DAVIS LANGDON

CONSTRUCTION SENTIMENT
The Davis Langdon Sentiment Monitor

Findings Report Four | November 2007

EXECUTIVE SUMMARY

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

The past two years have seen this report measure movements in construction industry sentiment and identify confidence, outlook and emerging issues for the industry.

Our thanks go out to the wide cross section of industry participants who generously contribute their feedback in our twice yearly surveys.

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

- Skills Shortage worsens
- Election claws its way up construction industry's hottest issues
- Significant increases in the level of new business - up 9%
- Industry workload is set to increase over the next 12 months
- Multi Unit Residential appears to have at last turned the corner
- Office segment is unanimously considered most likely to contribute to growth

THE HOT ISSUES

The Election has overtaken Construction Costs to become the second hottest issue in the industry.

For the fourth consecutive quarter, the Skills Shortage remains the hottest issue in the industry.

Despite easing slightly since January, 51% of respondents still consider it as the hottest issue; 14% higher than 12 months ago.

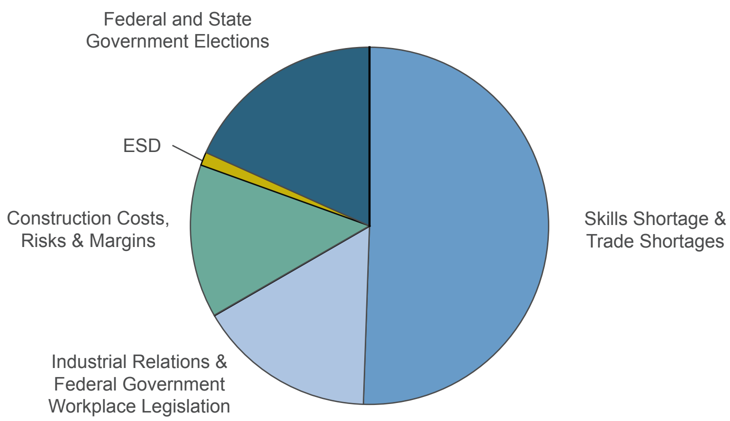
The impact of the ensuing Federal Government Election has overtaken Construction Costs, Risks and Margins to become the second hottest issue in the industry at the moment (18%). Industry participants have indicated their concern about the consequences a change in government might make – particularly the knock-on effect it may mean for Industrial Relations and AWA uncertainty.

Industrial Relations rose 9.5% during the past 6 months, now with 16% of respondents considering it in the top three hottest issues our industry faces at the moment.

Sentiment toward Construction Costs, Risks and Margins eased slightly during the past 6 months, down 3.8% to account for 14%.

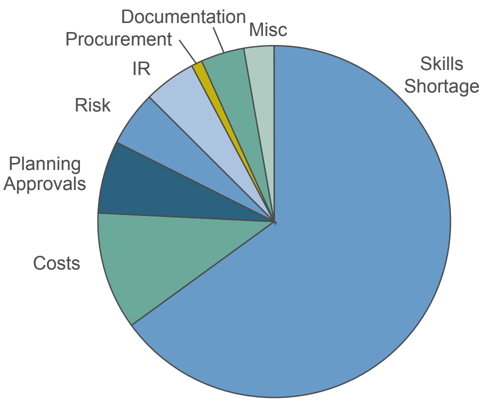
Compliance Issues also dropped off the hot list, as did Documentation.

The hottest issues in the industry at the moment



PROBLEMS IN THE INDUSTRY

Participants have voiced concern about the cascading of contractual risk.



98% of participants now believe there are problems in the industry at the moment; up 10% on last survey.

The Skills Shortage worsened significantly in the eyes of participants, with 65% now viewing this as the greatest problem in the industry, worsening 14% since January.

Now shaping up as a permanent fixture on the industry landscape, we wonder if the Federal Government's $2.1 billion pledge to ease the skills crisis could make a dent in the problem. Given the long lead time for training and apprenticeships, along with current unemployment rates of 4.3%, we expect this topic to be on the industry radar for some years to come.

Costs are now perceived as the second greatest problem in the industry, ramping up by 6% across the past 6 months and overtaking Planning Approvals, which moved to third place.

For the first time since the commencement of this survey, Risk was isolated as a problem in the industry. Participants have voiced their concern about the cascading of contractual risk, believing that risk is being unreasonably transferred to other parties via contracts.

