# BUILDING ACTIVITY

BUILDING CONSULTANCY DIVISION BULLETIN

A quarterly insight into construction related issues impacting the insurance industry

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# Q2 2022 - Building activity

## Executive summary

Building activity throughout Australia remains incredibly strong through the opening half of 2022 and is forecasted to continue much into 2023. This trend is spurred on by government investment in infrastructure projects, run off of the *HomeBuilder* program that ceased in early 2021, the spike of renovation building approvals in 2020/21 and the increase in demand of construction related materials/trades in responding to one of the largest Insurance events on record – SEQ and NSW Floods of 2022.

As the economy continues to recover from the Covid-19 pandemic, construction remains one of the core pillars to the nation's recovery. Whilst construction is always volatile through supply and demand challenges, the current Industry shortages are impacting everyone in the supply chain right through to consumers who are experiencing increasing costs and delays in delivery.

Insurance Council of Australia (ICA) has reported that approximately 36.30% of flood claims have been closed/settled which would typically account for the smaller or less complex matters, leaving the bulk or more complex matters yet to be delivered. We should therefore consider the supply and demand challenges in both materials and labor to continue to impact project delivery for the construction and Insurance industries alike.


**Figure 1:A** SEQ & NSW flood claim volume, Insurance Council of Australia, 2022

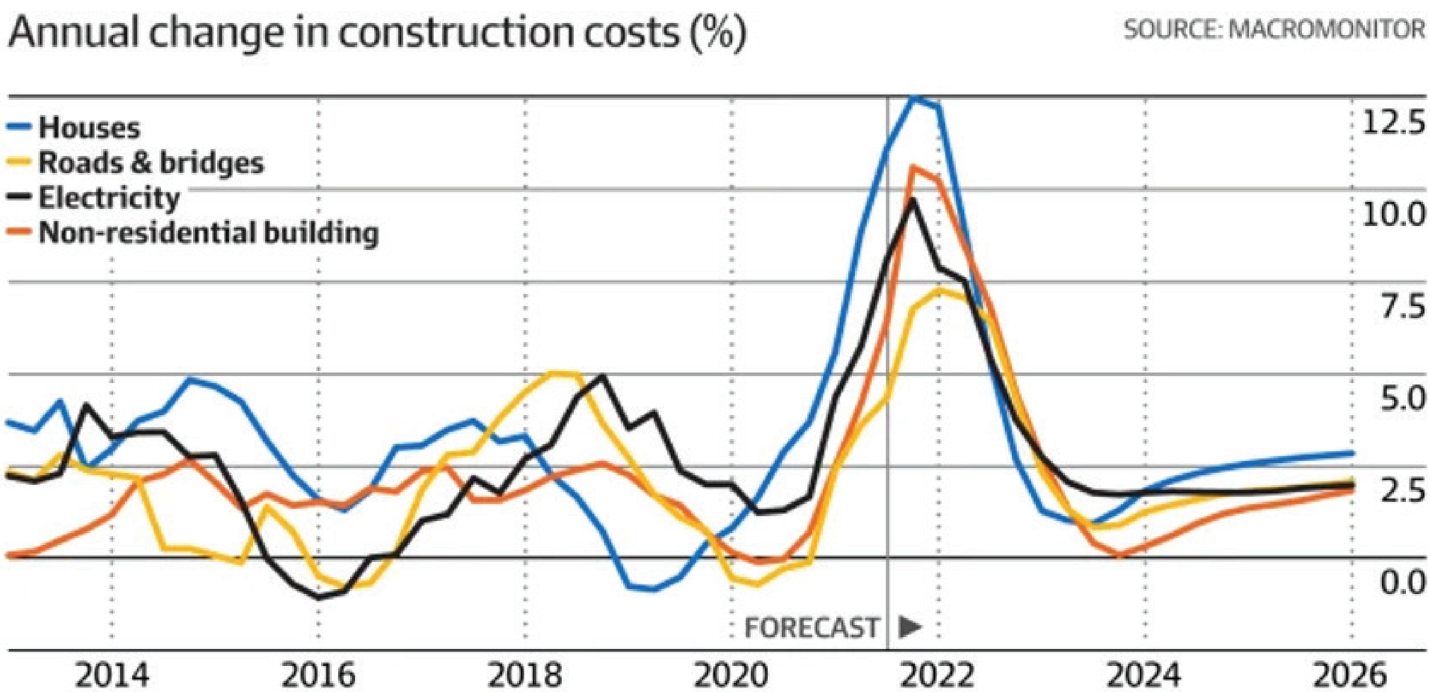



**Figure 1:B** (Source ABS) highlights the spike in both housing and infrastructure investments.

## Statistics on construction - (Source Australian Bureau of Statistics)

Over the past 12 months, input prices to house construction rose overall 15.4% due to timber, board and joinery (+20.6%) and other metal products (+16.2%).

**Figure 2:A** below highlights the increase in the cost of timber which, makes up a large portion of the structural element of a dwelling and often equates to more than 30% of the overall contract value. Board includes the wall and ceiling linings, whilst joinery includes, but not limited to, the largest prime cost fixture within the home being kitchen cabinetry.

Concrete supply pricing has increased incrementally throughout 2021/22, with most merchants posting quarterly increases ranging from 2-9%. Concrete products are typically used in domestic construction for footing/slab construction only. However, in commercial and civil projects concrete can make up >70% of the overall material volume.

With these three material categories of a project experiencing such volatility, we should expect construction costs to remain inflated until availability of materials and strain in supply chain logistics stabilise.

### Input prices to house construction recorded rises due to ongoing tight supply of materials and high freight costs

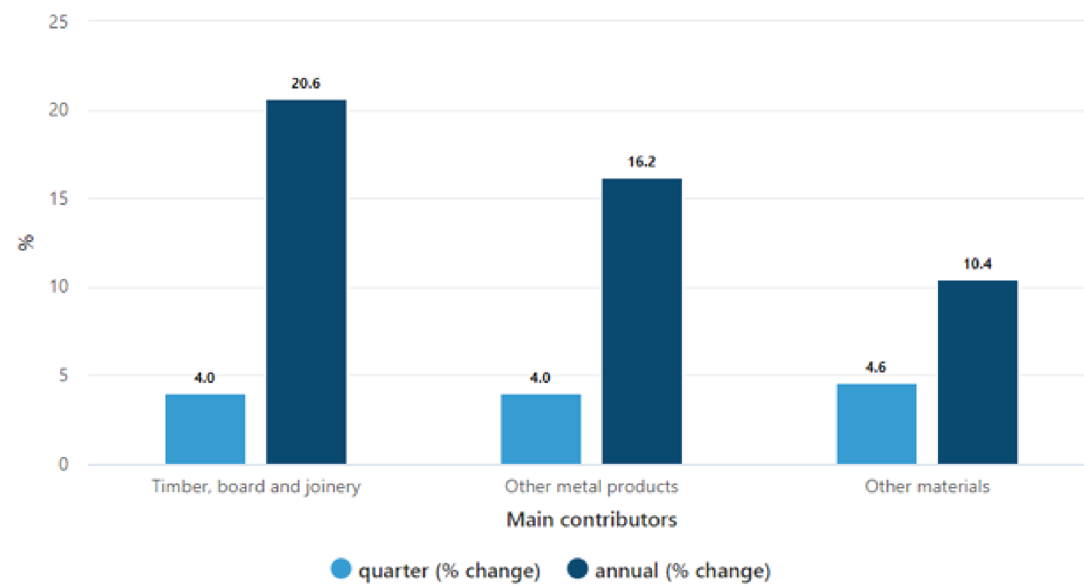
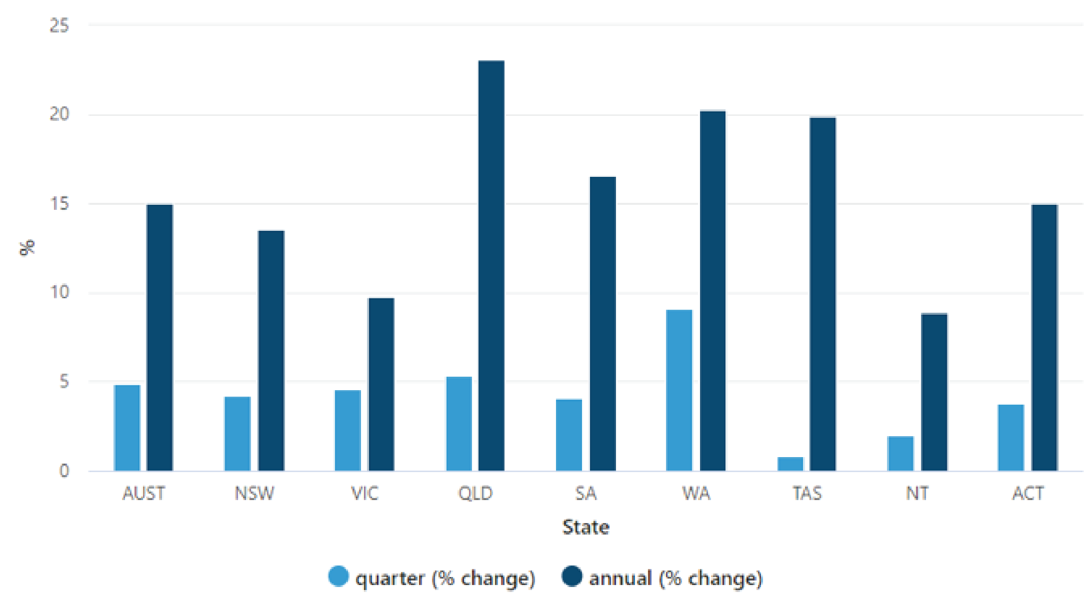



