DAVIS LANGDON

# CONSTRUCTION SENTIMENT
# The Davis Langdon Sentiment Monitor

Findings Report Five | May 2008

## EXECUTIVE SUMMARY

We are pleased to release the findings of this, our fifth Davis Langdon Sentiment Monitor.

Davis Langdon's Construction Sentiment Index fell 19 points across the past 6 months to reach 108 – the first fall since the commencement of the survey in 2006.

We hope the findings of this report are insightful for you and we look forward to updating the results again in Spring 2008.

If you would like to discuss the details of this report further, please contact Rachel Kelloway, Davis Langdon's National Research Manager, by email or phone:

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### Key Findings

- Industry sentiment turns the corner
- Market Volatility & the Credit Crisis – enters the hottest issues
- Shortage of Professional Design Services – impacting on 48% of industry
- Concern about costs – up 4% across the past 6 months
- Expectations for Tourism related construction have plummeted

# THE HOT ISSUES

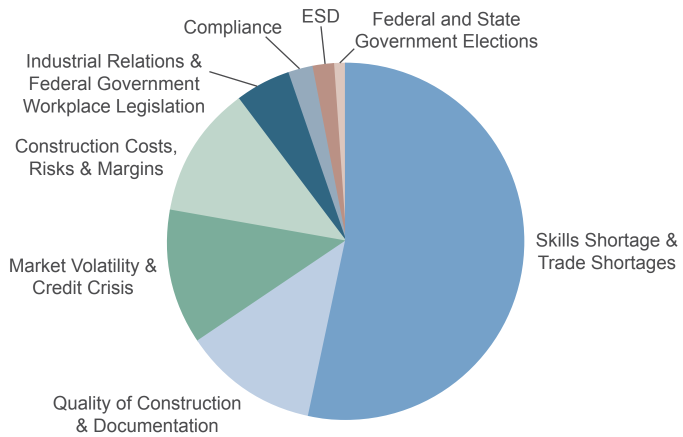
*Concern about Industrial Relations eased substantially, falling 11%*

**The Skills Shortage** remains uncontested as the hottest issue in the industry – worsening by a further 3% during the past 6 months to account for 54% of all respondents.

Construction Costs, Risks & Margins remains the second hottest issue (12%), however this time accompanied by two equally hot issues. The Quality of Construction & Documentation took a share of the pie at 12%, as equally did Market Volatility & Credit Crisis – a new addition to the hottest issues this time around (also 12%).

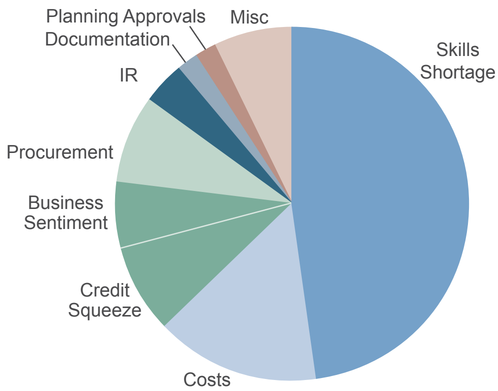
Concern about Industrial Relations eased substantially, falling 11% since last survey, indicating that industry participants are more confident subsequent to the change in Government – despite previously citing concerns that a change in Government may adversely affect Industrial Relations.

### The hottest issues in the industry at the moment



## PROBLEMS IN THE INDUSTRY

*Concern about costs lifted 4% across the past 6 months*




89% of participants now believe there are problems in the industry at the moment, down 10% on last survey.

While the Skills Shortage does appear to be easing as an industry concern (down 17% on last survey) it remains the greatest problem in the industry at the moment, according to 48% of respondents.

Concern about costs lifted 4% across the past 6 months (up 10% across the past year) maintaining its place as the second greatest problem in the industry.

Two new closely related problems have also emerged this time around – the credit squeeze (both globally and locally) along with the overall dip in business sentiment.

Accounting for a combined 14% of responses, these issues have emerged in the top three greatest problems concerning industry players.

Problems associated with procurement became a greater nuisance during the past 6 months too, escalating by 7%. Participants identified the cost of entry to PPP projects as a major problem, along with indicating the implausibility of smaller firms being able to compete with the larger multi discipline firms in this arena.

## NEW BUSINESS – MODERATING

*The level of new business reported by participants eased somewhat...*

We are starting to see the first signs of some restraint making an impression on the level of new business being experienced in construction.

