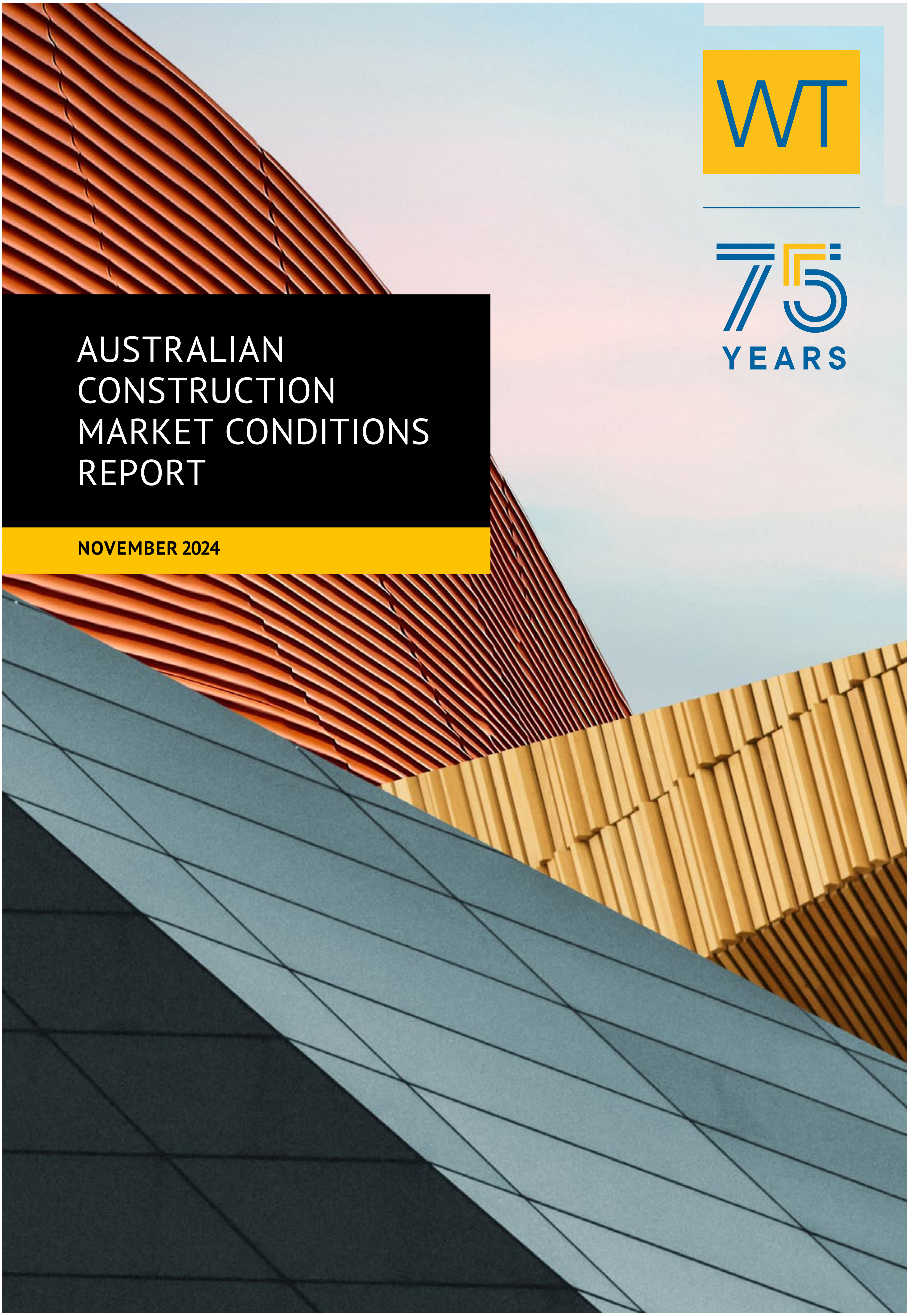

AUSTRALIAN CONSTRUCTION MARKET CONDITIONS REPORT

NOVEMBER 2024

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ABOUT THE AUTHOR

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INTRODUCTION

SIGNIFICANT INVESTMENT IN SECTOR CAPABILITY IS REQUIRED FOR A SUSTAINED SOLUTION TO HIGH ESCALATION. WHEN MIGHT THIS SHIFT BEGIN AND WHAT WILL HAPPEN TO MARKETS IN THE INTERIM?

Elevated construction cost escalation is now a feature of the construction sector. However, it is not sustainable from a medium-term perspective, especially with fundamentals pointing to the need for strong levels of construction activity and the ongoing presence of weak sector profits and margins.

In this edition of WT's *Australian Construction Market Conditions Report*, we explore how this might be resolved and the key signs to watch for.

In addition, we provide our regular updates on economic, construction and cost escalation conditions by market and sector with a three-year view, both from the broader market perspective and by input.

Gurrowa Place Tower 3 (render), Melbourne

COST ESCALATION
BUILDING

WT'S VIEW ON AUSTRALIAN COST ESCALATION BY KEY MARKET – BUILDING

	2023	2024	2025	2026	2027
SYDNEY	5.2%	5.0%	4.6%	5.0%	5.5%
MELBOURNE	9.0%	5.5%	4.8%	4.5%	5.0%
BRISBANE	8.0%	7.5%	6.5%	5.3%	7.5%
ADELAIDE	5.0%	5.0%	5.0%	5.0%	5.8%
PERTH	4.5%	5.0%	6.0%	6.0%	5.5%
HOBART	6.0%	5.5%	6.0%	6.0%	5.5%
CANBERRA	6.0%	4.0%	3.0%	3.5%	4.0%
DARWIN	5.5%	4.3%	3.8%	5.0%	4.5%
NEWCASTLE	6.5%	5.5%	4.9%	5.3%	6.0%
GEELONG	9.5%	6.0%	5.5%	4.8%	5.0%
GOLD COAST	8.5%	7.5%	7.5%	8.0%	8.0%
CAIRNS	5.5%	7.0%	5.0%	6.5%	5.5%

CONTRIBUTION TO COST ESCALATION BY INPUT – BUILDING

	2024	2025
LABOUR (DIRECT)	Makes escalation somewhat worse	Makes escalation somewhat worse
MATERIALS	Improves escalation significantly	Has no real impact on escalation
PLANT AND EQUIPMENT	Makes escalation somewhat worse	Makes escalation much worse
ENERGY	Improves escalation significantly	Has no real impact on escalation
FREIGHT	Improves escalation significantly	Makes escalation much worse
EXCHANGE RATES	Improves escalation significantly	Makes escalation somewhat worse
INDIRECT COSTS	Makes escalation much worse	Makes escalation somewhat worse
TOTAL	Makes escalation much worse	Makes escalation much worse

VS. LONG-TERM ESCALATION AVERAGES

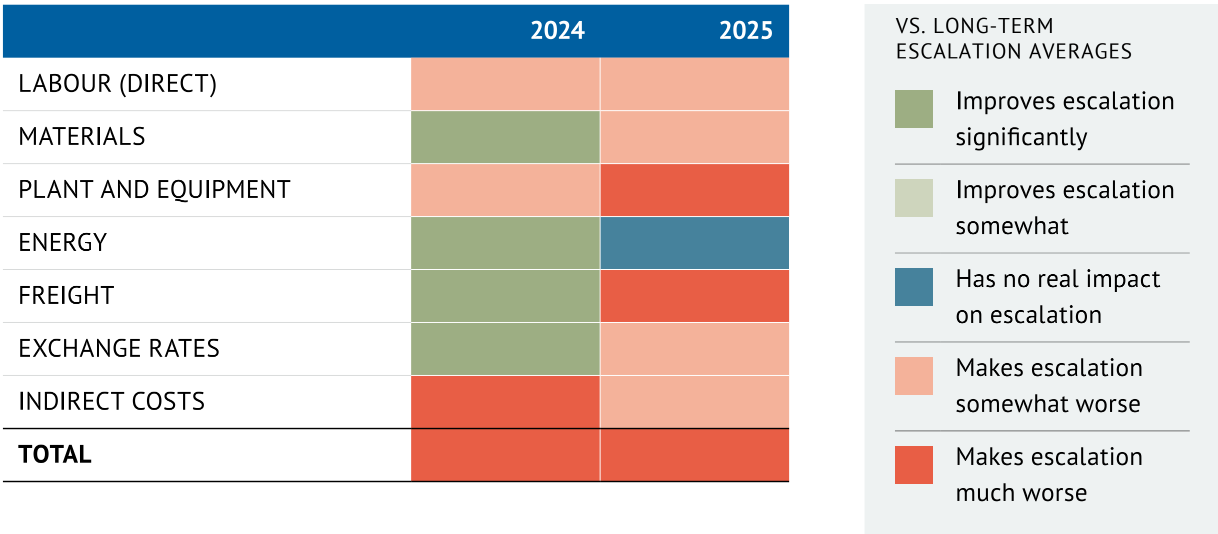
- Improves escalation significantly
- Improves escalation somewhat
- Has no real impact on escalation
- Makes escalation somewhat worse
- Makes escalation much worse