Respondents also highlighted early warning signs that the industry will be exposed to greater net risk moving forward, as an increasing volume of work is undertaken by inexperienced people as a consequence of the skills shortage.

NEW BUSINESS

52% reported 'significant' increases in new business...

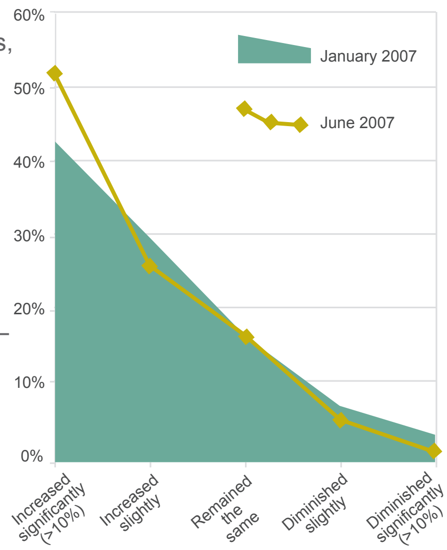
Just when we thought the level of new business had peaked, a record 52% of respondents reported that they experienced 'significant' increases in new business during the past 6 months, up 9% on January figures.

With no signs of slowing, 79% of respondents reported that new business to their firm had increased in some way, up 6% on last survey.

17% of participants reported the level of new business they were experiencing remained the same – unchanged from last survey.

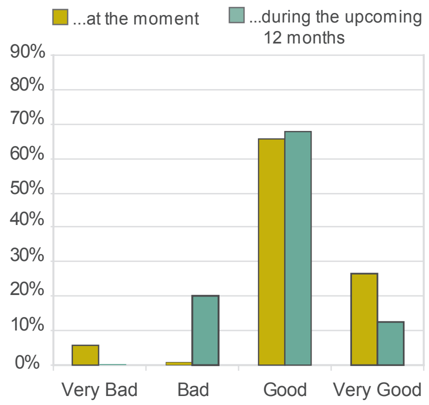
Just 5% of the industry said that their level of new business had diminished slightly.

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 has been adversely impacted by the November federal election.

While 93% of participants regard industrial relations as Good to Very Good at the moment, expectations for the next 12 months are less optimistic. 80% of participants are expecting Good to Very Good industrial relations looking ahead, while 20% foresee bad industrial relations (up 19%).

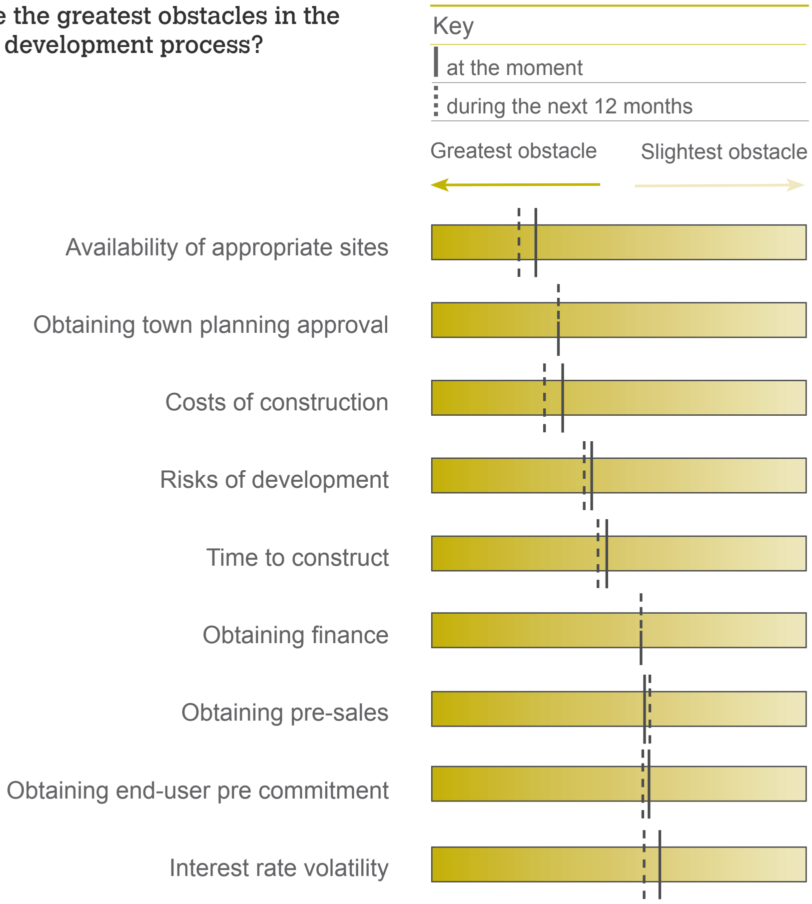
However, the Davis Langdon Sentiment Monitor has learned from past experience that Sentiment toward industrial relations can be seriously impacted by fear of the unknown.

