Turner & Townsend

Australia and New Zealand market insight report

Q4 2020

making the **difference**

Australia market overview

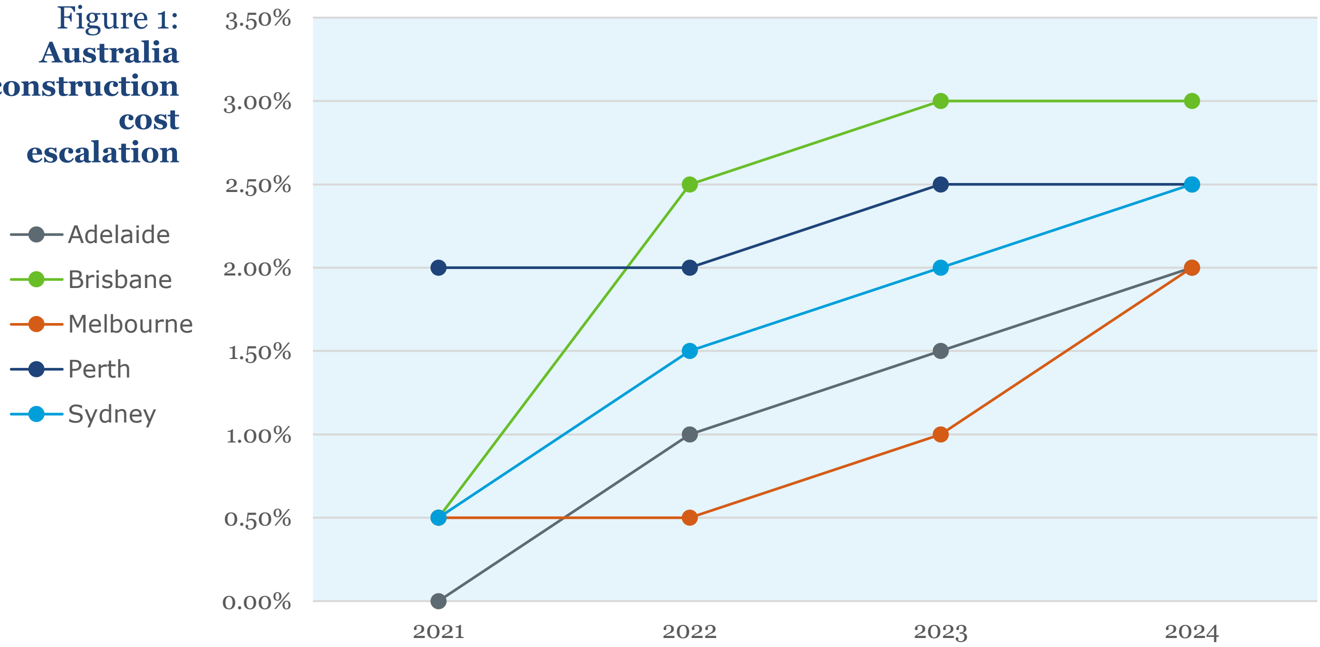
In the last quarter of 2020, there was a distinct improvement in sentiment across construction markets in Australia. As restrictions continued to ease from the relatively low COVID-19 case numbers, consumer and business confidence strengthened and economic activity gained momentum.

Over 2020, the public sector did most of the heavy lifting in terms of construction expenditure. Many private sector projects were placed on hold to avoid risking downtime, while some were cancelled altogether due to the uncertainty brought on by the pandemic. While a number of these private sector projects remain on hold across Australia, many have now resumed, in line with the economic recovery gaining momentum.

While many of these projects are now progressing, 2021 is anticipated to have a decline in overall construction activity in the non-residential sector. Private sector investment was scaled back significantly over 2020 and this will lead to a smaller pipeline of activity in 2021. Leading this decline will be offices, accommodation, and retail projects. Public sector activity is expected to remain strong over 2021, dominated by a significant pipeline of education and health projects.

In H2 2021, a recovery in private sector investment is forecast to begin, in line with improving economic conditions. Fiscal and monetary policy is expected to support construction activity, while private investment remains subdued.