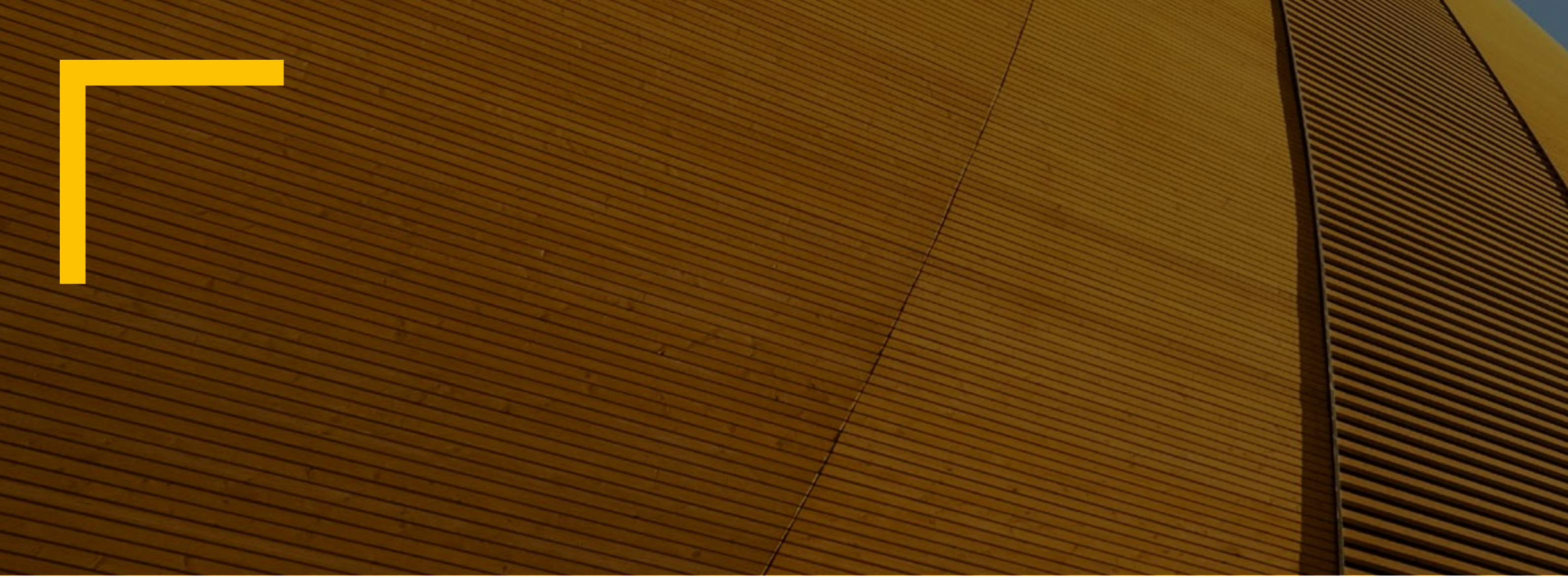
COST ESCALATION
INFRASTRUCTURE

WT'S VIEW ON AUSTRALIAN COST ESCALATION BY KEY MARKET – INFRASTRUCTURE

	2023	2024	2025	2026	2027
SYDNEY	7.0%	4.8%	5.0%	5.3%	5.8%
MELBOURNE	5.5%	5.0%	5.0%	4.5%	4.8%
BRISBANE	5.3%	5.5%	7.5%	6.3%	6.0%
ADELAIDE	7.0%	4.5%	7.0%	6.5%	5.0%
PERTH	4.7%	4.0%	4.8%	5.5%	4.3%
HOBART	8.5%	4.8%	3.5%	4.0%	6.5%
CANBERRA	6.0%	6.0%	5.0%	4.8%	4.5%
DARWIN	5.0%	3.0%	4.0%	6.5%	5.0%

CONTRIBUTION TO COST ESCALATION BY INPUT – INFRASTRUCTURE





CONSTRUCTION ACTIVITY BAROMETER BY BROAD SECTOR

	STARTS 2023/24 (INFLATION-ADJUSTED)	VS STARTS 2013/14–22/23 (AVERAGE ANNUAL)	LEAD INDICATORS ($B, INFLATION-ADJUSTED, 2023/24)
BUILDING			**APPROVALS**
COMMERCIAL	$19b	9% higher	$20b
APARTMENTS	$27b	16% lower	$24b
INDUSTRIAL	$11b	52% higher	$12b
SOCIAL	$22b	5% lower	$24b
INFRASTRUCTURE			**WORK YET TO BE DONE**
TRANSPORT	$32b	3% lower	$45b
UTILITIES	$43b	21% higher	$46b
RESOURCES	$25b	2% lower	$33b

Source: ABS, WT

LEGEND:

- 2023/24 activity more than 20% above annual average of the prior decade
- 2023/24 between 10 and 20% above annual average of prior decade
- 2023/24 activity between +10 and –10% vs annual average of prior decade
- 2023/24 activity between 10 and 20% below annual average of prior decade
- 2023/24 activity more than 20% below annual average of prior decade

KEY POINTS TO ESCALATION OUTLOOK BY MARKET

CAPITAL CITY MARKETS

Sydney

Escalation is set to remain stubborn, with increased unionisation of trades, the ongoing impact of regulation, strength in sectors such as **health** and **transport**, and the risk of skills flowing to Brisbane and South East Queensland.

Melbourne

Similar to Sydney, the Melbourne market is seeing the impact of regulation and the attraction of skills to local infrastructure projects and to opportunities north of the border. State government debt profile, statutory headwinds and broader economic sentiment are also weighing on conditions. Fundamentals should reassert themselves but perhaps not until after the next state election.

Brisbane

We expect to see continued market tightness, a strong pipeline, and shortages of key trades driving the outlook for Brisbane. However, the relationship between the sector and government policy should improve with the change of government.

Adelaide

A robust pipeline of major projects will keep escalation elevated. Several of these projects require Tier 1 involvement, likely increasing the influence of enterprise bargaining agreements (EBA) and driving escalation higher.

Perth

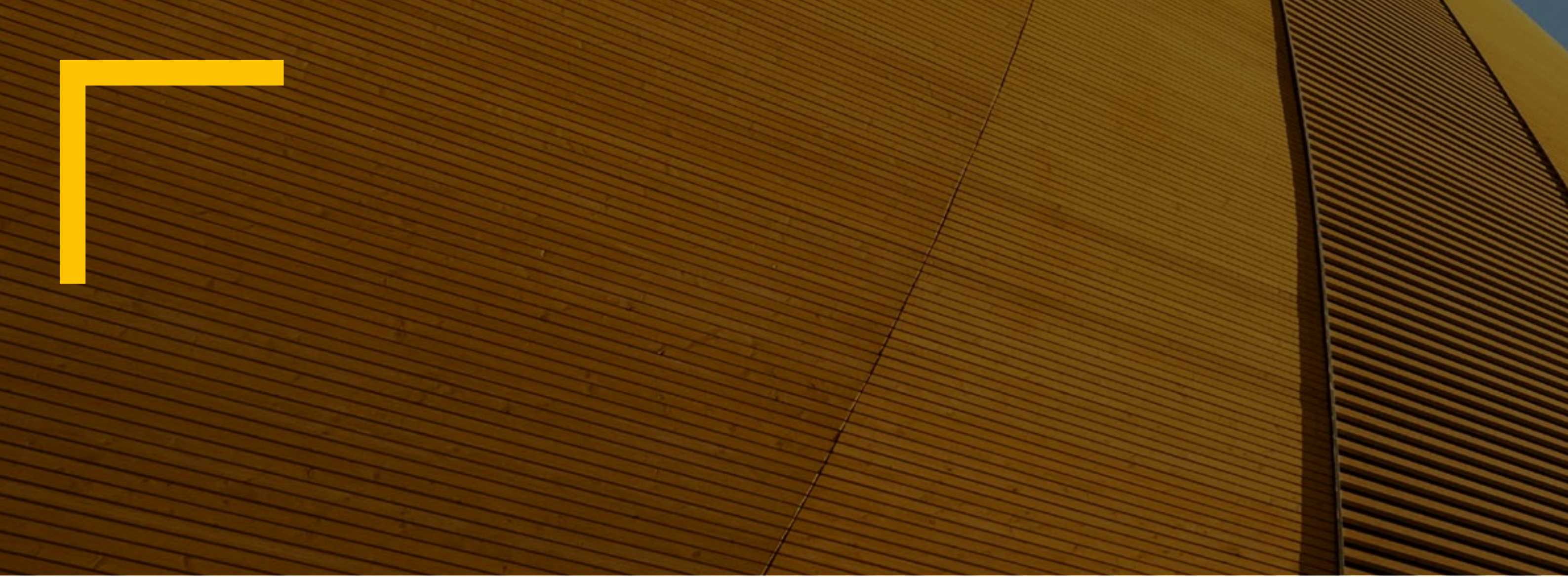
Healthy market fundamentals are exacerbating difficulties in attracting and keeping labour with the impact of the new EBA keeping escalation at or above 5% for some time to come.