Our second Findings Report in November 2006 revealed concerns about the (then) newly implemented workplace relations laws. However, despite negative sentiment brewing at that time, the state of industrial relations did not dampen, but conversely, improved.

GREATEST OBSTACLES IN BUILDING DEVELOPMENT

Nationally, the Availability of Appropriate Sites has become the greatest obstacle in development at the moment. Sentiment worsened by almost 30% during the past year and participants expect the situation to worsen further over the next 12 months.

What are the greatest obstacles in the building development process?



Obtaining Town Planning Approval, previously the top obstacle in building development, eased slightly to become the second greatest obstacle, contrary to expectations. Participants have indicated they expect this situation will remain stable over the upcoming 12 months.

Despite the Costs of Construction easing subtly since last survey (now the third greatest obstacle), pessimistic sentiment pervades and participants expect costs to worsen significantly during the next 12 months.

Construction timeframes became a greater obstacle since last survey, worsening by 10% since January and 20% on the previous year's sentiment.

Obtaining pre-sales remains unchanged on last survey, posing a relatively benign obstacle to development, as is Obtaining end user pre-commitment.

Interest rate volatility continues to pose the least concern to development according to our survey participants, however there is general consensus that this will worsen during the upcoming 12 months.

DESIGN AND CONSTRUCTION STANDARDS

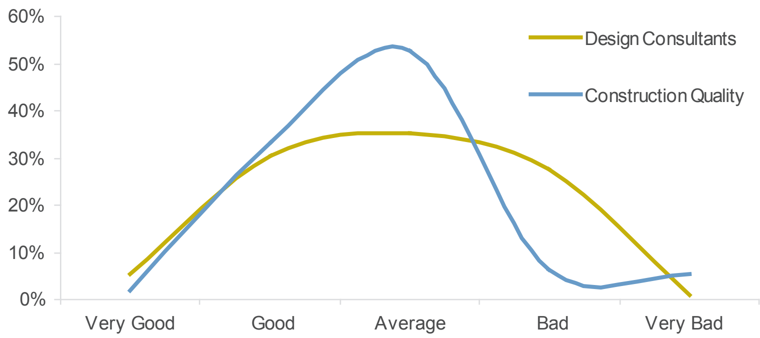
We asked participants how they rate the standard of Design Consultants and Construction Quality, based on their recent experiences.

In a dismal sign for the industry, the standard of Construction Quality was rated as Very Good by just 2% of respondents, while Design Consultants fared slightly better at 6%.

The standard of Design Consultants received a fairly even spread of responses, with the remaining participants split evenly across Good, Average and Bad experiences.

Over half of the respondents reported that the standard of Construction Quality they experienced was Average, 12% reporting Bad to Very Bad. 33% reported Good Construction Quality.

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



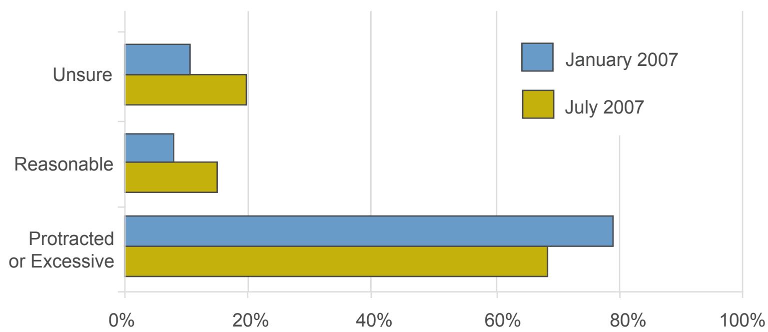
PLANNING APPROVAL – FOR BETTER AND WORSE

Respondents reporting excessive or protracted delays fell 15%.