Figure 1: Australia construction cost escalation



New Zealand market overview

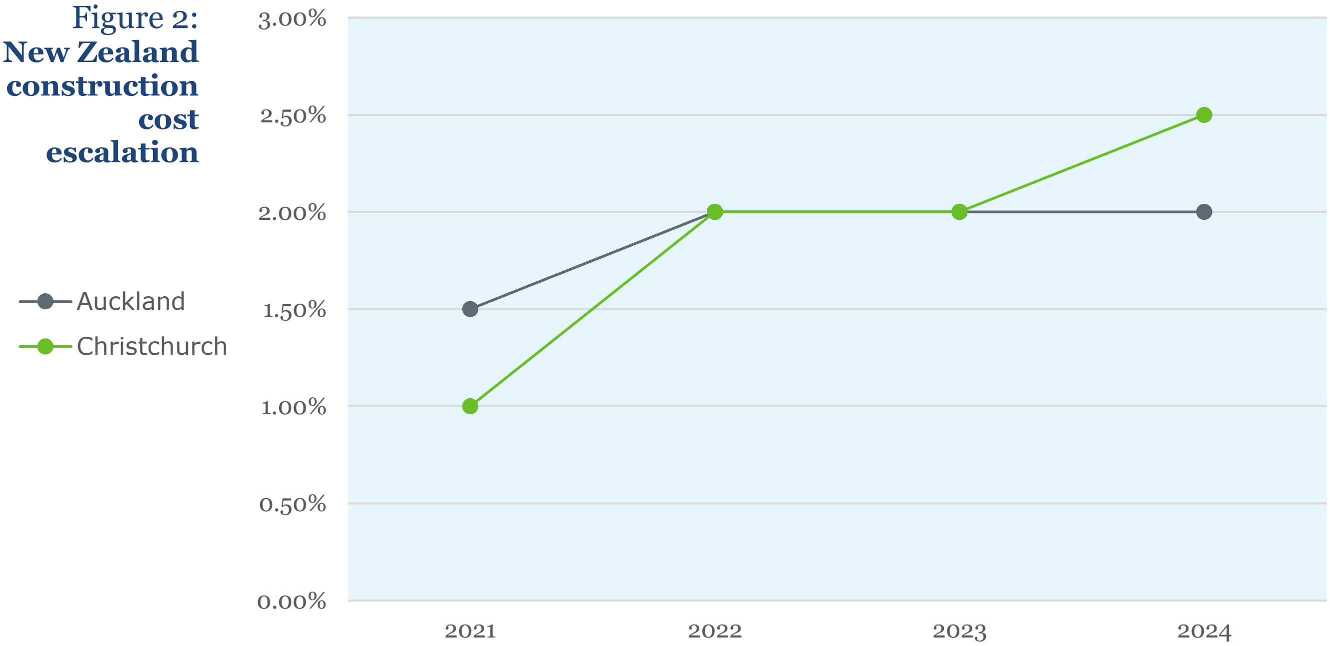
The impact caused by COVID-19 on New Zealand's construction industry was significant, however, there are now signs that a recovery is underway.

In response to the downturn, the New Zealand Government announced plans to fund large shovel-ready infrastructure projects to boost economic activity and provide much needed support to the industry. This saw the formation of the Infrastructure Industry Reference Group (IIRG) to identify public and private infrastructure projects which can start immediately or within the next six months. As of July 2020, the government had approved 150 major projects across 40 sectors. Over the December quarter, several of these projects came through the pipeline and are slowly starting to fill voids left in the market from the downturn.

While public and private sector construction activity is increasing, there is still anticipated to be a significant decline in activity over 2021, from a reduction in private investment last year. Tendering conditions remain extremely competitive, as businesses look to secure future pipelines of work. Margins and preliminary costs are being trimmed to allow for this lower pricing.

While lower tenders are on offer, many contractors are facing challenges with increased costs in their procurement. New Zealand's construction industry continues to experience ongoing market capacity challenges. Skills and material shortages are one of the biggest issues faced by contractors, which is resulting in volatility in costs. This is presenting a serious issue for contractors who are already reducing their costs to secure work, while incurring higher costs for materials and labour. These challenges are likely to continue in 2021 while the recovery takes place.

Figure 2: **New Zealand construction cost escalation**



New South Wales

Key price indicators

Movement (%) Q4 2019 to Q4 2020

3%	0%	4%	0%	-30%
Site foreman /hr	Group 1 tradesman	Concrete 30 MPa/m^3	Plasterboard 13mm thick to stud wall/m^2	Main contractors margin movement

Confidence appears to be returning to the market with contractors and consultants reporting an uptick in enquiries over the period. This is expected to continue to strengthen over 2021, in line with private investment increasing.

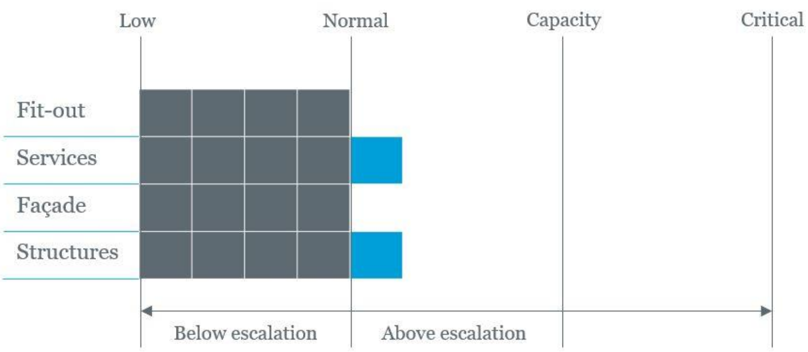
Government projects continued to dominate the activity in the market in Q4 2020, with the roll out of funding on social infrastructure projects such as schools and hospitals. Most consultants and contractors have now shifted their focus to these types of projects in the absence of new private sector work. While there has been a noticeable reduction in the number of private sector projects in the pipeline, there are several major private sector projects underway, including the towers at Barangaroo and Circular Quay.