Hobart

Escalation is expected to remain high, though uneven across sectors. In major projects, escalation is likely to rise further, particularly where trades are on EBAs. For smaller projects, escalation may be lower, with more contractors seeking work.

Canberra

Continuing concerns about the (federal-led) **commercial** pipeline are weighing on escalation, although the **social** pipeline is stronger. Elevated **infrastructure** spending is likely to put a floor under market cost pressures.



SMALLER CAPITAL CITIES AND MAJOR REGIONAL CENTRES

Darwin

We expect **defence** and, less so, **resources** and **renewables** to anchor activity amidst the ongoing battle to attract and keep labour. Escalation is set to average around 5% per annum to 2027.

Newcastle

Newcastle is well-placed to benefit from activity across many **building** and **infrastructure** sectors. Major concerns around skills shortages have been limited so far, but this may be tested in coming years.

Geelong

Geelong has a healthy project pipeline. The soft Melbourne market is boosting the supply of trades, but this may change when the Melbourne market recovers.

Gold Coast

There is an increasingly robust activity pipeline for the Gold Coast, which is stretching availability of resources to deliver projects across all sectors. This is continuing to put upward pressure on escalation.

Cairns

A healthy recovery in tourism, rebuild from the impact of Cyclone Jasper, elevated spending from local government, and strong market conditions in Townsville have contributed to a shortage of key trades and an elevated escalation outlook in Cairns. The change of government at the state level should see further pressures in the years ahead.

KEY POINTS TO ESCALATION OUTLOOK BY YEAR

2024

- Data and trends for the year so far have largely tracked as we outlined in our May 2024 report. Escalation has remained elevated in most markets and sectors despite construction activity moderating and most supply chain disruption having receded.
- **Building** escalation should be 4 to 5.5% for most cities – with Brisbane the exception at 7.5%. For **infrastructure**, escalation of 4 to 5.5% is also likely, with Canberra to stand out at 6%.

2025

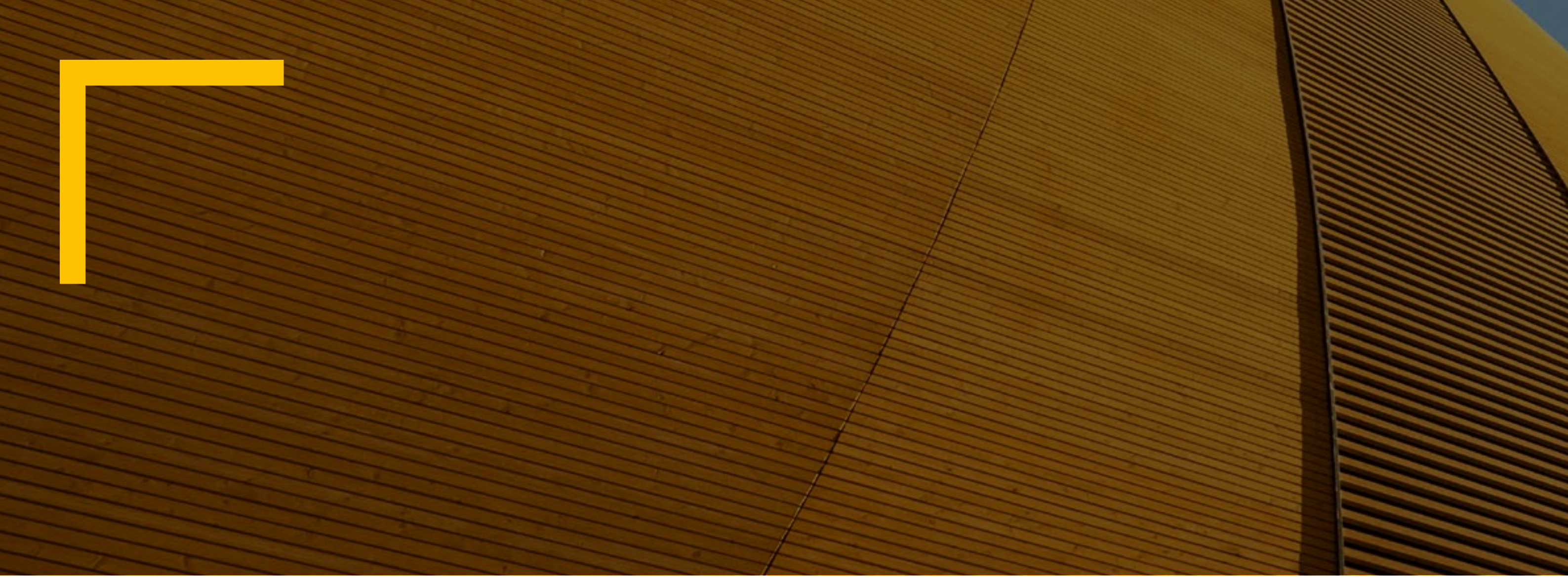
- While local and international economies should continue to see steady improvement, this will not translate to construction activity quite yet. Furthermore, the better economic numbers will increase some sources of escalation pressure.
- For **building**, escalation is forecast to be 4.5–6% across most cities. Brisbane is again expected to lead the way at 6.5%, while Canberra falls back to 3%.
- For **infrastructure**, the national average should hit 5.5% due to higher activity in many sectors.

2026

- By 2026, more concrete signs of improved market conditions should start to become visible. This will support the pipeline in the near term, perhaps putting some downward pressure on escalation via increased competition but, more importantly from a longer-term angle, laying the foundation for a sustained lift in sector investment in capacity and capability.
- For **building**, escalation is forecast to remain at 4.5–6% in most cities. Perth and Hobart are set to lead the way on the back of strong conditions, both at 6%.
- For **infrastructure**, our forecast is 4.5–6.5% escalation in most cities as activity rises further.

2027 and beyond

- By 2027, there should be greater visibility on the improved outlook for market conditions. Although much of the expected rise in sector investment may not yet be complete, the improved outlook may drive greater sector capacity/capability and put downward pressure on escalation.
- Hence, escalation is forecast to remain elevated in 2027 (4.5%–7.5% for **building** and 4.5–6.5% for **infrastructure**) before greater signs of downward pressure become likely from 2028.
- Signs of improved investment data should be visible by 2027; if these are not evident, the status quo may continue, or lower construction activity may eventuate.



Key implications and risks

- Current market conditions are not sustainable (both at the market-wide and project levels).
- Geopolitical risks and uncertainties are likely to persist at elevated levels, following the US election.
- A housing crisis response is likely to have an impact, including for key worker accommodation.
- China's economic outlook remains important, with the silver lining that weakness may mean sustained lower escalation on some materials and plant/equipment.
- A rigorous and legislated project pipeline may be one solution to insufficient sector investment – but the sector may become a target for outsiders before profit gains are realised.
- Sustained initiatives to boost numbers in vocational training for key trades may also be important. This could include greater targeted efforts to attract trades from overseas.

Woree Social & Affordable Housing Precinct (render), Cairns

BROAD SECTOR DRIVERS WITH IMPLICATIONS FOR ESCALATION

ECONOMY (LOCAL AND INTERNATIONAL)

The Australian economy appears increasingly unlikely to experience a recession. For those who remember the early 1990s, the early 1980s, or parts of the 1970s, this is good news. And, of course, this will generally mean an improved backdrop for construction activity.

However, the fact that the Australian economy has – 2020 aside – avoided a recession for over three decades is, on the surface, an amazing achievement. But an examination of the Gross National Expenditure chart on page 10 shows how economic growth has trended markedly lower over the last decade or so. Yes, the economy avoided a (non-pandemic-led) recession, but performance over the last decade has been uninspiring, with 2023 and 2024 solid examples of this.

It is then perhaps hardly surprising that the construction sector's view of its own outlook has become increasingly negative over this time (with many of its drivers tied closely to economic performance).

A key feature of our May 2024 report was that construction cost escalation was set to remain well above long-term historical averages due in part to insufficient investment in sector capacity/capability, and that this issue had taken many years to develop. A major implication of this is that the sector has not done enough to gear up for future growth. Instead, with market conditions of 2020–22 as the catalyst, elevated construction activity is often enough for above-average escalation to result.

This remains our view – however, such market positioning is not sustainable. With this report's coverage extended to 2027, the combination of improved economic conditions and a forecast upswing in construction activity could provide the platform for an overdue jump in the construction sector's investment. Visibility of these improved economic and sector conditions should be evident by 2027 but may be seen as early as 2026.

Such a scenario would be unlikely to noticeably impact on construction's capacity/capability and hence the escalation climate by 2027, but it does point to an improved likelihood of sector conditions commensurate with a subsequent reduced risk of elevated escalation.

While a recession is increasingly unlikely, a period of further weakness seems assured. Households remain under pressure, even with the recently enacted federal tax cut and a range of subsidies from various state governments. Ongoing weakness with households has begun to seep into the corporate sector, with profits taking a hit in recent quarters.

Importantly though, capital expenditure plans for this financial year have held firm and continue to point to a solid increase in construction spending.