In line with Town Planning Approval slipping to the second greatest obstacle in building development, we recorded a 6% increase in the number of respondents experiencing reasonable timeframes for Planning Approval. Likewise, the number of respondents reporting excessive or protracted delays fell 15% on January figures, to reach 64% – the lowest since the commencement of the survey.

But it's not all good news. Of those continuing to experience protracted or excessive delays, the timeframe for the delays worsened significantly. 81% reported timeframes that were protracted by 30% or more, while 39% were exposed to planning approval timeframes that were protracted by greater than 50%.

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



GREEN OBJECTIVES

99% of participants now consider green objectives are an issue.

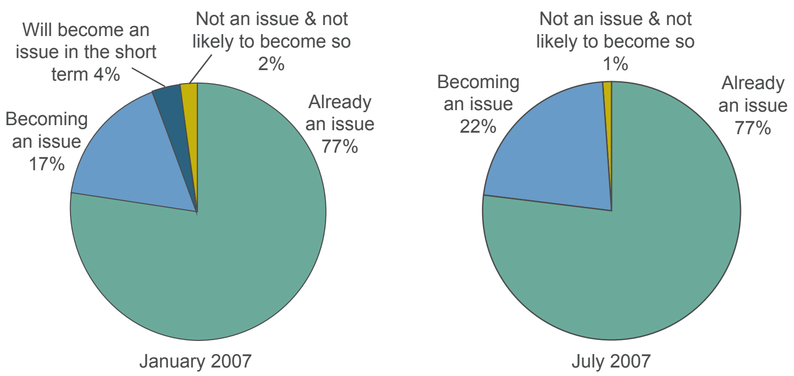
The results of the Davis Langdon Construction Sentiment Survey continue to signal that green objectives are an issue.

99% of participants now consider that green objectives are Already an issue or Becoming an issue, (up 3% since the survey first began in January 2006). Just 1% of respondents do not view green objectives as an issue.

Tenant demand is the main driver pushing green objectives at the moment, with many participants also believing that changes to the BCA requirements (Section J) have acted as one of the greatest drivers.

Interestingly, anxiety about the cost of green seems to be slipping off the radar.

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



GOVERNMENT PROJECTS

Exposure to government projects has crept up 15% since January – now involving 78% of the industry. State Government work still outweighs Federal Government workload, but the gap is narrowing. 54% of the industry has involvement in State Government work, while Federal Government accounts for 46%.

We asked participants “What Government factors do you think are affecting the industry?” Government expenditure topped the list, particularly in relation to infrastructure and capital works spend, followed by industrial relations.

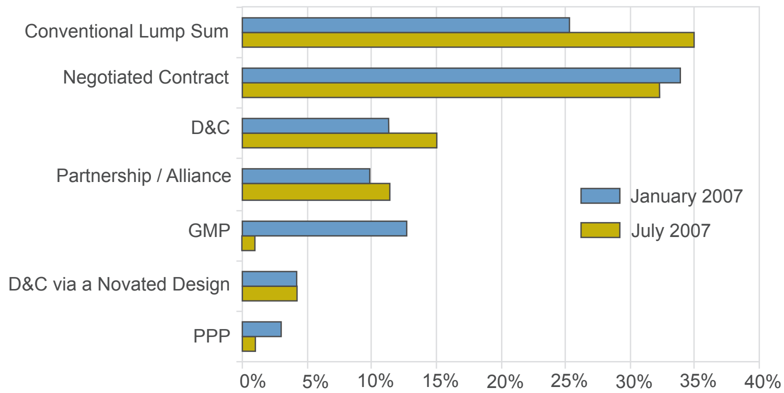
PROCUREMENT PREFERENCES – CERTAINTY IS THE NEW BLACK

Preference for conventional lump sum contracts continues to increase, rising a further 10% since last survey and now the most preferred procurement method by 35% of respondents.

Running a very close second, industry participants are still tending strongly toward negotiated contracts, with 32% of the industry indicating a preference for them; reflecting minimal change in sentiment since January (easing by just 1%).

Sentiment toward PPPs fell further, reaching just 1% – still the industry's least preferred method.

