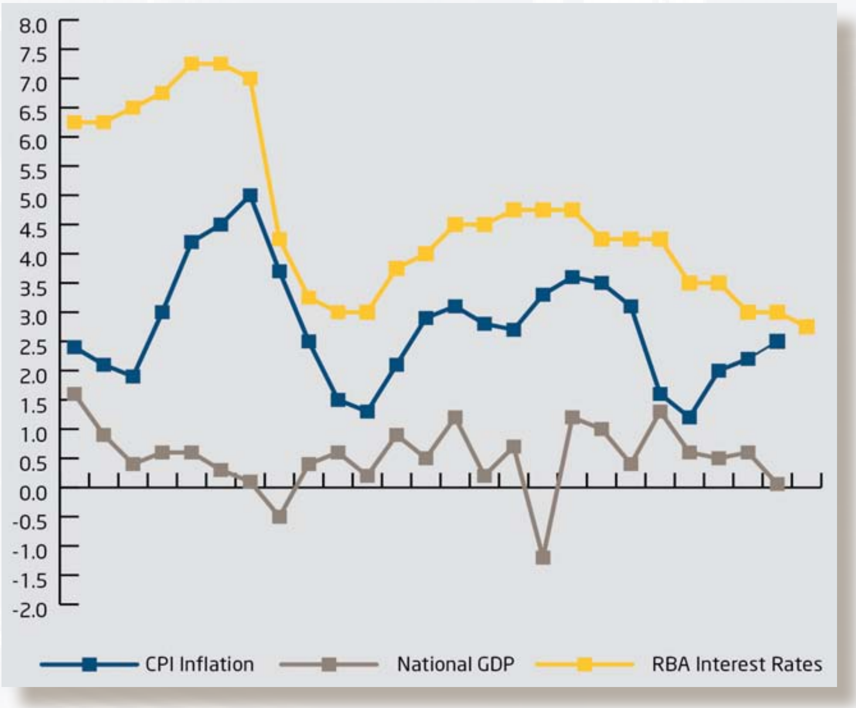
With increases in the cost of building rising, it is only a matter of time until the fierce tender price cutting seen over recent years relents or more contractors hit the wall. With the exception of South Australia and Tasmania, each of our offices expects that tender pricing will continue at competitive levels for the immediate future and that cost pressures will eventually come to bear next year and into 2015 when escalation in tender pricing will be trending at levels of around 3.0 to 4.0%.

It takes more than bargain building prices to stimulate property development and the markets around the country await the outcome of the Federal election and the return of investment as confidence materialises into construction.



NATIONAL ECONOMIC INDICATORS

- GDP expanded 2.3% from March 2012 through to March 2013 averaging a quarterly increase of 0.58% each quarter for the same period.
- CPI rose 2.5% over the year ending March 2013. This compares with a rise of 1.6% through the year ending December 2012. The downward trend seen between June 2011 and September 2012 appears to have reversed with inflation currently trending around 2.4%.
- The AUD traded at parity with the USD throughout 2012. The AUD has now fallen below parity with the USD and as of June 2013 was at approximately $0.92. Predictions are that the AUD will continue to decline against the USD to levels below $0.90.
- The seasonally adjusted Australian unemployment rate has increased since our previous report. The rate was 5.5% in the ABS May 2013 data.
- Since the beginning of the 2012 calendar year, the RBA reduced the official cash rate by a total of 150 basis points. The RBA's current Cash Rate is 2.75%.



National GDP measure: seasonally adjusted quarterly % change
Source: RBA; ABS; Quarterly trend review on GDP, CPI inflation, RBA cash rate.