Tenders continue to be very competitive as contractors look to secure their pipeline of work, however, it is expected that this has now bottomed out, with further reductions in margin unlikely. We anticipate the competition will remain in the market for the next 6 – 12 months while the cycle for non-residential construction bottoms out. Office vacancy rates across Sydney have almost doubled over the last 12 months to over 8 percent, as a result of a decrease in demand and an increase in supply coming to the market. This has returned Sydney CBD office vacancy rates back in line with the long-term average. There is still a great deal of uncertainty on what the future workplace will look like and how this will play out in the long term.

Contractors have adapted well to the evolving COVID-19 situation and now have additional procedures in place for supply chain management and site safety. Should another outbreak occur, the majority of contractors feel they will be in a good position to uphold productivity and avoid delays.

Construction costs for non-residential projects declined by 1.5 percent in the 12 months to December (ABS). With the non-residential cycle anticipated to bottom out over 2021, construction cost escalation is unlikely. From 2022 onwards, private sector investment is forecast to recover, which is expected to see an increase in projects underway and will subsequently push up construction costs as the market tightens.

Figure 3: Supply chain capacity in New South Wales Q4 2020



Queensland

Key price indicators
Movement (%)
Q4 2019 to Q4 2020

-8.3%	4.7%	0%	-2%	-33%
Site foreman / hr	Group 1 tradesman	Concrete 30 MPa/m³	Plasterboard 13mm thick to stud wall/m²	Main contractors margin movement

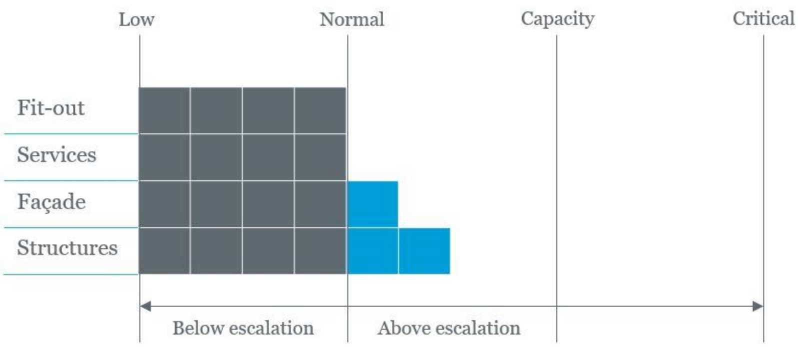
New private sector investment requires much needed stimulus which would benefit from Government support as the incumbent Labour Party serves another term. However, despite the lack of stimulus, Queensland had an already robust pre-existing pipeline of major projects committed for the state. Projects include Queen’s Wharf, 360 Queen Street office tower, Caboolture Hospital redevelopment, and the Logan Hospital redevelopment.

Major transport infrastructure projects which have been earmarked for some time such as Cross River Rail, Brisbane Metro and the Inland Rail (Queensland sections) continue to progress, however, the budget in December made no announcements for any other significant infrastructure spend. Overall, non-residential activity in Brisbane is forecast to decline over 2021, due to the lack of private sector investment in 2020. However, work forecasts indicate that an increase in activity will occur from 2022 onwards.

Tender enquiries have started to increase, particularly in the health and education sectors. Commercial office development and office fit-out sectors remain relatively subdued, as landlords and tenants assess the impacts of working from home and reduced demand.

Non-residential construction in Queensland has seen very little cost escalation over the past couple of years, due to fairly weak activity levels. In the 12 months to December 2020, construction costs for non-residential projects increased by 0.5 percent and we expect a similar level of escalation to occur over 2021.