What is your preferred method of procurement?



STAFFING EXPECTATIONS – BLOOD FROM A STONE

79% of participants expect their levels of permanent staffing to increase...

Forget coming to terms with skills shortage.

During the next 6 months 79% of participants expect their levels of permanent staffing to increase from current levels. Of these 59% are expecting their levels of permanent staffing to increase by 5–20%. The past 6 months recorded permanent staff increases of 5–20% by half of all respondents, and some level of increase by 75%. Just 14% indicated there had been no change in staffing levels.

The last 6 months recorded a relatively stable Contract staffing situation, with 34% remaining at the same levels as January, while 31% increased by less than 5%. The next 6 months however instil a little more expectation with 61% anticipating their contract staff to increase by up to 10%.

SKILLS SHORTAGES – NO HOPE IN SIGHT

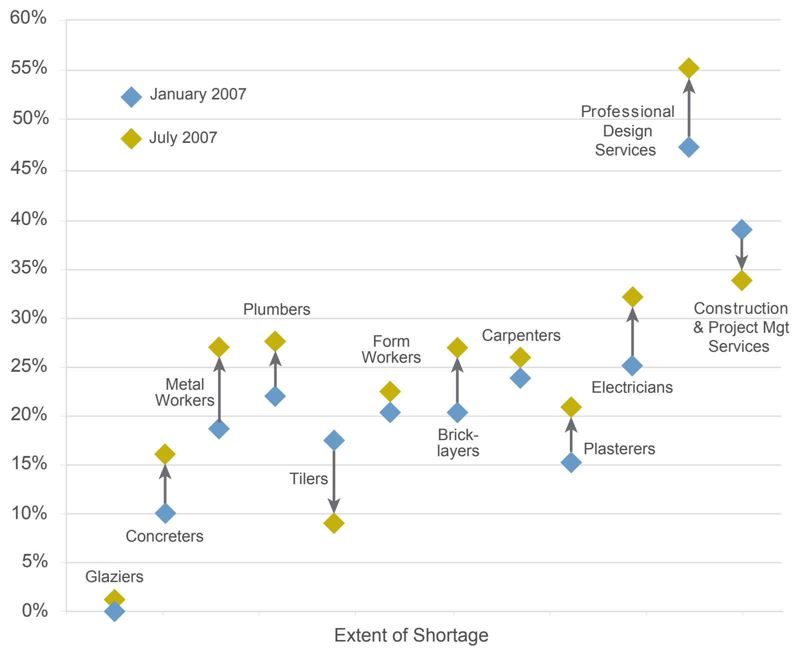
Professional Design Services climbed higher on top of the Skills Shortage heap, up 8% on January figures, now impacting on 55% of all respondents.

Construction & Project Management Services remains in second place, despite easing by 5% since last survey. Now at 34%, this is the lowest since the commencement of the survey.

The most difficult to obtain trades now include Metal Workers, Plumbers, Bricklayers, Carpenters and Electricians , with shortages now being experienced by more than 25% of all participants.

Demand for Tilers was the only trade shortage which recorded any degree of easing – down 8%.

Skilled trades shortages – which areas are worst affected?



SKILLS SHORTAGES – MAJOR CAUSES

An unprecedented super cycle

Some interesting perspectives have emerged about the causes behind the skills shortage.

One survey participant eloquently summed it up as "*an unprecedented super cycle which has thrown all historical training and planning guidelines out the window*".

This is a significant shift from 12 months ago, where participants largely blamed the government for failing to plan ahead.

The major causes behind the shortage of trades and skilled labour remain unchanged with the combined lack of training and high levels of demand topping the list.

However, the presence of a two-tiered shortage (split between trades and professions) points to a much larger problem. The overseas migration of professional staff (Architectural, Project Management, Engineering) to lucrative overseas positions in other booming international cities is exponentially increasing the problem to a more global level.

Increasingly stringent OHS laws were also earmarked as a disincentive. The possibility of supervisors facing criminal charges if someone is injured on a job site was highlighted as an unreasonable risk to take – just for 'doing your job'. Simply put, it's easier to make a living doing other things.

COST EXPECTATIONS

Overall, Cost Movements for the upcoming 12 months are anticipated to peak between 5–8% according to industry participants. Over the past 12 months, the majority of participants experienced Cost Movements of less than 5%.