Why might this be the case? One reason is the strength of public sector spending. The other is improved economic performance among many of Australia's key trading partners.

Some media and commentators consistently critique anything other than the minimum of government spending, even seeing such low levels of spending as excessive, wasteful or inefficient. There are signs that spending by some governments may be slowing, with higher interest rates increasing the budgetary impact of spending programs, but there is no doubt governments have become increasingly vital to the Australian economy remaining afloat.

With that said, the run of elections over 2024 and the first half of 2025 may see changes of government and spending cuts or, at the very least, the potential for reevaluating elevated spending. This is certainly a risk factor over the near term.

Elsewhere, further improvements to the external economic landscape have helped buttress the Australian economic situation. Periodic updates to the economic view of major international bodies (such as the International Monetary Fund, the Organisation of Economic Cooperation and Development, and the World Bank) over the last year or so have steadily increased the near-term economic outlook for major economies.

While several events in the United States have caused jitters or panic on US financial markets, this has not flowed through to the broader economy, which has carried on steadily. Even in the aftermath of the US Federal Reserve's recent and somewhat surprising 50 basis point interest rate cut, economic and markets data have settled quickly, bringing a strong regime of further interest rate cuts into increasing doubt.

Even for China, where economic performance has been patchy over the last 18 months or more, the recent announcement of quite significant economic stimulus suggests that concerns about recent growth are genuine and that there should be some economic improvement in response.

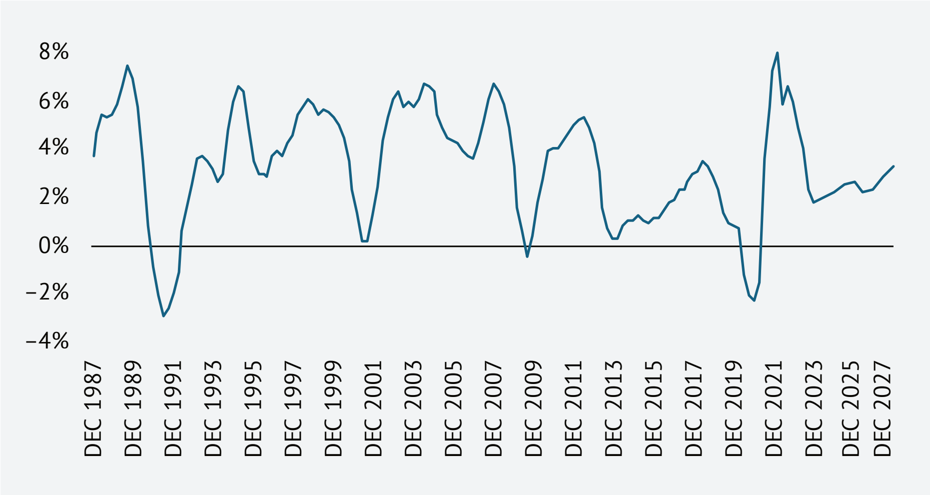
The US presidential election could see many different scenarios play out, some of which could weigh on near and even medium-term Australian economic performance. More broadly, the climate of geopolitical volatility and risk remains elevated. While the US election outcome may be prominent

Gross National Expenditure (GNE)

Annual % change

(2024 estimate, 2025–2027 forecast)

Source: ABS, IMF, WT



in the eyes of many, the potential for (further) war and unrest in much of the world arguably has greater potential to play havoc with escalation.

If the Australian economy can avoid these risks and maintain a steady, if somewhat underwhelming, growth trajectory over this year and next, conditions should begin to improve further from 2026 and into 2027. In addition to factors already mentioned, this outlook should be supported by the ongoing need to invest to facilitate recent (and expected) population growth, a now-substantial arsenal of interest rate cuts to be deployed by the Reserve Bank of Australia (RBA) if need be, and the potential for significant increases in investment (mostly by business but also by government) in areas such as AI, the clean energy transition and resilience of infrastructure.

CONSTRUCTION-WIDE ANALYSIS

Analysis of the construction sector more broadly provides wider context and a greater understanding of the current state of play. Specifically, why did the end of pandemic-era disruption not lead to escalation returning to the long-term average of 3% per annum in most markets?

Overall construction activity

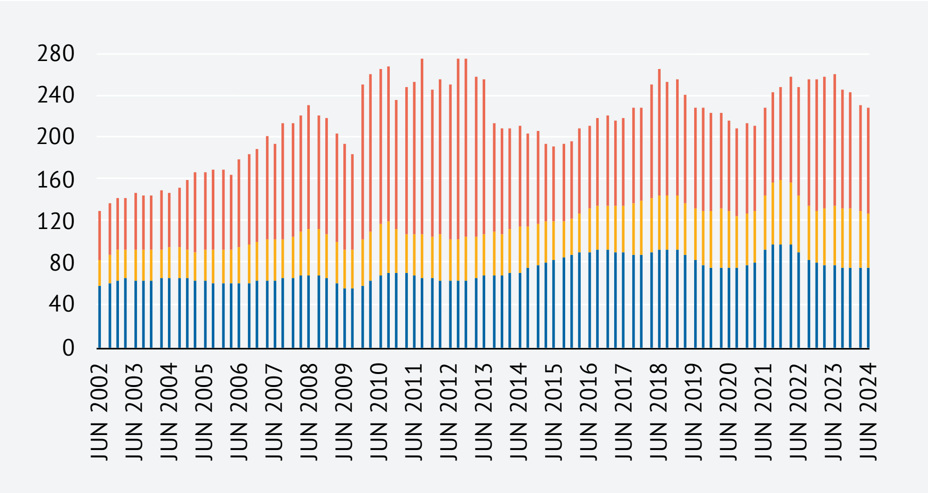
Looking across the construction sector (residential, non-residential and infrastructure), our construction activity chart below shows activity was at a sustained decade-plus high during 2021/22 and 2022/23, in part due to policy and other decisions to provide stimulus in the wake of the pandemic. For **building** sectors, this period was the highest level of activity on record. For **infrastructure**, while activity during much of the 2009–13 period was higher than in recent years, a notable portion of this work was (a) directly related to the mining boom and (b) undertaken offshore and shipped to Australia (with the full value of this work incorrectly assigned to construction).

While total activity has eased about 12% since peaking in June 2023 and supply chains are now largely repaired, escalation remains at the same elevated levels in most markets and sectors.

Construction activity by broad sector

$b

Commencements basis, moving annual total, inflation-adjusted



Residential
Non-residential
Infrastructure

Source: ABS, WT

Amount of work still in the system

While the total value of construction starts has moderated over the last few years, other trends mean the amount of work in the system peaked during 2023/24 at record high levels. These trends include larger and/or more complex projects and greater requirements for more specialist trades and equipment. Separate Australian Bureau of Statistics (ABS) data (only available for **building** sectors) on the value of work under construction indicates a similar conclusion for work yet to be done.

There is one more aspect of broad sector analysis that helps paint the complete picture of why escalation remains elevated: trends in investment (or lack thereof) in sector capacity and capability.

Investment in sector capacity/capability

We introduced this concept and its impact on escalation in our May 2024 report. New investment in productive capacity (and capability) reflects confidence in medium-to-long-term growth prospects, as well as the periodic need to update and replace aging infrastructure.

As the chart on page 13 shows, the trend of new investment in construction has flattened almost completely since 2010, despite the sector's strong recent activity, record levels of work in the system and robust demand drivers. For the non-metallic mineral products sector (responsible for key building materials including glass, concrete and plasterboard), the trend has been negative since 2010.

Larger and/or more complex projects and greater specialist trade and equipment requirements translate to a greater need for new sector investment, not the same or less.

Encouragingly, ABS capital expenditure data has suggested that the data over recent quarters has improved. Capital expenditure is not quite the same as investment (known in economic jargon as gross fixed capital formation), but it is reported quarterly as opposed to investment (by industry), which is only reported annually.

Work yet to be done by broad sector

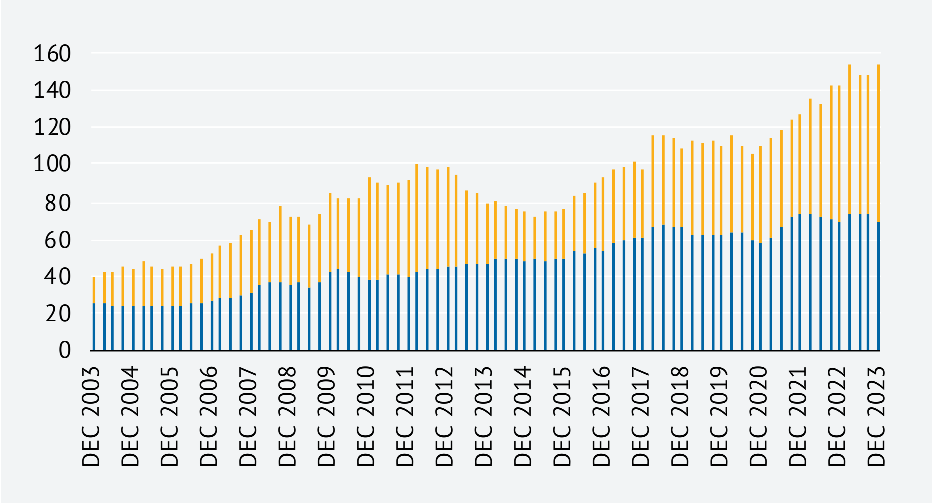
$b

Inflation-adjusted

Building (non-res, apartments)

Infrastructure (ex-mining)

Source: ABS, WT



Even if the 2023/24 investment data shows stronger figures for construction, this situation has been years in the making. A quick fix is unlikely. With that said, the unsustainability of the status quo – and our view that an improved economy and stronger outlook for construction will become apparent by 2027 (if not 2026) – could provide the basis for a sustained and overdue upswing in sector investment. A return to the long-term escalation average heading back towards 3% may not be far off.