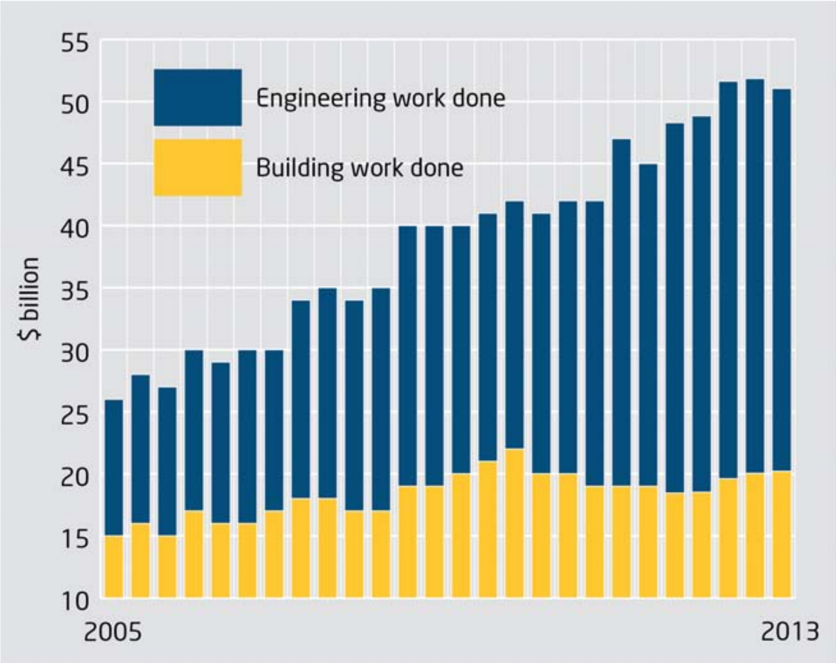
NATIONAL CONSTRUCTION INDICATORS

In the 12 months preceding April 2013, the total value of construction work done increased by 5.6%. This compares with 14.2% for the same period one year earlier.

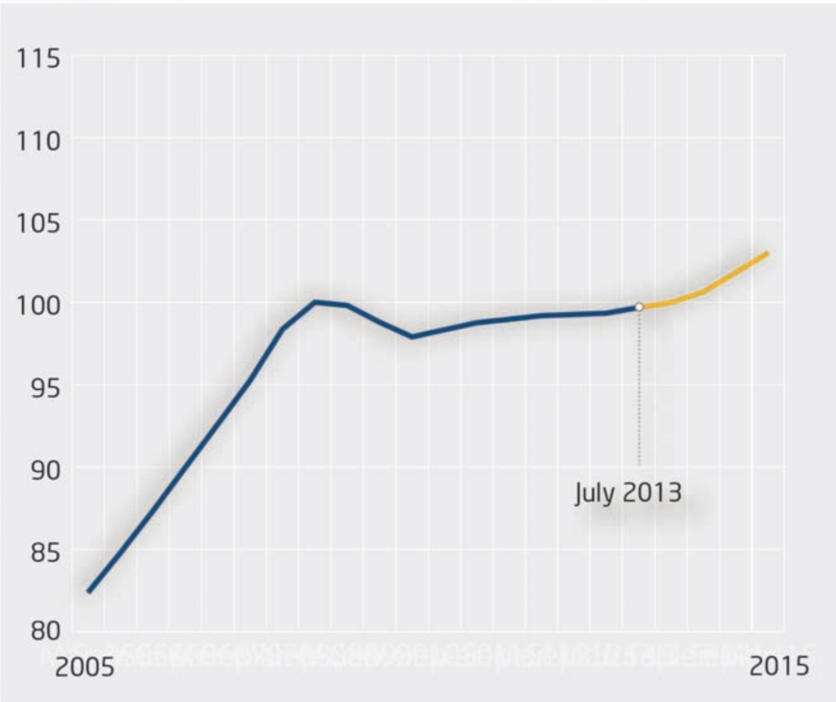
In the 12 months preceding April 2013, the seasonally adjusted estimate for 'building work done' increased by 9.21%. This compares with -7.95% for the same period one year earlier. On the other hand, in the 12 months preceding April 2013, the seasonally adjusted estimate for 'engineering work done' increased by 3.53%. This is a stark decrease in comparison with the same period one year earlier which saw 'engineering work done' increase by 32.05%.

Of the 'total construction work done' in the amount of $203 billion during the 12 months preceding April 2013, 'building work done' represents 38% of total construction work done while 'engineering work done' represents 62%. Engineering work done, as a percentage of total construction work done, is now trending flat since a continued increase from the September 2010 quarter through to the September 2012 quarter. The latest data for the March 2013 quarter only, shows that 'building work done' represents 40% of total construction work done whilst 'engineering work done' represents 60%.

VALUE OF CONSTRUCTION WORK DONE IN AUSTRALIA ($ BILLION)



WT PARTNERSHIP 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).

State By State Commentary

NEW SOUTH WALES

The New South Wales building industry continues to struggle, despite sparks of activity in the retail and residential sectors. Strong pre-sales, lack of demand and low interest rates are all contributing factors.

Aggressive, competitive tendering by contractors in all construction market sectors continues as relatively empty order books are sought to be filled.

Non-residential sectors, as a group, remain flat although health and aged care investment is relatively strong. Barangaroo is a dominant driver for commercial building and construction and retail projects, previously on hold, are being re-investigated.