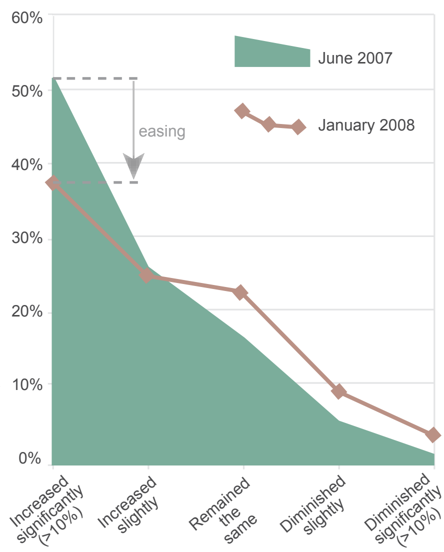
The level of new business reported by participants eased somewhat from last survey's peak. 37% reported 'significant' increases in new business during the past 6 months, down 15% on July 2007.

Similarly, 62% of respondents reported that new business to their firm had increased in some way, down 17% on the results from our last survey – and a solid indicator of an overall moderation for construction sentiment.

The greatest increase was from those participants who reported their levels of new business remaining unchanged – up 7% to reach 24%.

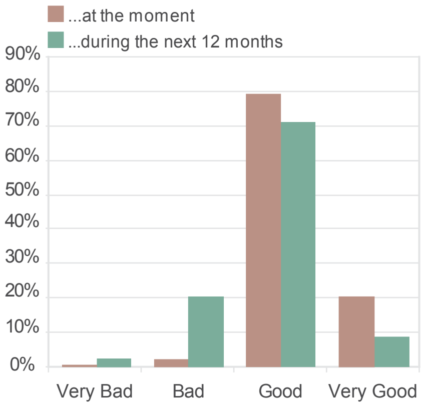
13% of the industry reported that their level of new business had diminished in some way – up 8%.

**Has the level of new business in your company changed in the last six months?**



## THE STATE OF INDUSTRIAL RELATIONS

**How do you perceive Industrial Relations?**



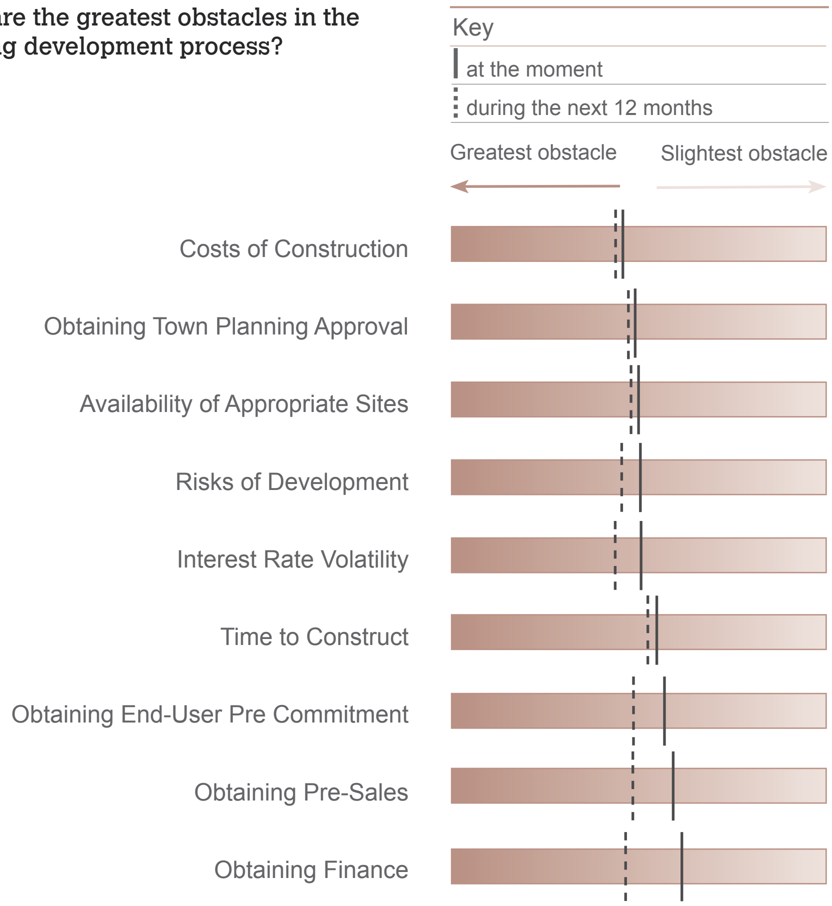

Sentiment toward Industrial Relations is at its highest since the commencement of the Davis Langdon Sentiment Survey, with 99% of respondents agreeing that industrial relations are Good to Very Good at the moment.