**Figure 2:A** (Source ABS)

## Statistics - by Regions

### House construction prices rose due to strong demand for trades and materials and builders reducing bonus offers




### Other residential building construction prices rose 1.8%

Other residential construction prices recorded increases for all states driven by price rises for materials and labour. Ongoing public and private investment across construction has tightened the supply of tradespeople and placed further pressure on costs. The ongoing disruptions to international freight has driven the increase in prices for materials.

Over the past twelve months Other residential building construction prices rose 7.1%.

**Figure 2:B** (source ABS)

Looking across state and territory regions, there are fluctuations in the drivers behind the inflated construction costs however, consistencies all the same. **Figure 3:A** highlights that construction inflation is a national trend and whilst the capital cities are an indicator, the industry is reporting that regional areas are facing supply challenges of their own and often more severe than capital cities due to their inability to match the demand in capital cities when purchasing bulk materials.

Capital city price movements (Territory prices are not sampled):

- Sydney (+3.6%), driven by Other materials (+6.0%).
- Melbourne (+4.6%), driven by Other metal products (+4.5%).
- Brisbane (+3.7%), driven by Other metal products (+4.9%).
- Adelaide (+3.5%), driven by Timber, board and joinery (+4.7%).
- Perth (+4.8%), driven by Ceramic products (+14.4%).
- Hobart (+4.2%), driven by Timber, board and joinery (+5.6%).

**Figure 3:A** (source ABS)

The industry has experienced a steady rise in construction related costs throughout the last decade typically aligned to inflation. However, the last 18 months has spiked significantly due to a range of influences from the covid-19 pandemic, government investment in construction, insurance events and more recently the war in Ukraine.