Figure 4: **Supply chain capacity in Queensland Q4 2020**



South Australia

Key price indicators Movement (%) Q4 2019 to Q4 2020				
5.9%	1.8%	-4.0%	20.00%	0%
Site foreman / hr	Group 1 tradesman	Concrete 30 MPa/m^3	Plasterboard 13mm thick to stud wall/m^2	Main Contractors Margin movement

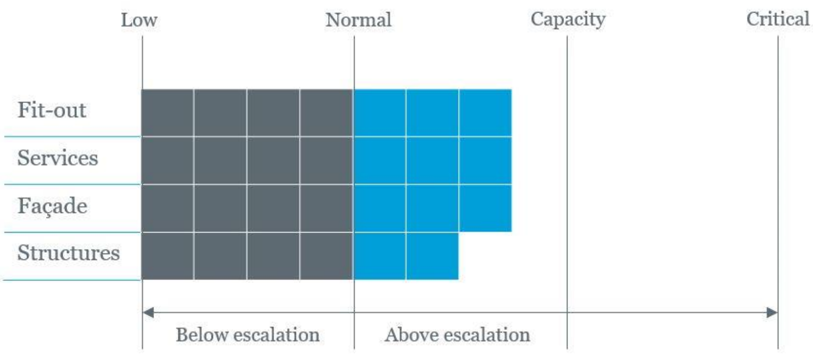
The State Government continues to support the industry with its expansive school building programs. The 'Building Better Schools' program is in its third quarter with most projects committed and in construction phase, and a handful of smaller schools to be tendered in the next six months. Currently under construction are the three super schools ($350m), as well as the $100m Yatala Labour Prison upgrade and several defence projects.

Overall, non-residential activity for South Australia has not yet reached the trough in the cycle. A decline in activity is forecast for 2021 and 2022, before activity starts to strengthen. The significant investment into defence projects is preventing overall non-residential activity from falling further. Projects include the Air7000 and Air555 at RAAF Edinburgh and the next stage of the Osborne Ship Building Precinct.

Tendering conditions are forecast to hold steady over the next quarter. Major projects out for tender include the Queen Elizabeth Hospital upgrade, SAMHRI 2 and the upgrade of the Fullarton Road/Glen Osmond Road intersection. Private sector developers are still cautious following the COVID-19 downturn and we expect investment will remain subdued over 2021, while there is still uncertainty.

While non-residential activity is forecast to remain subdued, civil infrastructure and residential construction are forecast to see significant growth over the next two years. Given the relatively small size of the South Australian construction market, it's likely that we will see some construction workers transition over to these sectors where there is an increase in work opportunities. This may result in some low-level cost escalation over the outlook period, as the market tightens.

Figure 5: Supply chain capacity in South Australia Q4 2020



Victoria

Key price indicators
Movement (%)
Q4 2019 to Q4 2020

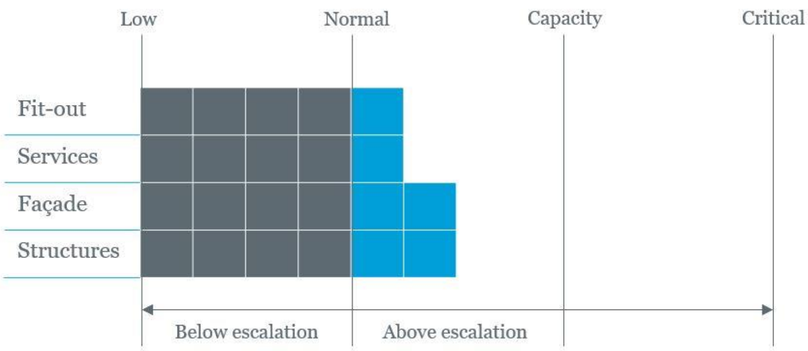
4.3%	4.4%	3%	7%	-25%
Site foreman / hr	Group 1 tradesman	Concrete 30 MPa/m^3	Plasterboard 13mm thick to stud wall/m^2	Main contractors margin movement

Following the second wave of COVID-19 in Melbourne, construction expenditure has been subdued. Confidence has not yet returned to the market and this is evident in the limited number of private sector projects out for tender. While private sector activity remains weak, there are a number of major social infrastructure projects in the pipeline across the health and education sectors. This includes the $1bn Footscray Hospital, the $400m Victorian Heart Hospital, and the $350m Ballarat Base Hospital redevelopment.

Overall, non-residential construction activity is forecast to decline over 2021, due to the lack of private sector activity to come through the pipeline. There are several major civil infrastructure projects under construction and due to commence, which will help to keep the construction sector buoyed over the next 12 months. Additionally, Melbourne is expected to have a significant increase in housing construction, following the federal and state policy, to support the residential housing sector.

Overall, tendering conditions remain competitive in Melbourne. The lack of private sector projects out for tender is resulting in many contractors turning their focus to public sector projects. A marked increase in private sector investment is not forecast to take place during 2021. Private sector investment is expected to start recovering from the end of 2021 and into 2022.

Figure 6: **Supply chain capacity in Victoria Q4 2020**



Western Australia

Key price indicators

Movement (%) Q4 2019 to Q4 2020

2.8%	2.9%	1.7%	7.3%	11%
Site foreman / hr	Group 1 tradesman	Concrete 30 MPa/m^3	Plasterboard 13mm thick to stud wall/m^2	Main contractors margin movement

The Western Australian economy and construction market appears to have now recovered following a period of uncertainty.