Of course, sector profitability is important here too. Construction sector margins have been poor for many years and sector insolvencies continue to move higher, well into record territory. Of more immediate importance, however, the sector requires state governments to remain committed to their significant construction programs, at least for the next few years, amid long-term highs in debt and debt-servicing costs.

International Towers, Barangaroo, Sydney

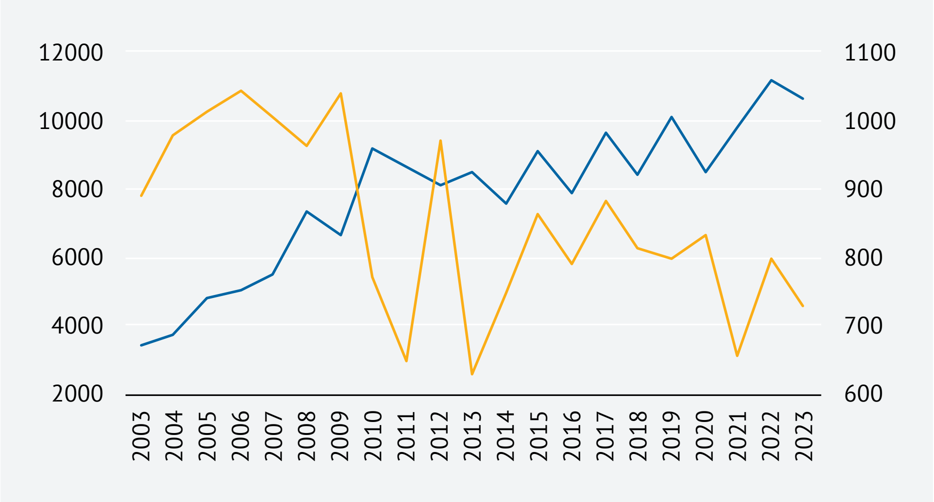
New investment in sector capacity/ capability

$m

Inflation-adjusted

- Construction
- Non-metallic mineral products manufacture (right axis)

Source: ABS, WT



IMPORTANCE OF STATE GOVERNMENTS

State government budgets have traditionally received much less attention than their federal counterparts. However, this view has shifted in recent years, given how significant some state government investment programs have become.

More importantly, while the federal government has made prominent efforts to rein in its (mostly infrastructure) construction spending, states – certainly the major ones – have largely carried on regardless.

While the state government contribution to construction activity has become increasingly important, the pressure that this has placed on state budgets has increased, both in absolute terms but also indirectly via increased debt and debt servicing costs.

There is no 'magic number' of debt to total state output that triggers a credit rating cut (i.e. increases state borrowing costs) or any other significant consequence. For NSW and Victoria though, debt profiles have moved into unchartered waters (at least in the post early '90s recession era). There were some efforts in their FY25 budgets released earlier this year to keep a lid on construction spending levels, but these were insignificant in the bigger picture.

Queensland appears to be the next to move into danger territory. Queensland's spending profile in the years ahead will be significant and is largely locked in, while there are concerns over the revenue side (led by coal royalties). Only Western Australia is really in a healthy position when it comes to state government finances.

With that said, we don't expect any major cuts to state government-led construction programs in the near term, even in those states with or likely to see a change of government in the run of elections over 2024 and 2025. Victoria might be under most pressure, but with its next election not until November 2026, any spending cuts of note may not take place until 2027 at the earliest.

CONSTRUCTION ACTIVITY OVERVIEW AND OUTLOOK BY KEY SECTOR

The table below and the chart opposite reflect our combined view on demand (i.e. the project pipeline, the strength of various drivers and how the state of these drivers in recent years will translate to projects being delivered) and supply (cost pressures for specific inputs in the context of the overall capacity/capability issue for construction).

Construction activity outlook to 2027 by sector

SECTOR	OUTLOOK TO 2027	2027 $b (2024 $b)
Commercial	Data centre, transport key drivers; next office projects likely by 2027	$26b ($23b)
Apartments	Strong need for activity but timing may shift via ongoing sector issues	$30b ($24b)
Industrial	Current drivers to persist, keeping activity elevated for medium term	$13b ($12b)
Social	Stadia, accommodation, defence, aged care to offset softer health, education	$23b ($24b)
Transport	Next rail (and ports) projects to offset fewer major roads projects	$26b ($26b)
Utilities	Strength in renewables, water and telco make utilities best performer	$51b ($46b)
Resources	Uplift via gas, critical metals, hydrogen but well off early 2010s pace	$25b ($18b)

Source: ABS, WT, numerous sources of project-level information

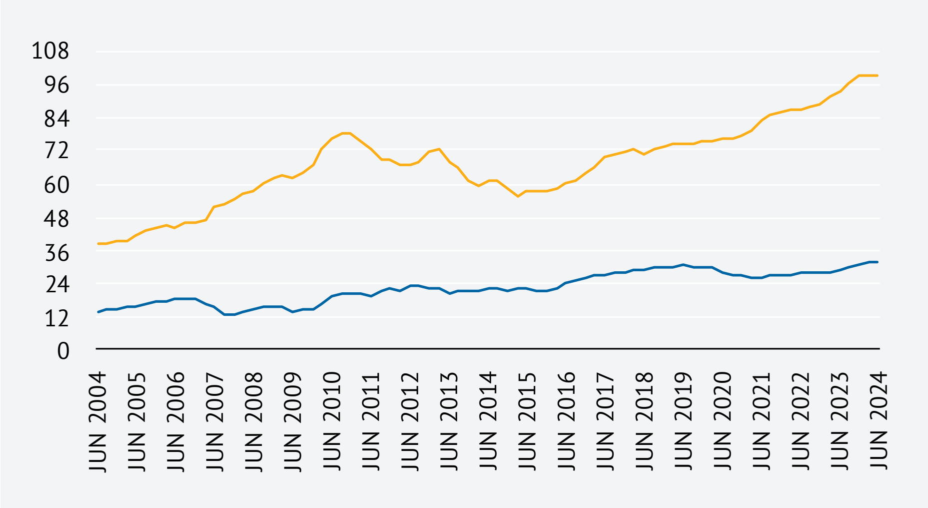
New investment (construction + other): federal v. state governments