Our previous Findings Report (July 2007) coincided with the lead up to the federal election and revealed concerns about the possibility of adverse impacts with a change of government. It is not uncommon for sentiment toward Industrial Relations to be seriously impacted upon by fear of the unknown, however we have yet to see sentiment toward industrial relations take a significant turn.

Expectations for the next 12 months are damper, with 19% of respondents expecting bad industrial relations ahead.

## GREATEST OBSTACLES IN BUILDING DEVELOPMENT

**What are the greatest obstacles in the building development process?**




For the past three years we have asked participants to indicate the greatest obstacles they are experiencing in the building development process. For the first time since the commencement of the survey notably pessimistic sentiment pervades, with participants anticipating every obstacle will worsen during the next 12 months and indicating a significant turning point in construction sentiment.

The Costs of Construction crept up the list of concerns to become the greatest obstacle to building development at the moment (previously the third greatest obstacle). Participants have indicated they expect this situation will worsen during the upcoming 12 months.

Town Planning Approval remains the second greatest obstacle, unchanged on last survey, however followed closely by Availability of Appropriate Sites – with both expected to worsen during the upcoming 12 months.

Interest Rate Volatility, which previously posed the slightest obstacle to development, worsened considerably, leaping four places to become the fifth greatest obstacle to building development. Our survey participants hold a general consensus that the worst is yet to come, with expectations that it may become the top obstacle within the upcoming 12 months.

Obtaining Finance nevertheless poses the least concern to industry players – at least for now. Slipping three places to become the slightest obstacle, participants expect this situation will worsen significantly during the next 12 months.

## DESIGN AND CONSTRUCTION STANDARDS

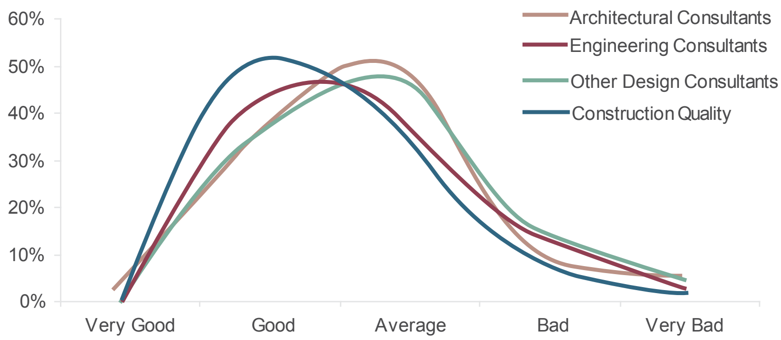
Based on their recent experiences we asked participants how they rate the standard of Design Consultants and Construction Quality at the moment.

Sentiment towards Construction Quality continues to fluctuate, with 50% of respondents reporting Good to Very Good Construction Quality – up 15% during the past six months, but still 11% lower than a year ago.

The standard of Engineering and Design Consultants received a fairly even spread of responses, with recent experiences reflecting that participants are still split broadly across Good, Average and Bad experiences.

Architects enjoyed a significant swing, with over a third of industry participants now reporting experiencing Good to Very Good standards of Architectural Consultants – up 7% on a year ago.

**In your recent experience how would you rate the following ...**




## PLANNING APPROVAL – ARE WE THERE YET?

*84% of respondents now cite delays of 30% or more.*

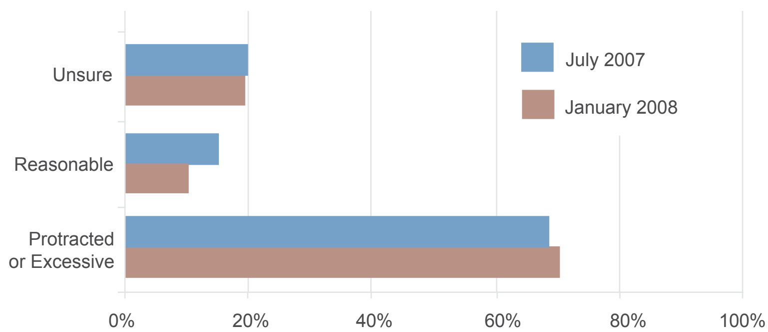
Town Planning Approval remains the Achilles heel of the development process.