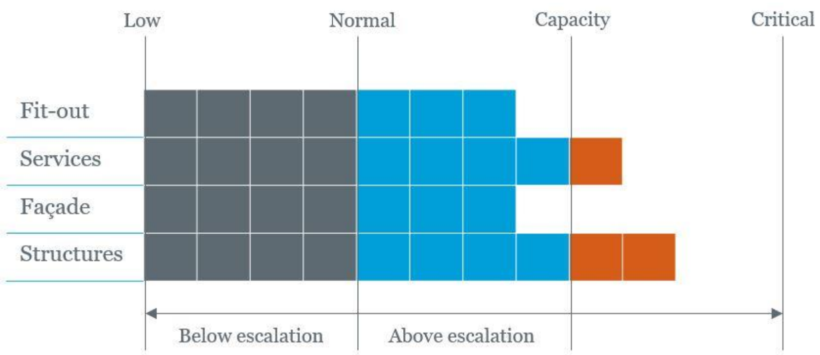
The impact of the governments accelerated multisector stimulus drive will likely see tender prices increase due to the limited availability of skilled labour and materials in Western Australia. We have tracked various rail infrastructure projects commencing procurement or starting onsite in parallel which will directly impact competitive tension in the market. We are also seeing significant cost increases in civil construction, steelwork, concrete and reinforcement due to the unavailability of skilled labour related to these trades.

This supply and demand impact will be exacerbated by a restriction in overseas skilled labour entering Western Australia, which will likely result in a lack of competition in labour rates and in turn will drive a price spike over the next quarter.

Other contributing factors relate to the migration of skilled trades and materials being consumed by the residential sector boom because of the government incentivisation schemes released in response to the pandemic.

Other real estate sectors such as education and food retail have demonstrated strong growth through a mixture of government investment and capital funds being invested to future proof for the new way of operations in terms of consumer convenience.

Figure 7: **Supply chain capacity in Western Australia Q4 2020**



New Zealand

Key price indicators
Movement (%) Q4 2019 to Q4 2020

5.6%	6.2%	8.3%	9.1%	20%
Site foreman / hr	Group 1 tradesman	Concrete 30 MPa/m^3	Plasterboard 13mm thick to stud wall/m^2	Main contractors margin movement

A successful general election for the Labour Party in October 2020 has provided an element of stability to the Auckland and Christchurch markets. With all areas of New Zealand remaining at Alert Level 1 since 7 October 2020, the market saw strong levels of activity leading up to the December holiday break.

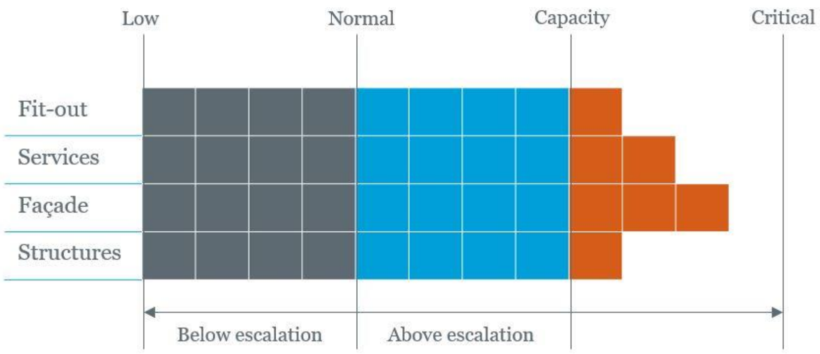
Large public spend is likely to continue across social infrastructure projects such as schools, hospitals and housing, in addition to the shovel ready projects announced during 2020. There is the potential for slower growth in the commercial and retail sectors as clients re-assess future plans and ways of working. Both markets are yet to see the return of large projects in sectors such as aviation which were strongly impacted during 2020.

The outlook for the high-tech sector in Auckland is likely to remain strong, with continued investments anticipated from international companies, in particular data centre developments.

In relation to the day-to-day risks posed by COVID-19, the construction industry across New Zealand is now prepared to react quickly and safely to any new lockdowns and has well established protocols for the various alert levels, which will enable a swift transition to revised ways of working where necessary, minimising impacts on productivity. However, the continued international border closure will put pressure on the supply chain for both labour and materials, with the façade trade now under critical pressure.

Auckland and Christchurch construction markets continue to experience significant resource shortages in both labour and materials. Construction cost inflation continues to outpace tender price inflation, and this is one of the largest concerns contractors are currently facing.

Figure 8: **Supply chain capacity in Auckland and Christchurch Q4 2020**



Australia economic overview

Australia's Gross Domestic Product (GDP) rebounded by 3.3 percent over the quarter, indicating economic recovery is underway.