$b

Inflation-adjusted, annual totals shown quarterly

Federal
States

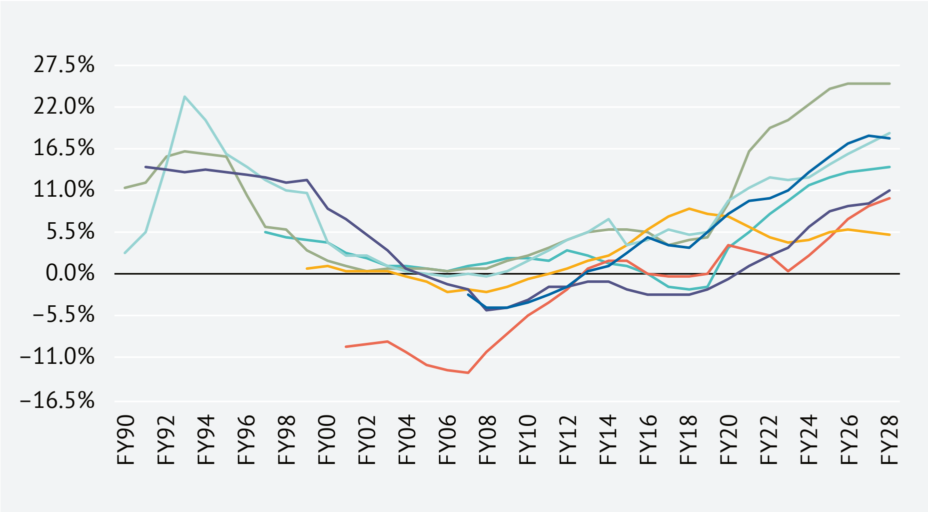
Source: ABS, WT



Net government debt: % of gross state product

NSW
VIC
QLD
WA
SA
TAS
ACT

Source: Numerous state government budget papers, WT



Construction activity outlook by sector

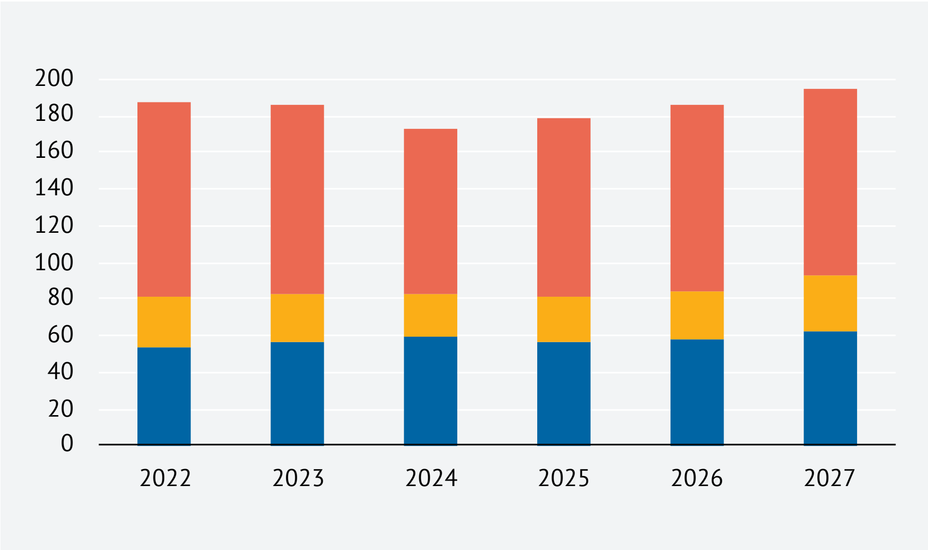
$b

Inflation-adjusted

(calendar years, 2024 estimate, 2025+ forecasts)

Non-residential
Attached residential
Infrastructure

Source: ABS, WT



IMPLICATIONS FOR CONSTRUCTION COST ESCALATION

At the beginning of this section, we noted the key factors for how we got to the current situation (with above-average construction cost escalation remaining persistent):

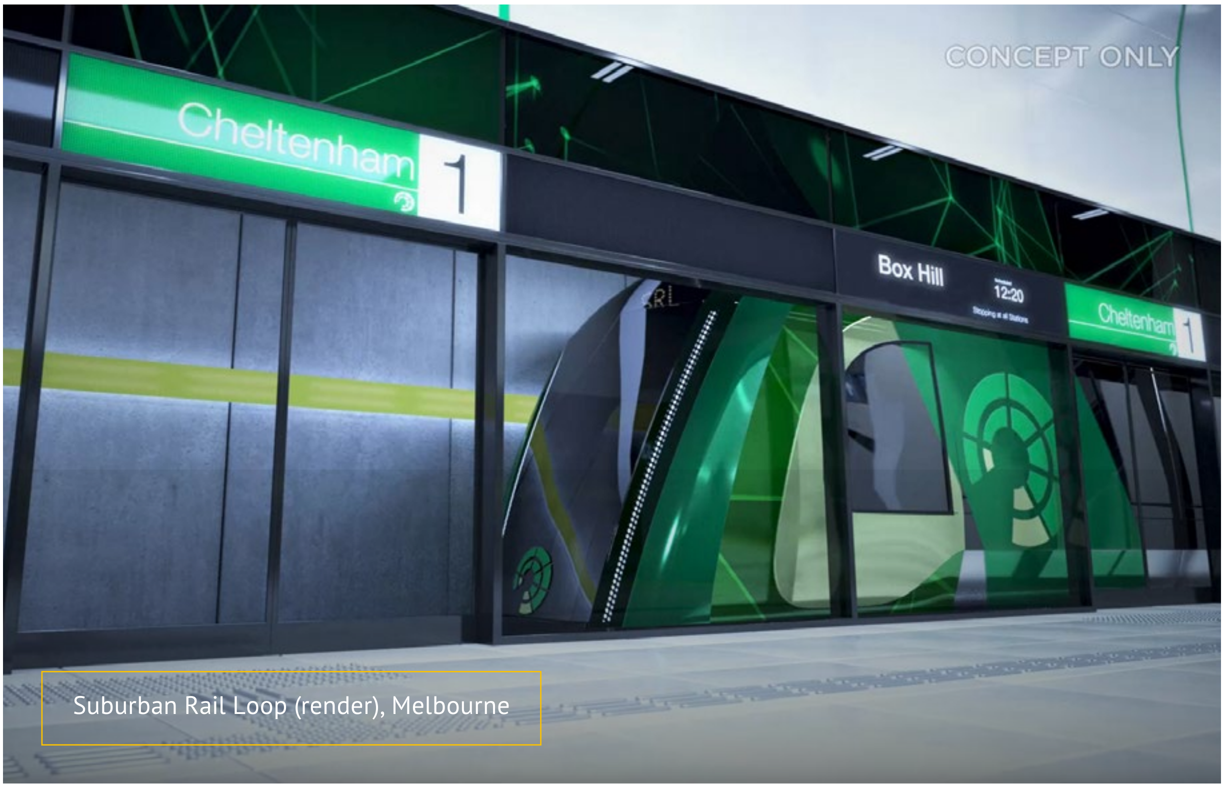
- economic underperformance and a lack of belief that economic growth could return to pre-global financial crisis levels
- elevated construction activity across all sectors
- record levels of work in the system, due initially to supply chains being disrupted by the pandemic before changing trends in terms of size and complexity of projects (necessitating more specific/niche trades, materials and equipment) took over as a cause
- sub-par levels of investment in sector capacity and capability (with sector margins and profitability also coming under increased pressure) since the early 2010s.

With momentum of construction activity cooling over recent years and underlying economic performance weakening further (albeit remaining above recessionary territory), this is a difficult environment for the necessary investments in sector capacity/capability to come through.

While recent quarters of capital expenditure data have strengthened and suggest a high likelihood of stronger construction sector investment in FY24, ongoing difficult sector conditions make a sustained lift in this investment through FY25 unlikely.

Hence, our view is that construction cost escalation for **building** and **infrastructure** across key markets to 2027 will remain elevated.

However, our outlook to 2027 points to improved economic and construction market conditions. Combined with an increasing realisation that the status quo is unsustainable, we believe this will lead to an increasing likelihood of stronger sector investment from 2026. This would be unlikely to come onstream by 2027, but it does point to a climate of less escalation pressure by the late 2020s.



Suburban Rail Loop (render), Melbourne

ESCALATION ANALYSIS
KEY COMPONENTS

LABOUR (DIRECT)

Recent trends: It appears that construction wages growth has finally peaked, reaching a 14-year high in March 2024. Leading indicators of construction activity and labour demand had pointed in this direction for some time, which is a signal of how tight construction labour markets remain.

Looking forward: The state of play regarding a national, comprehensive view on construction wages has always been tricky but recent trends suggest this is becoming more difficult.

While the construction sector is seeing general market conditions continuing to moderate further, which would point to wage escalation following suit, the strong numbers from the recently enacted enterprise bargaining agreements (EBAs) will put a floor under these declines.

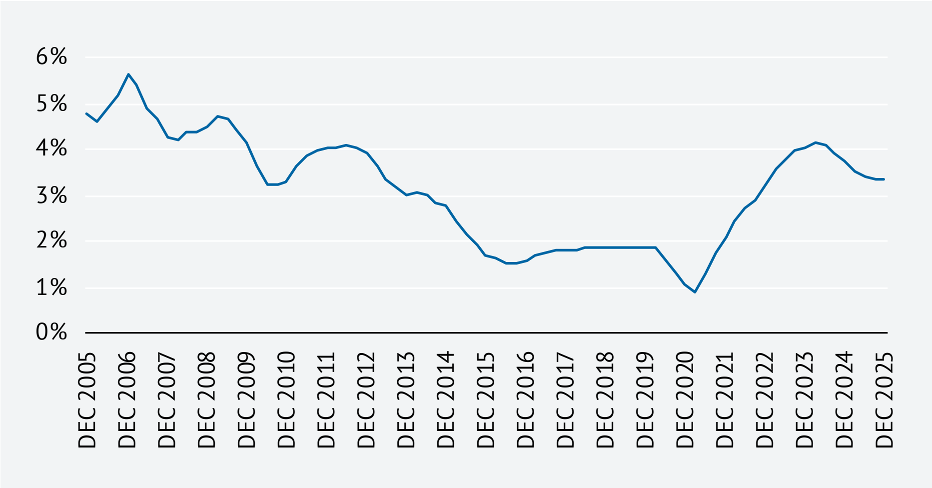
Overall sector wages growth may remain steady or even increase, but the exact proportion of workers for whom the new higher EBA wage escalation conditions will apply is unclear. Furthermore, the strength of the new EBA is set to deliver a supersized wage boost in FY25 – over 10% (from the perspective of wage levels averaged over the year vs those of the previous year) before the agreed-upon 5% per annum wage increase cadence returns from FY26.

Australia construction wages

Annual % change

(calendar years: 2024 estimate, 2025 forecast)

Source: ABS, WT



Data from the Department of Employment and Workplace Relations (DEWR) and the ABS suggests around 7% of construction workers are currently covered by a construction EBA. However, EBA conditions cascading down to subcontractors on major projects or to those in other Tier 1 builders or others in construction is well known in the industry. That the recently enacted EBAs will run through to FY28 could see this situation continue for several years.