The number of respondents reporting excessive or protracted delays crept higher (up 5% on July figures), to reach 69%.

The timeframe for the delays being experienced worsened slightly – with 84% of respondents now citing delays of 30% or more (up 3% since June 2007).

The number of respondents experiencing reasonable timeframes slipped to just 12% (down 4%).

**Is the timeframe for obtaining town planning approvals excessive or reasonable?**



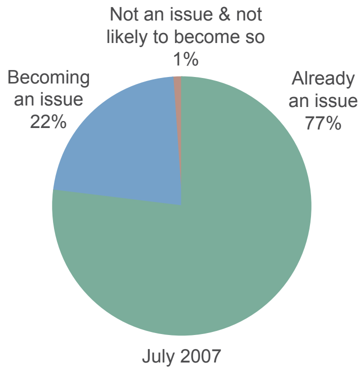
## GREEN OBJECTIVES

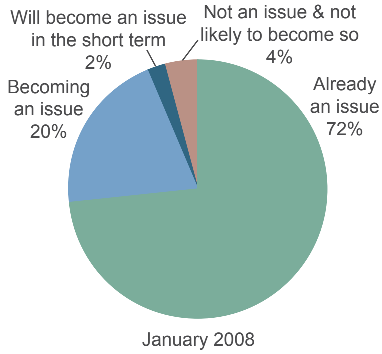
**Green objectives eased slightly** as an issue since our last survey in July 2007.

Participants who reported that green objectives are Already an issue or Becoming an issue, declined by 7% to reach 92%, while 4% of respondents do not view green objectives as an issue.

We wonder whether the mainstreaming of sustainability as an issue has influenced participants responses; whether the oversaturation of sustainability messages through all forms of media and industry has forced some participants into a kind of complacency?

**To what extent do you see green objectives for development to be relevant to your sector and region?**




## GOVERNMENT PROJECTS

*77% of the industry is in some way involved in Government projects.*

**Exposure to Government projects** remains stable with 77% of the industry reporting that their business is in some way involved in Government projects.

State Government work remains more dominant than Federal Government workload. 59% of the industry has involvement in State Government work, with participants reporting that State Government work makes up approximately 43% of their total workload.

35% of participants are currently involved with Federal Government projects – these projects accounting for 15% of their total business at present.

Participants expressed that Government methods of procurement and terms of contract are often more onerous than some private sector clients. They are also concerned that political expediency is driving budget allocations and unrealistic project timeframes, without consideration of how these projects will be resourced.

## PROCUREMENT PREFERENCES – CERTAINTY IS THE NEW BLACK

*Clients are moving towards win-win arrangements to secure contracting performance...*

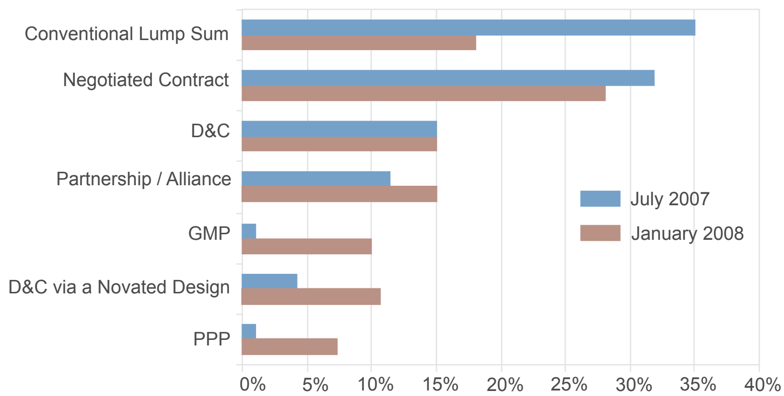
**Negotiated contracts** remain the industry's preferred procurement method and despite easing slightly since last survey, remain the preferred method by 28% of respondents (down 4%).

Preference for conventional lump sum contracts fell substantially since last survey, down 19% during the past 6 months, but keeping their place as the industry's second most preferred procurement method.