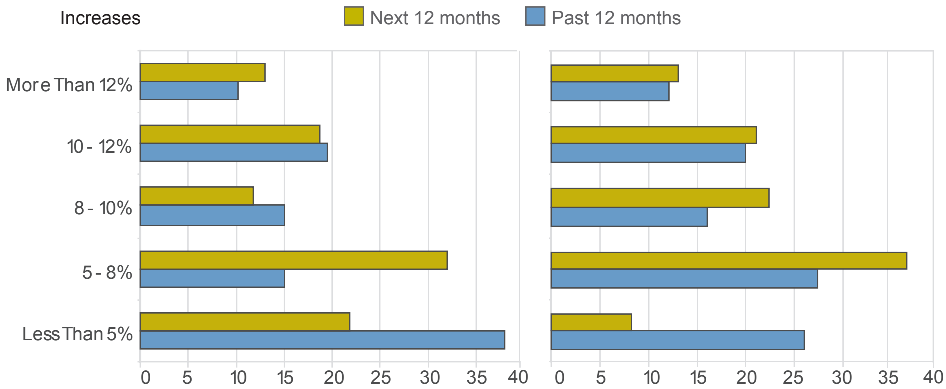
Notwithstanding, the duplicity of Cost Movements within the Australian market at the moment has been exposed in this question, with almost 20% of respondents reporting cost movements of 10–12% and more than a third expecting movements of 10% or higher over the next 12 months.

Market Price Movements (movement in tender prices) are widely anticipated to track at between 5–8%, during the upcoming year.

These expectations tracked very closely to our Davis Langdon Tender Indices which recorded median annual cost increases of 5.4% nationally across the past 12 months. We forecast increases in the vicinity of 6% across the upcoming year.

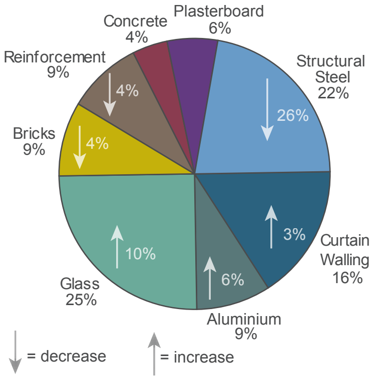
What is your view of . . .

general cost movements? **market cost movements?**



MATERIALS SHORTAGES

Building materials in short supply



Building materials shortages have crept up by 1% since January, with 40% of industry participants now reporting short supply of one or more materials.

Glass shortages are now impacting 25% of the industry (up 15%) and 16% of respondents experienced Curtain Walling shortages (up 3%).

Structural Steel shortages eased substantially from January's 48% peak, to a more manageable 22% – nevertheless, still ranking Steel as the second worst affected material in the industry.

Of lesser concern were Plasterboard, Reinforcement, Bricks, Aluminium and Concrete which, while still making an appearance as materials in short supply, all recorded at sub 10%.

COMPETITIVENESS AMONGST CONTRACTORS

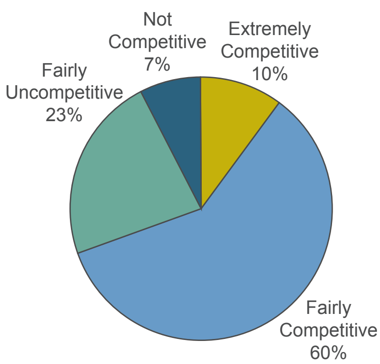
General Contractors reported increasingly competitive conditions, with 70% now reporting their situation as Fairly to Extremely Competitive – up 3% on last survey.

Conversely, Sub Contractors became less competitive across the period, with just 47% reporting their situation as Fairly to Extremely Competitive (down 5% on January figures).

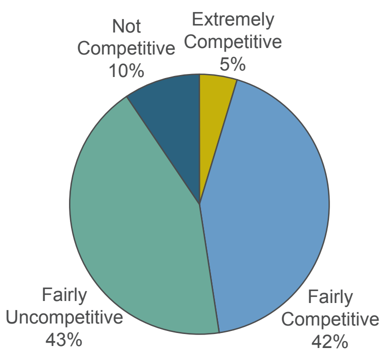
Sub Contractors experiencing Uncompetitive Conditions crept up 5%, now accounting for 53% of Sub Contractors.