Commercial vacancy rates in the CBD are at extremely low levels with suburban areas easing in the latest quarter. Future demand will be absorbed by projects either planned or currently under construction which will create vacant space within the CBD around 2015/16.

Strong tenant demand for rental properties and an apparent undersupply of housing, especially in inner city locations, has not yet resulted in the expected increase in residential dwelling construction. Growth in this sector is expected later in 2013 and early 2014.
The effect of negotiations of EBAs on labour costs, following the success of the CFMEU in its recent matter against the State of Victoria will likely start to impact in NSW later this year.

In its Long Term Master Plan, the NSW State Government's spending plans focus heavily on transportation projects. The South West Rail Link is in the construction phase, the North West Rail Link Tunnelling package has been awarded with the Station Viaduct and Operating Train System packages to follow. Sydney Light Rail is expected to commence work in 2014, the F3 – M2 Link has moved to stage 3 of the unsolicited proposal process and the WestConnex business case is being prepared.

Major road upgrades and extensions are being planned. This increase in activity will inevitably drive prices higher for this sector as both contractors and consultants react to demand.

The resource related sectors have slowed as the demand for coal eases and the potential coal seam gas projects become tied up in red tape and face growing opposition from landowners.

The perceived confidence that investment will increase for the construction sector due to the current low base and low interest rates is yet to materialise and provide much needed stimulation.

We project average cost escalation of 1.0% for 2013, 3.0% for 2014 and 4.0% for 2015.

VICTORIA

Interest in Melbourne CBD and inner suburban development projects continued to improve in the second quarter of 2013 and there are few signs that this will abate in the next six months. Sites are typically being considered for multi-unit residential or hotel construction.

Tier 1, 2 and 3 builders are reporting subcontractor discounts in tender pricing which suggests that real material and labour cost increases are being more than absorbed in current pricing. Furthermore, overall tender returns suggest that discounting factors are also being applied at the head contractor level in a competitive market.

Port and airport construction and infrastructure project demand is steady and future commitments appear positive. Recent tenders across buildings and civil trades have proven competitive.

Major road and rail infrastructure projects at planning or EOI phase include the East West Link and Melbourne Metro rail tunnel with tier 1 contractors formulating their strategy in anticipation of the State Government proceeding with the projects under PPP contracts.

There is a volume of work being priced or in the pipeline across most sectors however, there is still underlying capacity generally across the industry.

In light of recent subcontractor and builder tender returns, we anticipate cost escalation through the balance of 2013 to be 2.0 to 2.5%, 2.5% in 2014 and 2.5 to 3.0% in 2015.

The Barangaroo development (1) in Sydney and Melbourne's East West Link project (2) have bouyed the local construction and infrastructure sectors in those states.

Images courtesy of Lend Lease and Linking Melbourne Authority.

QUEENSLAND

Our Queensland offices continue to experience tender pricing at extremely keen levels with builders' overheads, preliminaries and margins at record lows. As commencements of larger projects continue to be pushed back, tier 1 contractors are bidding smaller jobs attempting to meet the pricing levels of the tier 2 market.

Uncertainty and lack of confidence continue to undermine the construction market as investors and tenants await the outcome of the Federal Government election.

Residential construction is expected to pick up with the New Brisbane City Plan and the South East Queensland Regional Plan anticipating strong population growth. There are already a number of significant apartment developments under construction or targeting pre-sales and BIS Shrapnel predicts a 22% increase in dwelling starts for Greater Brisbane. Retail construction is also expected to increase around the South East region as owners refurbish and redevelop to retain tenants and reposition their assets.

Office vacancy rates are at record highs and further new activity in major commercial developments is unlikely without a major tenant committment.

Following the commencement of 1 William Street, the tender market eagerly awaits the next phase of the Brisbane CBD and North Bank regeneration, a State Government initiative aimed at reinvigorating the inner city and stimulating the ailing construction industry.

Construction activity on the Gold Coast will increase with the delivery of the Commonwealth Games, the redevelopment of Pacific Fair, the stations and precincts around the Light Rail and the anticipated development of the Breakwater Marine Project.

Our Townsville office reports that prices continue to be very competitive as the tender market remains subdued with major projects such as the Townsville Hospital, Nathan Plaza, Lavarack Barracks, the Cruise Ship Terminal, Jezzine Barracks, Verde Office Building, and JCU Clinical Building under construction or completed.

The resources sector continues to slow and private property developments are largely on hold pending the Federal election, however certain areas, in particular the Townsville Port, are buoyant and are showing signs of growth.