We see this as a sign of reaction to a relatively uncompetitive market and the industry's desire to better manage risk allocation. But as the industry returns to a more competitive state (see page 10) contracting preferences may change.

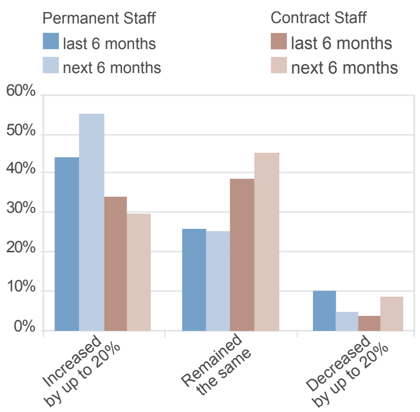
While PPPs remain the least preferred method of procurement, they managed to climb 6% since last survey.

### What is your preferred method of procurement?




## STAFFING EXPECTATIONS – SIGNS OF CHANGE

*Contract staffing declined significantly during the six months to January...*




**It appears that staffing** expectations may be beginning to stabilise.

Respondents expecting their staffing levels to remain stable doubled during the past six months, indicating that the winds of change have begun in the industry.

Contract staffing declined significantly during the 6 months to January with just 34% reporting Contract Staff increases (of up to 20%), while 45% reported Contract Staffing levels remained the same – indicating a measured slowdown in demand for Contract Staff.

44% of participants reported their own Permanent Staffing levels increased by up to 20%. While this is still positive news and unlikely to see the Skills Shortage ease any time soon, the result is still 19% lower than 6 months ago, indicating a slowing in expectations.

26% of respondents report that Permanent Staffing levels remained stable across the past 6 months and expect them to remain stable for the remainder of the year – double previous expectations.

## SKILLS SHORTAGES – THE TIDE HAS TURNED

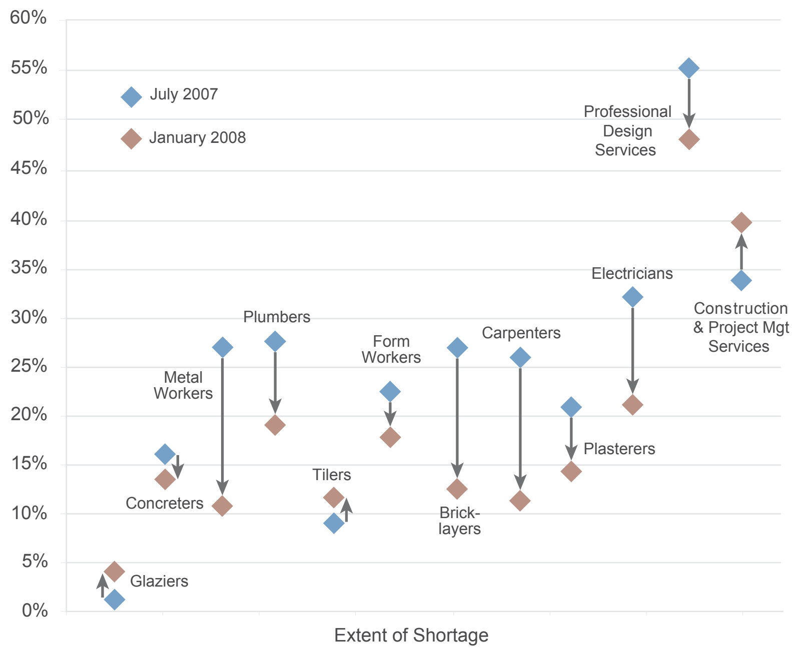
Across the board, shortages eased 6.4% since last survey, indicating some light relief – at least for the short term.

Professional Design Services continues to impact on 48% of all respondents, leaving it at number one on the Skills Shortage heap, despite easing by 7%. Construction & Project Management Services follows closely – up 5.4% on last survey, now impacting at 40%.

Plumbers, Form Workers and Electricians became the trades worst affected by the Skills Shortage, impacting on approximately 20% of respondents, but nevertheless down 5-10% on 6 months ago.

Demand for Metal Workers, Bricklayers and Carpenters eased significantly, with shortages alleviated by 14%-16% during the last 6 months.

### Skilled trades shortages – which areas are worst affected?



## SKILLS SHORTAGES – MAJOR CAUSES

*"(The) New generation (is) too soft to do the hard yards of the demands of the construction industry."*

**Like 'the recession we had to have'**, there is a general consensus that today's skills shortage has been in the pipeline for some time. 40% of respondents believe that a lack of training/education in the industry over the last 10 to 20 years is the major cause.