As Sub Contractors shift into a less competitive state, we forecast potential problems for Head Contractors, as Head Contractors are forced to contract with less competitive Sub Contractors.

Are General Contractors competitive?

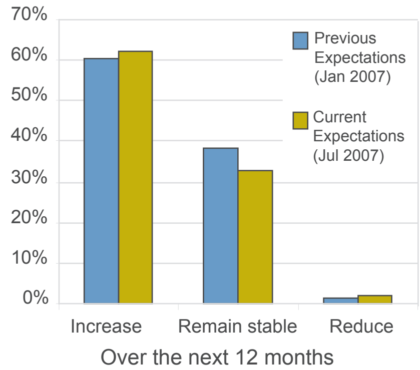


Are Sub Contractors competitive?



THE NEXT 12 MONTHS . . .

Construction industry work will . . .



There is a widely held expectation that there is more work ahead.

62% of industry players believe workload for the construction industry will increase over the next 12 months, up 2% on last survey and now at its highest since the commencement of Davis Langdon's Sentiment Reports.

The likelihood of workload remaining stable has now declined to just 33%.

The optimistic outlook for the year ahead has been attributed primarily to continued government expenditure and the amount of forward workload. Also fuelling the fire is the level of enquiry being experienced on top of existing work in progress.

Multi Unit Residential appears to have at last turned the corner.

The Office segment is unanimously considered most likely to contribute to growth in the construction industry over the next 12 months.

We're not surprised to see sentiment toward Health and Retirement & Aged Care continue at very high levels, given the magnitude of government spending. Still in the top three, 70–75% of respondents consider they will be major contributors to industry growth over the upcoming 12 months.

The Civil and Resource sector dropped several notches (from number one last survey) to now become fourth most likely.

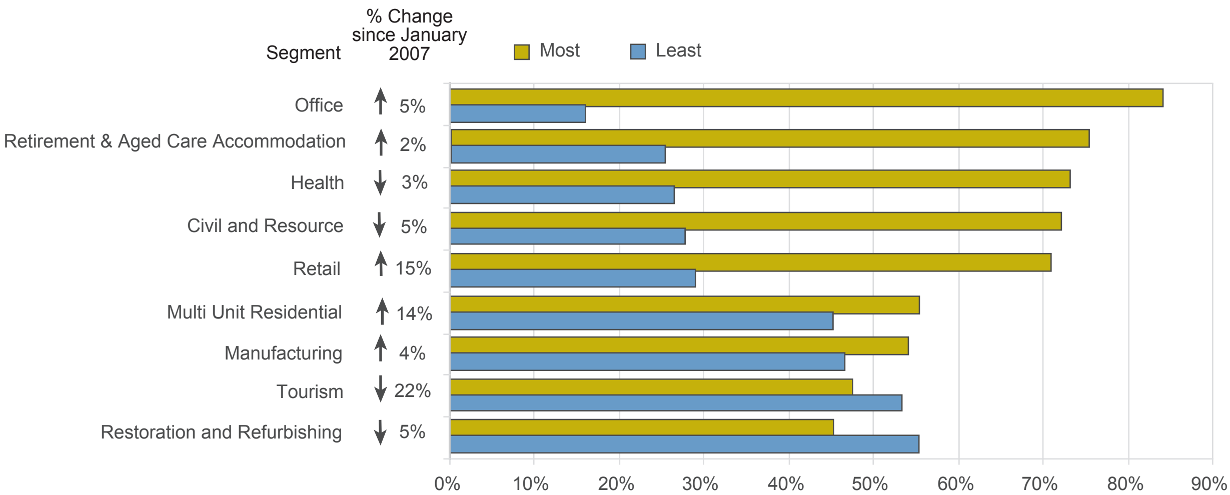
Retail is maintaining sustained positive sentiment, with consumer spending keeping the sector buoyant and in high demand. 71% of participants now anticipate it will contribute most to construction growth in the next year.

Multi Unit Residential appears to have at last turned the corner, up 14% on last survey.

In an interesting shift, 55% now believe it will contribute to growth (it was previously bottom of the rung) which may be a by-product of rental growth showing slight signs of encouragement.

Tourism related construction plummeted 22%, now with 53% of industry players 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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