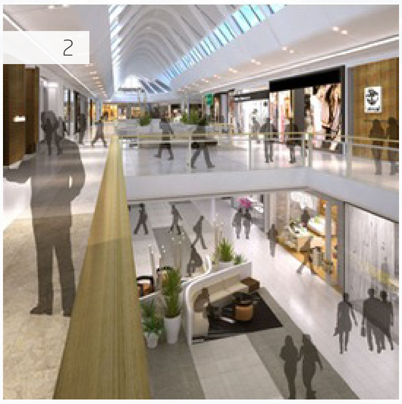
In the South East corner of the state, we forecast that tender prices generally will continue to trend at around 1.0 to 2.0% to the end of the year and then rise to around 3.0% by 2015.

The redevelopment of both AMP's Pacific Fair (1) and Westfield's Garden City (2) is indicative of the renewed activity in Queensland's retail sector.

Images courtesy of AMP and Westfield.

1

2



ACT

Ongoing concern of flat domestic economic conditions and the uncertainty surrounding the Federal political environment continues to undermine confidence in the ACT property sector.

However, the recent ACT budget as well as cuts to transaction costs for property purchases has provided some reinvigoration to the home building sector. These savings are however offset by an increase in property holding costs.

The ACT budget does include a strong capital works program over the next two years as well as forward design funding for the proposed light rail, the City to the Lake project and the new Australia Forum.

The labour market has softened with unemployment increasing. Up until now, investment has been strong but is now showing signs of slowing down. The Commonwealth Government is contracting both its purchasing and employment with further job cuts in the public sector expected over the next 12 to 18 months.

The current property market remains competitive with large tier 1 builders looking to tender on what they would traditionally view as 'small projects'.

It is anticipated that tender prices will continue to be keen for the remainder of 2013, with a forecast for cost escalation expected to be at 0.5 to 1.0% for the foreseeable future.

SOUTH AUSTRALIA

There has been little sign of improvement in the South Australian market since our last report, although the recently evident aggressive competitive tender pricing seems to have abated. This has largely been influenced by the return to select tender calls as opposed to the open tendering that dominated 2012, as well as the incidence of trade contractor failures causing main contractors and employers to be more cautious about selection of the lowest trade tenders.

Positive indicators include the recent weakening of the Australian Dollar, which will help South Australian manufacturers. It is often overlooked that manufacturing represents 10% of the South Australian economy and 9% of its employment, with about 70% of the State's total exports to both overseas and interstate coming from manufacturing.

Manufacturing related to the defence industry continues with ongoing capital and maintenance expenditure, although the local automotive industry looks likely to contract with signs that General Motors will reduce production at its Elizabeth plant, with the ripple effect impacting on many supply chain businesses. Retrenched automotive workers often look for employment within the construction and engineering industries but the current situation in those industries will limit this.

Local government expenditure on long term capital investment strategies continued, taking advantage of competitive construction prices, but it is evident that there is a general air of caution. Education continues to provide a source of work for contractors, with a large number of Government funded school projects now underway, although there is little sign that such levels of expenditure will be maintained over the medium term.

Overall, the pessimism that we noted back in our March 2013 review continues to pervade the industry. We eagerly await the conclusion of the Federal and State elections in the hope that this will create some stability and basis for recovery.

We forecast an escalation rate of 1.0% for the remainder of 2013 with an increase to 2.0% expected in 2015.

WESTERN AUSTRALIA

In the non-resource sector, the return of the Liberal administration at the recent State election will see continued significant capital works expenditure with the Government's commitment to deliver the new Perth Stadium, significant rail infrastructure and continued investment in health, particularly in country and regional areas.

Despite the slow down in mining activity affecting overall sentiment, strong activity is still anticipated in the hospitality sector due to the very limited stock of hotel rooms available to service business travellers.

Continued activity is also expected in the commercial office market for the forthcoming year due to Perth's still limited stock of commercial office space as evidenced by the country's lowest office vacancy rate, currently at 6.5%.

Based on our view of future activity, we anticipate that increases in construction prices will trend at 0.6% for the remainder of 2013, 2.3% for 2014 then rising to 3.2% for 2015.

TASMANIA

The Tasmanian Building and Construction Industry Training Board, in its June 2013 forecast, stated that Tasmania is continuing to experience a downturn with activity expected to drop by $544 million (or 25%) in the next two years.

The downturn will affect all sectors of the industry but the civil construction sector is expected to be worst hit as work dries up, especially in the North of the State as both State and Federal Government investment in the region has ended. Overall the construction industry has shed some 5,000 jobs since 2011/12.