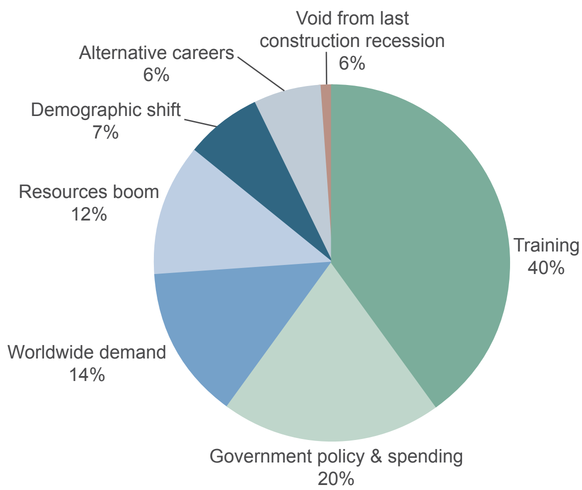
A secondary component has emerged which adds significant weight to this argument. There has been a sizable demographic shift in Australia during the past decade. The ageing of the workforce means baby boomer skilled labour and trades are retiring while concurrently, younger generations are opting for other types of employment in other parts of the labour force.

One survey participant went a step further, summing the problem up as "(The) New generation (is) too soft to do the hard yards of the demands of the construction industry".

Generation X & Y are increasingly exercising their extremely mobile workforce qualities – not only locally but into other countries.

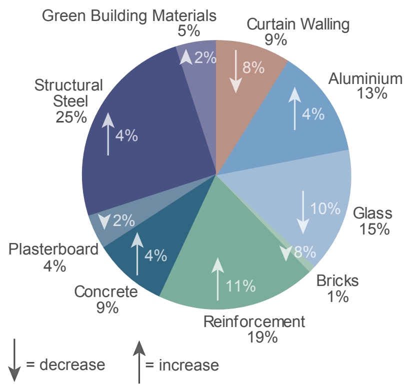
Respondents have identified worldwide demand for staff as one of the major contributors to our own skills shortage. The overseas migration of professional staff is exacerbating the problem, taking it to a global level.

Of course, Government policies and spending received the lion's share of the blame, with 20% of participants identifying that Government decisions to commit to major projects (at a time when the industry is overheated) is to blame.



## MATERIALS SHORTAGES

### Building materials in short supply




The scope of industry participants experiencing building material shortages eased 6% since the last survey, now with 34% of respondents reporting experiencing short supply of one or more materials.

The most affected materials include Structural Steel (up 4%) and Reinforcement (up 11%), which together make up almost half of all materials in short supply.

Glass shortages eased significantly during the past 6 months, as did Curtain Walling and Bricks.

For the first time Green Building Materials featured on the list (chilled beams, etc) which 5% of participants had experienced a supply shortfall.

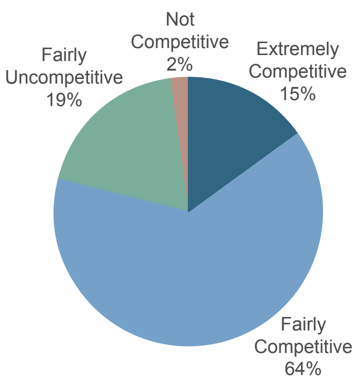
## COMPETITIVENESS – RAMPING UP

Competition among General Contractors continues to heat up, with 79% reporting Fairly to Extremely Competitive conditions – up 9% during the past 6 months.

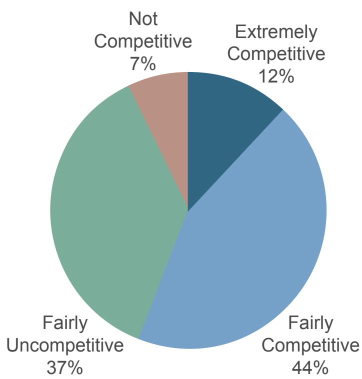
Sub Contractors also became more competitive across the period, with 56% reporting their situation as Fairly to Extremely Competitive (up 8% on last survey).

Sub Contractors experiencing uncompetitive conditions declined 2% to reach 7%, while just 2% of General Contractors are experiencing Uncompetitive conditions (down 6%).