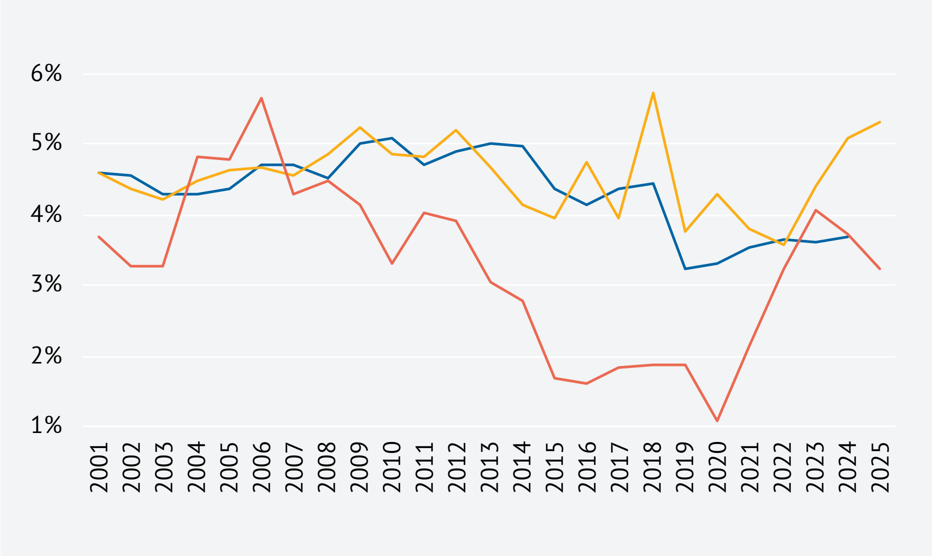
An outlook with elevated wage escalation over the medium term seems likely, however our forecast for improved market conditions by 2027 will be important. Should this be delayed, it may reduce labour's bargaining power for the next EBA while putting downward pressure on non-EBA wages.

Annual construction wages growth by wage determination mechanism

(calendar years: 2024 estimate, 2025 forecast)

- EBAs (total)
- EBAs (recently approved)
- Total construction wages

Source: ABS, DEWR, WT



Deeper dive – specific trades (labour capability, implication)

Analysis of drivers of wage escalation by trade has the potential to highlight new trends and build a greater understanding of how escalation can differ across trades.

While Australian Tax Office (ATO) data on wage escalation by trade is very interesting (even if it lags by two or more years), commencements data (of apprenticeships or other vocational training) is perhaps most relevant. Put simply, commencements of apprenticeships represent investment in the number and quality of trades. It is an additional angle to the concept of investment in capability presented for the sector in general, and for production of building materials.

On this metric, carpenters fare worst with numbers weakening over recent years. The fact that demand for carpenters (as represented by job vacancies) is relatively flat has prevented even stronger wage escalation for this trade.

Strong demand for electricians has led to a response in vocational training numbers, but it is not yet robust enough to prevent elevated wages growth. With demand for electricians likely to increase further over the medium to long term because of the renewable energy boom, vocational training numbers will need to increase substantially to prevent even stronger wages growth.

It is worth noting that short-term workers are usually only a small proportion of the workforce for each trade (well below vocational training numbers). Much greater visa numbers from this source would put downward pressure on escalation and help reduce the recurring skills shortage threat but this may not be realistically or politically achievable.

Wage escalation drivers/metrics by trade

	CARPENTERS/ JOINERS	PLASTERERS/ RENDERERS	ELECTRICIANS
JOB VACANCIES (AS % OF EMPLOYED)			
COMMENCEMENTS (OF APPRENTICESHIPS)			
ESTIMATED (ATO) WAGE ESCALATION			

LEGEND:

- Improves escalation significantly
- Improves escalation somewhat
- Has no real impact on escalation
- Makes escalation somewhat worse
- Makes escalation much worse

Note: Shading reflects % change between recent performance vs medium/long-term average
Note: ATO data only available to FY21–22; FY23–24 is WT estimates

Source: ABS, ATO, Jobs and Skills Australia, National Centre for Vocational Education Research

MATERIALS

Recent trends: The descent in materials escalation is just about at its lowest point. As expected, this will be seen in either September or December (2024) quarters (once final data for these quarters comes in) just over the 2% mark.

For materials priced and traded internationally, more moderate demand and incremental increases in supply have seen prices generally stabilise. An improved global picture has meant a higher bottom for materials escalation; although, ongoing economic weakness in China has translated to a softer picture for materials more reliant on Chinese demand.

For materials largely or totally produced locally, downward pressure on energy costs (via federal subsidies) has helped prices to stabilise.

Looking forward: For materials with price and demand mostly dictated by global factors, improvements in global demand should translate to prices in a near-to-medium-term setting. This, of course, includes China, where performance has continued to underwhelm but recent stimulus announcements should lead to some economic improvement.

For materials less tradeable internationally (produced locally), the likely ongoing presence of weak market conditions could see escalation remain flat, unless producers respond by limiting supply. Weak market conditions could also begin to impact the ability of producers to continually try to recapture pandemic-era costs. However, escalation may remain elevated by the long-term poor trend in sector investment in capacity and capability.

From a medium-to-long-term perspective, as the use of 'greener' materials becomes more common (at higher cost), escalation will shift higher until demand for these materials approaches other materials and the cost discrepancy narrows. Until then, projects based on greener materials could see much greater materials escalation than projects using cheaper alternatives.

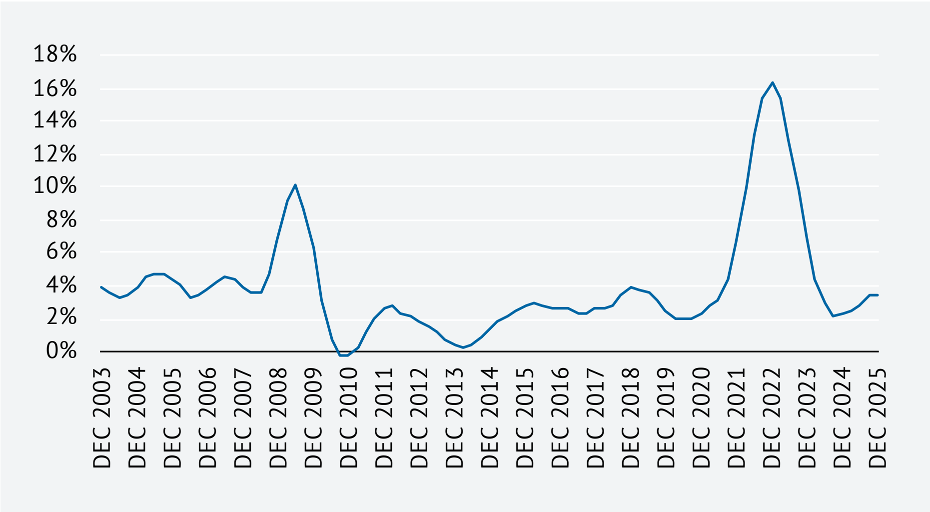
Of more immediate concern is the seemingly ongoing risk of significant international conflict, with freight and supply chain implications for materials costs (as for much of 2024).

Australia building materials cost index

Annual % change

(calendar years: 2024 estimate, 2025 forecast)

Source: ABS, WT



INDIRECT COSTS (INCLUDING PRELIMINARIES, DESIGN, OVERHEADS)

Recent trends: Indirect construction cost pressures have been notably stubborn, including:

- Professional services wage growth (both overall and for construction-specific sectors) likely peaked in recent quarters, hitting a 10.5-year high and (excluding COVID) 12-year high respectively.
- Sector insolvencies continue to grow, with another record high in the September quarter (876).
- Insurance cost escalation hit a new 23-year high in March, inching back to 15.3% in June.
- Strength in construction activity outside the five largest capital cities has continued, as represented by the percentage of construction job vacancies in rural areas hitting an 11-year high (excluding COVID) earlier this year.
- With the prospect of this rural and regional construction activity persisting for many years to come (led by very strong **renewable energy** construction), additional costs to attract workers away from major capital cities – such as Living Away From Home Allowance (LAFHA) and other labour costs – will become more widespread or even permanent.

We have noted previously that the rise in these costs has crucial follow-on impacts including:

- impact of insolvencies spread across overheads or new projects
- lower subcontractor competition, more so among Tier 2 players
- risk contingencies moving higher.

These phenomena have persisted, reflecting soft market conditions.

Looking forward: The persistence of elevated indirect costs, and – worryingly – these follow-on impacts, suggests there is more to come, given our near-term outlook.