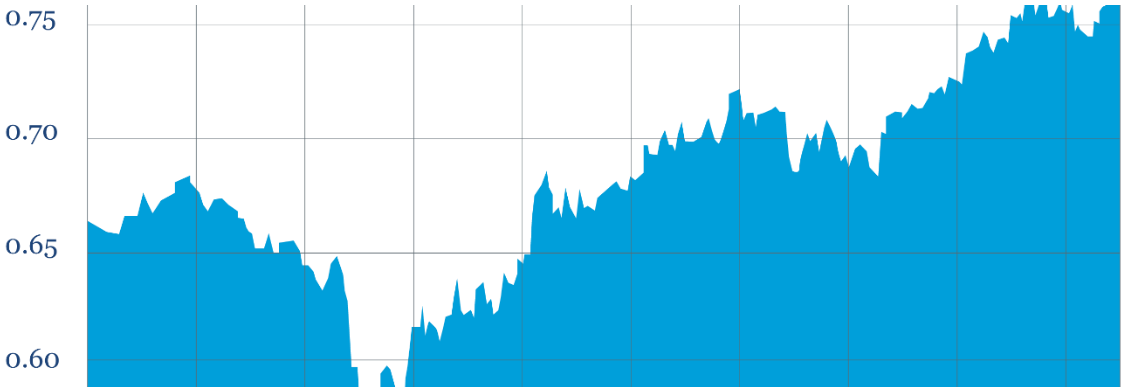
Restrictions have continued to ease around the country, which has driven an increase in economic activity. Additionally, the government's significant fiscal response to the pandemic has continued to support and speed up this recovery.

Over the December quarter, community transmission of COVID-19 remained low with only small outbreaks occurring. Additionally, Australia's virus case numbers continue to remain significantly lower than other developed economies, which is helping to increase confidence in the domestic economy. Retail sales continue to record much higher turnover than in 2019, with retail turnover up 9.6 percent in December, compared with the same period the previous year. Evidently, consumers are choosing to spend their money on goods, while services remain limited by COVID-19 restrictions and international travel is off the table. The labour market has continued to improve, with unemployment easing down to 6.6 percent in December.

Consumer and business confidence have improved, with an increase from 93.8 in September to 112 points in December, while business confidence turned positive for the first time since the start of the pandemic, increasing from -4 in September to 4 in December. Supporting this improvement is the conclusion of the Melbourne lockdown, which is expected to have boosted economic growth in the quarter.

While this economic situation is improving, the outlook for 2021 indicates a mixed recovery. Strong household spending, the rollout of the COVID-19 vaccine, and a recovery in private sector business investment are all expected to support the recovery of the economy over the year. However, some risks cloud the short-term outlook. Australian exports are likely to see a decline over 2021 in response to increasing trade tensions between China and Australia and overall weaker global demand. Additionally, tourism related services and universities are also expected to face ongoing challenges in 2021, while international borders remain closed.

Figure 9: AUD USD performance (Q4 2019 – Q4 2020)



Forex movement of +10% in 12 months

Figure 10: AUD FOREX forecasts

	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022
USD	0.77	0.77	0.76	0.77	0.76
GBP	0.56	0.56	0.56	0.56	0.55
EUR	0.64	0.64	0.63	0.63	0.63
YUAN	5.00	6.04	5.05	5.05	4.94

	Current	Previous
GDP quarterly growth rate	3.3% Jun 20 – Sep 20	-7.0% Mar 20 – Jun 20
GDP annual growth rate	-3.8% Sep 19 – Sep 20	-6.4% Jun 19 – Jun 20
Inflation (annual)	0.9% Dec 20	0.7% Sep 20
Unemployment rate	6.6% Dec 20	6.9% Sep 20
Business confidence index	5 Dec 20	-4 Sep 20
Retail sales	9.6% Dec 19 – Dec 20	5.6% Sep 19 – Sep 20
Interest rate	0.10% Dec 20	0.25% Sep 20

New Zealand economic overview

New Zealand's Gross Domestic Product (GDP) rebounded by 14 percent over the quarter, the largest quarterly increase on record.