The market remains tight across all sectors and, as forecast in our March report, we anticipate no tender price escalation for the remainder of 2013 with an increase in the order of 1.0 to 1.5% for 2014 and 2015.

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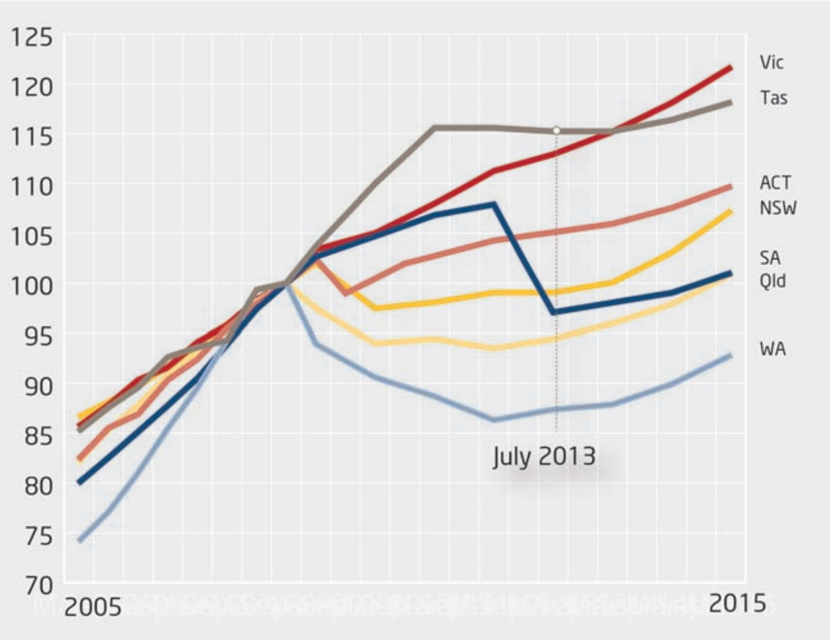
Lee Deacey, hobart

Tender Price Escalation Forecasts Regional Market Summary



	NSW	VIC	QLD	ACT	SA	WA	TAS
2005	3.5%	5.4%	6.9%	5.4%	6.4%	7.8%	4.8%
2006	4.6%	4.2%	5.9%	6.3%	6.3%	12.0%	5.9%
2007	4.6%	4.5%	5.5%	6.0%	7.6%	10.9%	5.1%
2008	4.0%	5.1%	-0.7%	4.6%	5.4%	-2.8%	5.2%
2009	-4.4%	1.6%	-3.6%	-1.9%	2.0%	-5.7%	4.7%
2010	0.6%	2.8%	0.5%	2.3%	2.0%	-2.1%	4.1%
2011	1.0%	3.0%	-1.0%	1.5%	1.0%	-2.7%	0.2%
2012	0.0%	1.5%	1.0%	0.8%	-10.0%	-1.6%	-2.9%
2013	1.0%	2.0%	1.6%	0.8%	1.0%	0.6%	0.0%
2014	3.0%	2.5%	2.0%	1.5%	1.0%	2.3%	1.0%
2015	4.0%	3.0%	3.0%	2.0%	2.0%	3.2%	1.5%

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

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CONTACT US

Adelaide

Sam Paddick
P: +61 8 8274 4666
E: spaddick@wtpartnership.com.au

Brisbane

Craig McHardy
P: +61 7 3839 8777
E: cmchardy@wtpartnership.com.au

Canberra

James Osenton
P: +61 2 6282 3733
E: josenton@wtpartnership.com.au

Gold Coast

Jason Thornley
P: +61 7 5591 9552
E: jthornley@wtpartnership.com.au

Hobart

Lee Deacey
P: +61 3 6234 5466
E: ldeacey@wtpartnership.com.au

Melbourne

Tim Roberts
P: +61 3 9867 3677
E:troberts@wtpartnership.com.au

Perth

Scott Parrott
P: +61 8 9202 1233
E: sparrott@wtpartnership.com.au

Sydney

Nick Deeks
P: +61 2 9929 7422
E: ndeeks@wtpartnership.com.au

Townsville

Jason Dixon
P: +61 7 4722 2760
E: jdixon@wtpartnership.com.au

WT Sustainability

Stephen Hennessy
P: +61 2 8197 9140
E: shennessy@wtsustainability.com.au

www.wtpartnership.com.au

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 arena, 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 above advice is offered for guide purposes only at this point..