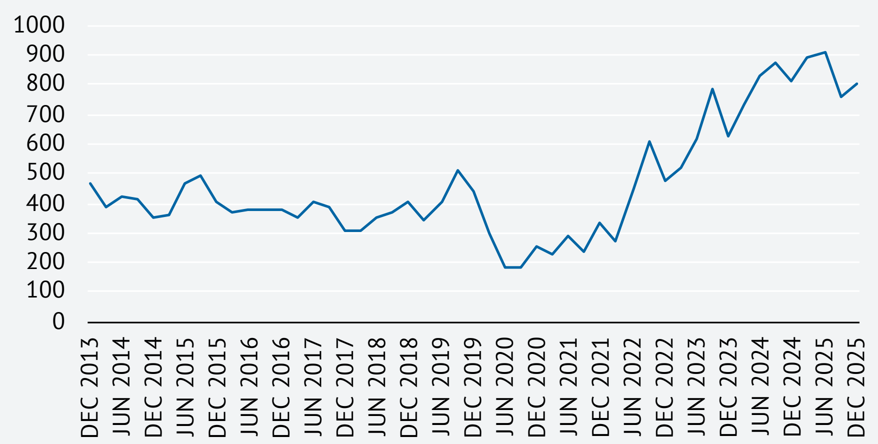
Most of the indirect costs raised are not related to the volume of work in the market. Instead, they reflect market imperfections or issues that have accumulated over many years and relate to insufficient investment in sector capacity or capability. This is another reason and motivation for the industry to swiftly remediate this weakness.

Australia construction insolvencies

Quarterly

(September 2024 onwards – forecast)

Source: Australian Securities and Investments Commission, WT



IMPLICATIONS AND RISKS

Sustainability of market conditions

- From a market-wide angle, the combination of above-average escalation, weak margins/profits and elevated construction activity is not sustainable.
- At the project level, ongoing cost pressures (more so for projects based on EBAs and using 'greener' materials) in a climate of sub-par demand is also not sustainable.
- The need for some sort of resolution to these key issues is a crucial implication of this analysis.

Geopolitical

- The potential for geopolitical uncertainty and volatility to impact upon market conditions continues and is likely to persist. This includes impacts from the US presidential election, with the full consequences and ramifications possibly not confirmed until January 2025.

Housing

- While a completely successful resolution of the housing crisis, including completing all announced policy and reaching targets, may be wishful thinking, any notable uplift in **residential** construction will have cost impacts on non-residential and, less so, on **infrastructure**.
- A related but increasingly important issue is housing for key workers. This is especially so with more major projects in regional areas but also constrains projects in capital cities.

China

- Should the Chinese economy remain weak or follow the Japanese path towards indefinite malaise (from the early 1990s), it will impact Australia directly and indirectly for an extended period.
- However, weakness in China may see even greater production of building materials and plant/equipment (similar to recent booms in renewables, chips, and electric vehicles). This would put downward pressure on these costs, reducing cost escalation, including in Australia.

Project pipeline – possible regulation

- One way to encourage investment in sector capacity/capability would be for government(s) to have a medium-to-long-term project pipeline backed by legislative power.
- This would give the sector much-needed certainty (and much greater in-house construction knowledge in government to be able to prepare a detailed, fully costed project pipeline) – but would risk becoming lucrative to foreigners or other outsiders.

Supply of key trades

- Greater government support and/or intervention may be the best levers to ensure sufficient numbers in vocational training for new trades, both to complete the overall sector demands and to replace those due to retire.
- While not popular with unions, further investigation into facilitating the import of skilled trades appears wise. Thus far, data on overseas numbers entering Australia to start a construction trade are generally sub-par.

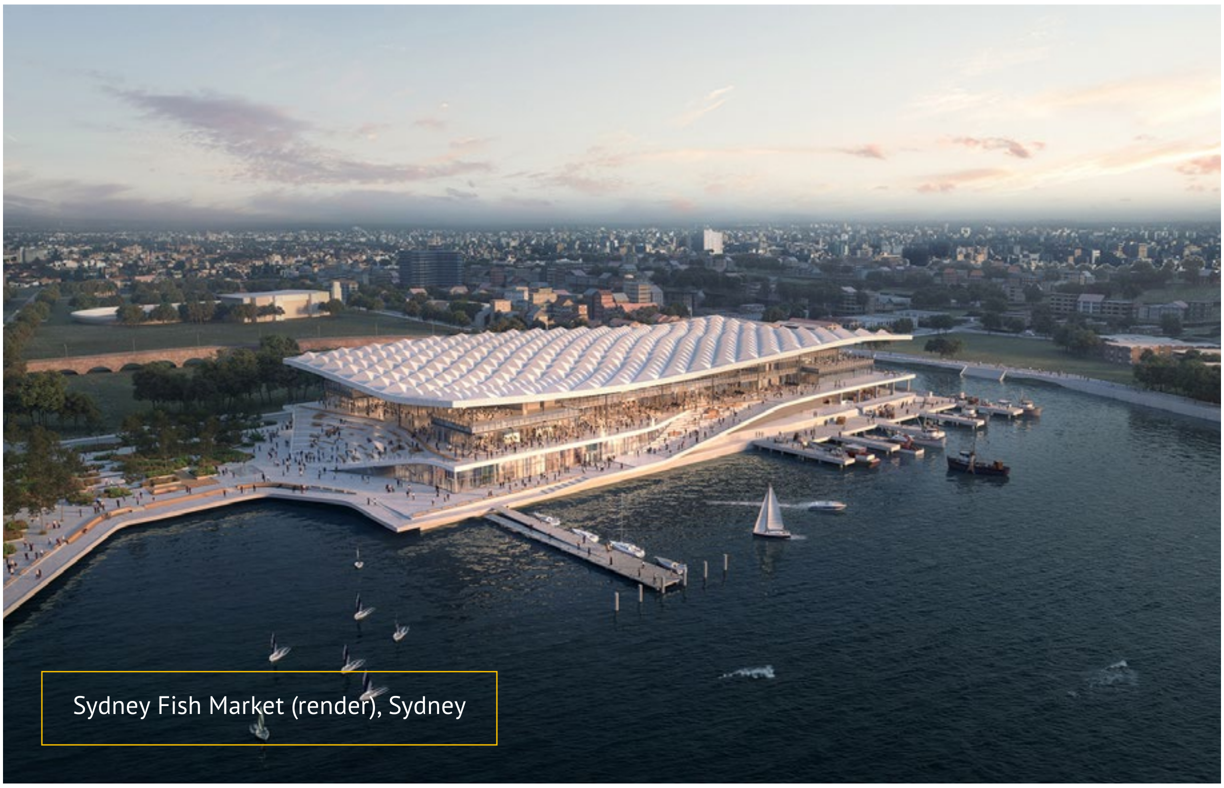
IN SUMMARY

Escalation has remained elevated in most markets and sectors, but elevated construction cost escalation is not sustainable. We expect to see some signs of improving market conditions emerge in 2026 and strengthen in 2027, which could be the catalyst for the investment in capability and capacity that the sector has long needed.

Escalation is forecast to remain elevated in 2027 (4.5%–7.5% for **building** and 4.5–6.5% for **infrastructure**) before possible downward pressure becomes apparent from 2028. A return to the long-term escalation average heading back towards 3% is possible from this point, but this is contingent on the necessary investment in the sector's capability/capacity coming through.

Key factors affecting the construction sector include ongoing geopolitical risks, the housing crisis, China's economic outlook, and the ongoing need for more training in key trades or more skilled trade migration.

We propose that a key opportunity to encourage investment in sector capacity/capability would be for government(s) to develop a rigorous, legislated medium-to-long-term project pipeline.



Sydney Fish Market (render), Sydney

DISCLAIMER AND METHODOLOGY

This report, and the market data it represents, are general market information only. WTP Australia Pty Ltd (WT) does not make or imply any specific advice or applicability of this information to any individual recipient. WT has taken care to ensure accuracy and that all data and details are correct to the best of our knowledge but does not warrant completeness or infallibility of said information. WT and its staff do not accept any liability for any loss or damage whatsoever arising from the use or dissemination of any part of this report (via any medium).

While our view is based on a variety of sources (not the least of which is our own market insight), the general approach in this pack is based on escalation from the input cost perspective. This aligns with the traditional QS approach to escalation but also allows rationalisation of bottom-up (i.e. input-level) and top-down (i.e. sector or economy level) escalation perspectives.

There is no single market-level data series that conceptually matches the above. However, data available by key inputs provides checks and balances on the overall WT view for key markets.

Points to note:

- All escalation shown is on a calendar year basis and is the % change between the full-year average vs the previous year's full-year average.
- Escalation contribution by input is on a general, Australia-wide basis, while state-by-state figures are general across sub-sectors, project types and values (i.e. contractor tiers).
- In addition, escalation contribution by input assumes no other major drivers of escalation (e.g. large productivity increases, significant regulation changes re approvals).

For more information on escalation relative to your project or sub-sector, please discuss with your usual contact or call your local WT office.

ABOUT US

At WT, we empower our clients to grow, inspiring confidence through our independent cost management and advisory services. Operating for 75 years, our expertise spans the building, construction, and infrastructure sectors.

We support our clients with an award-winning team of specialists in portfolio and program advisory, cost management and quantity surveying, commercial advisory, carbon and sustainability, and asset and facilities management.

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