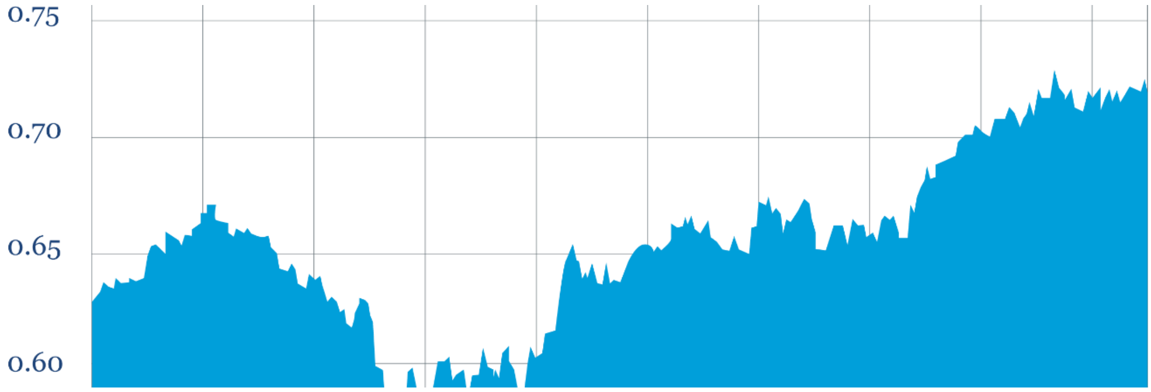
Driving this recovery was a sharp rebound in the services sector (+11.1 percent), retail trade and accommodation (+42.8 percent), wholesale trade (+19.2 percent), and transport, postal and warehousing (+16 percent). While this rebound has been significant, real GDP growth declined by 2.2 percent in the 12 months to September 2020, indicating that the strong growth was not enough to make up for the economic impact of COVID-19.

Household spending continues to be robust, with retail turnover increasing by 8.3 percent in September 2020, compared with the same period the previous year. Both consumer and business confidence are improving, in line with the country's successful handling of the virus. Business confidence increased from -6.9 points in September to 9.4 points in December, while consumer confidence increased from 95.1 points to 106 points. Unemployment fell from 5.3 percent in September to 4.9 percent in December, however, it remains higher than it's been since 2017.

While economic activity is strengthening, weak population growth from loss of migration continues to present a downside risk to the outlook. In November 2020 annual net migration was down 23 percent compared with the previous year and this will continue to remain subdued while borders are closed. Additionally, New Zealand's tourism sectors will continue to be negatively impacted while these restrictions are in place.

Overall, New Zealand's economy is better placed than most in terms of a swift recovery. The ongoing robust government fiscal and monetary policy is helping to generate economic activity and provide support for businesses and consumers. Additionally, the development of a travel bubble between Australia and New Zealand will help to strengthen the recovery even further by boosting hard-hit sectors such as tourism and hospitality.

Figure 11: NZD USD performance (Q4 2019 – Q4 2020)



Forex movement of +7.5% in 12 months

Figure 12: NZD FOREX forecasts

	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022
USD	0.71	0.71	0.71	0.70	0.70
GBP	0.52	0.51	0.51	0.52	0.52
EUR	0.59	0.59	0.58	0.58	0.58
YUAN	4.63	4.66	4.69	4.64	4.66

	Current	Previous
GDP quarterly growth rate	14% Jun 20 – Sep 20	-12.2% Mar 20 – Jun 20
GDP annual growth rate	+0.4% Sep 19 – Sep 20	-12.4% Jun 19 – Jun 20
Inflation	1.4% Dec 20	1.4% Sep 20
Unemployment rate	4.9% Dec 20	5.3% Sep 20
Business confidence index	9.4 Dec 20	-6.4 Sep 20
Retail sales	8.3% Dec 19 – Dec 20	-14.2% Sep 19 – Sep 20
Interest rate	0.25% Dec 20	0.25% Sep 20

Understanding the impact of COVID-19 on the commercial occupier sector

The commercial occupier sector has gone through an unimaginable change as a result of COVID-19, and the way we work has likely changed forever.

In Q4 2020, we undertook a market engagement survey with participation from our commercial occupier key clients across the globe to understand the impacts of COVID-19 on the sector. The findings, although mid-pandemic, are a sound indication of how different organisations are dealing with the pandemic in real time.