### Are General Contractors competitive?

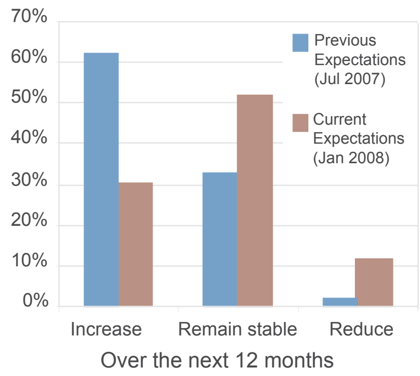



### Are Sub Contractors competitive?



## THE NEXT 12 MONTHS . . .

Construction industry work will . . .




The rose coloured glasses are definitely off.

Expectations of falling workload quadrupled during the past 6 months to reach 12% – the highest since the commencement of Davis Langdon's Sentiment Report.

The likelihood of workload remaining stable became stronger, with 53% of respondents expecting their workloads to remain relatively stable over the next 12 months (up 20%).

However those respondents expecting workload to increase over the next 12 months fell dramatically to just 33% (down 50%).

We asked participants what their reasoning was for these expectations. 41% attributed their sentiments to the following three factors: forward workload, level of enquiry and work in progress. The credit squeeze has also served as a major primary indicator to dampen market expectations (13%), while Government factors buoyed sentiment for 18% of participants.

*The Civil and Resource sector is most likely to contribute to growth...*

The Civil and Resource sector is back in the spotlight as the segment considered most likely to contribute to growth in the construction industry over the next 12 months. No surprises here, given the magnitude of Government spending and the magnitude of the resources boom.

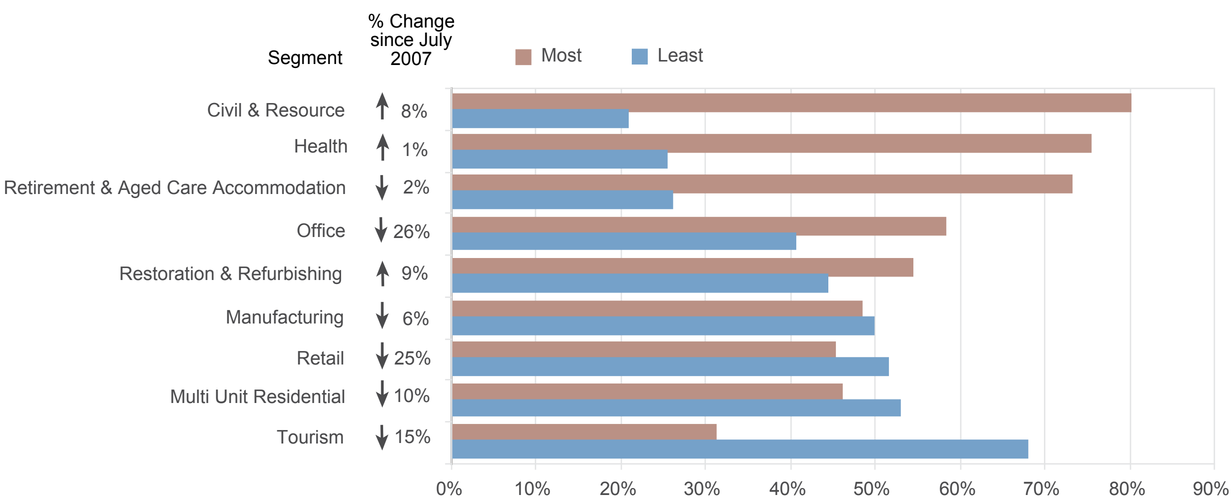
Health and Retirement & Aged Care are both vying for second place. 74% and 73% of respondents (respectively) considering these sectors will be major contributors to industry growth over the upcoming 12 months.

The Office segment slipped several notches to become fourth most likely to contribute to construction growth (down from number one in the last survey).

We're not surprised to see sentiment toward Retail slipping further down the list given recent interest rate hikes and consumer sentiment falls. Likewise, Multi Unit Residential took a tumble – slipping back 10% despite starting to show slight signs of encouragement last survey.

Expectations for Tourism related construction have plummeted a further 15% to reach the bottom of the rung, with 68% of industry players now considering it least likely to contribute to growth in the industry.

Which of the following segments do you think will contribute to growth in the construction industry in the next 12 months . . .



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