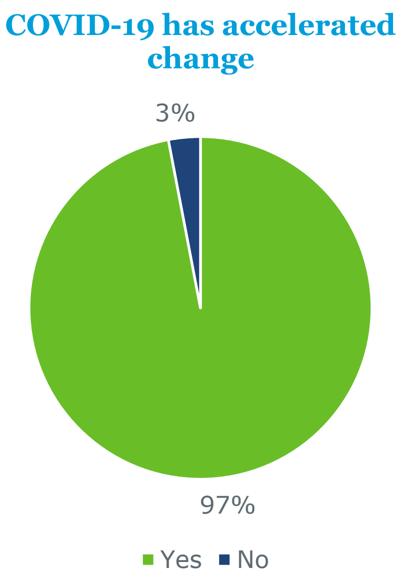
Key findings

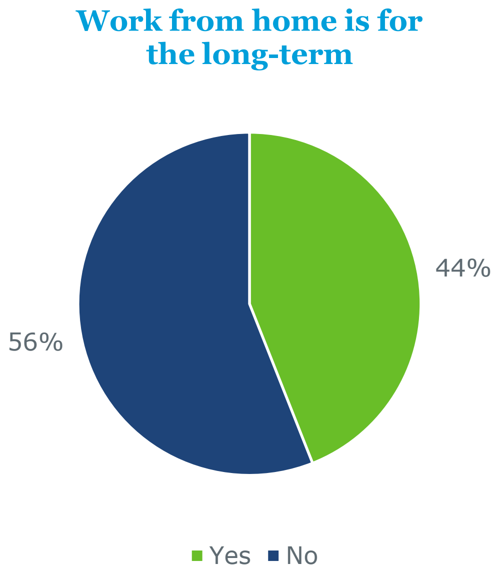
- 83 percent of respondents feel they have heard enough of the 'new normal' discussions.
- 97 percent of respondents feel COVID-19 has accelerated the pace of change in workplace in terms of flexible working and digital use.
- 44 percent of respondents feel we will revert to the old pre-COVID ways of working and 56 percent feel we will change for good.
- 56 percent of respondents are not as optimistic on the idea that home working is sustainable for the long term. The next generation of leaders need support and guidance, therefore this 'new normal' must ensure a healthy balance.

COVID-19 is a catalyst for change for how we work. Our pre-pandemic lives saw us working from the office five days a week, however working from home has now been proven to maintain and even improve productivity. There is however uncertainty on how we will emerge post-pandemic and what the workplace of the future will look like.

During this transition phase to the 'new normal' there have been multiple workplace strategies employed across real estate portfolios with varying degrees of success and take-up by employees.

The question whether we will revert to pre-pandemic ways of working following the implementation of the vaccine is one which divides our results. There are however several emerging trends such as increasing share ratios working from home, increased technology enablement in the workplace, increased collaboration spaces and employee wellbeing which will help to frame the future workplace strategy response.





Workplace strategy

Key findings

- 57 percent of respondents are waiting before proceeding with their strategies.
- 88 percent of respondents feel that the future of workplace will shift towards offices being used as collaboration/touch down space and less so as a 9-to-5 desking environment.
- 88 percent of respondents are already rethinking workplace strategies and developing future solutions.
- 70 percent of respondents are already implementing changes to the design and construction of workplaces for the future.

This is the first time our working population has experienced a global health pandemic and we are acutely aware of the health risks which are forcing us to reimagine the open-plan office space we have actively pursued over the last decade.

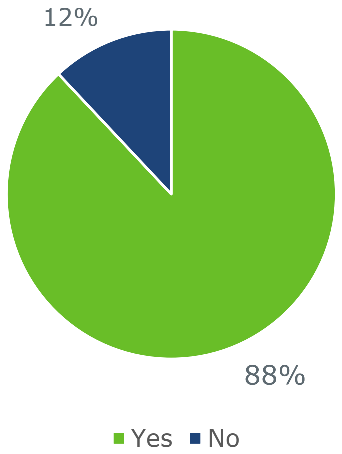
Interestingly, Australia and New Zealand have emerged from COVID-19 with almost zero community transmission and both workforces have largely returned to work and functioning in a post COVID-19 landscape.

Our survey results establish several emerging trends with 88 percent of respondents already rethinking workplace strategy and future solutions and 88 percent seeing the office as a collaboration touchpoint. These results contrast with our 'wait and see' question which has split the results.

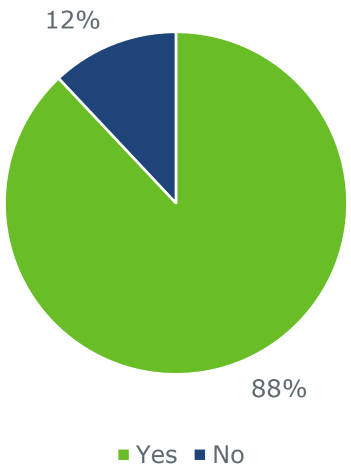
To frame a workplace strategy, we can look to the emerging trends from the data, which are as follows:

- Technology enabled spaces.
- Increase in collaboration spaces within the workplace.
- The home office as an extension of the workplace.
- Employees holistic wellbeing and implementing 'disease resilient workspaces'.

Shift to collaboration



Rethinking strategy and future solutions



Be prepared

We are living out the transition to the 'new normal' in real-time and every company and its requirements are different, there is not a one size fits all. However, one thing is certain, preparing your workplace strategy for the future requires robust planning and research. Whatever route you decide to take, ensure you partner with the appropriate advisors to remain on program and budget. Turner & Townsend is hosting a virtual roundtable in March 2021 to further discuss the impacts of COVID-19 on the workplace sector. To attend the roundtable please contact Francisco Smout at the details below.

About Turner & Townsend

We are an independent professional services company specialising in program management, project management, cost and commercial management and advisory across the real estate, infrastructure and natural resources sectors.

With 111 offices in 45 countries, we draw on our extensive global and industry experience to manage risk while maximising value and performance during the construction and operation of our clients' assets.

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