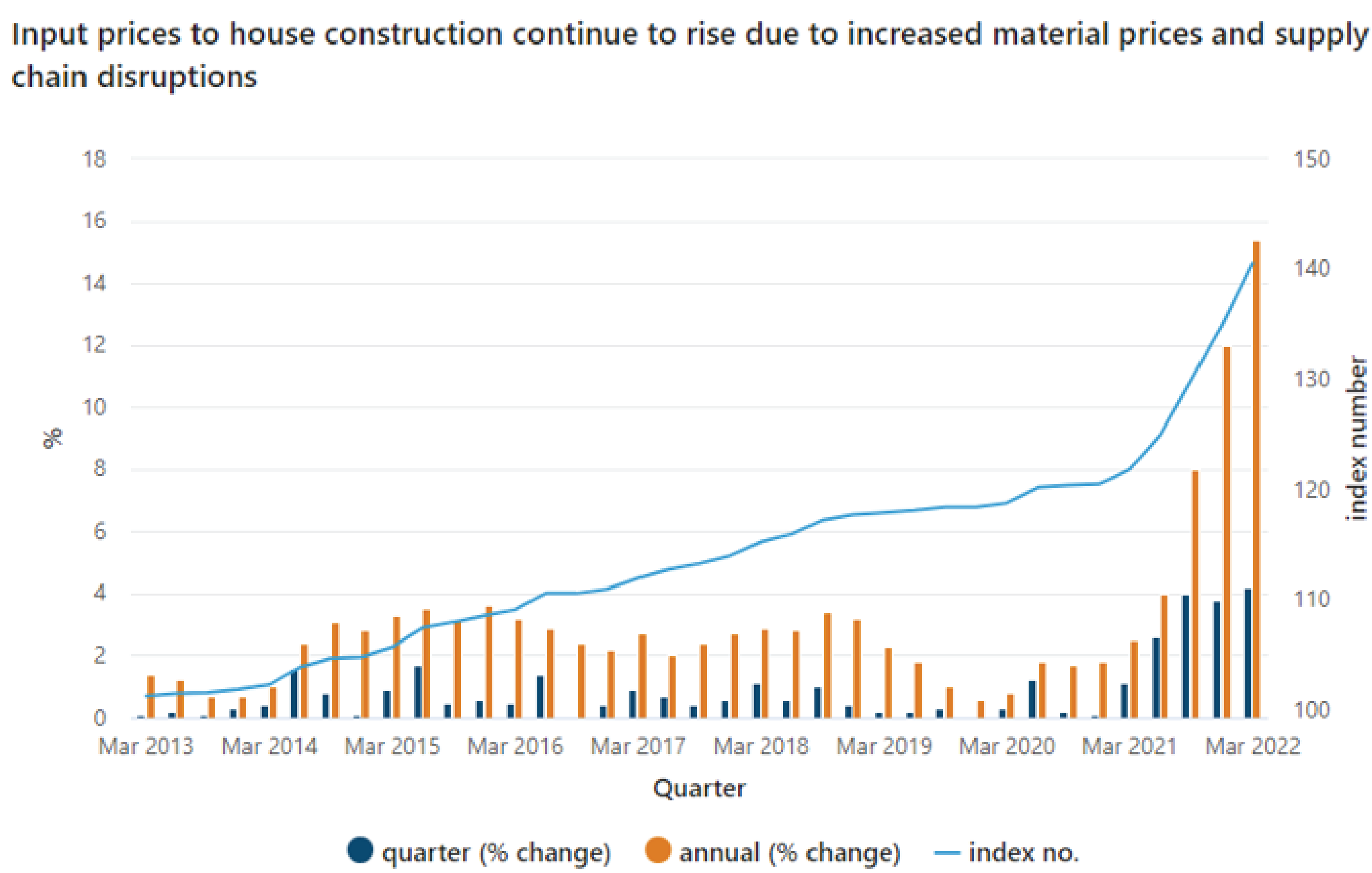



**Figure 4:A** (source ABS)

There is no portion of the construction industry that is immune to the trade and material supply challenges, it is widespread across all sectors of the domestic, commercial and infrastructure/civil markets. **Figure 4:B** demonstrates the strain the civil engineering construction projects are experiencing, albeit smaller percentage increments than the domestic markets, the value of the increases are phenomenal for an industry that typically operates at a lower profit margin than lower value markets.

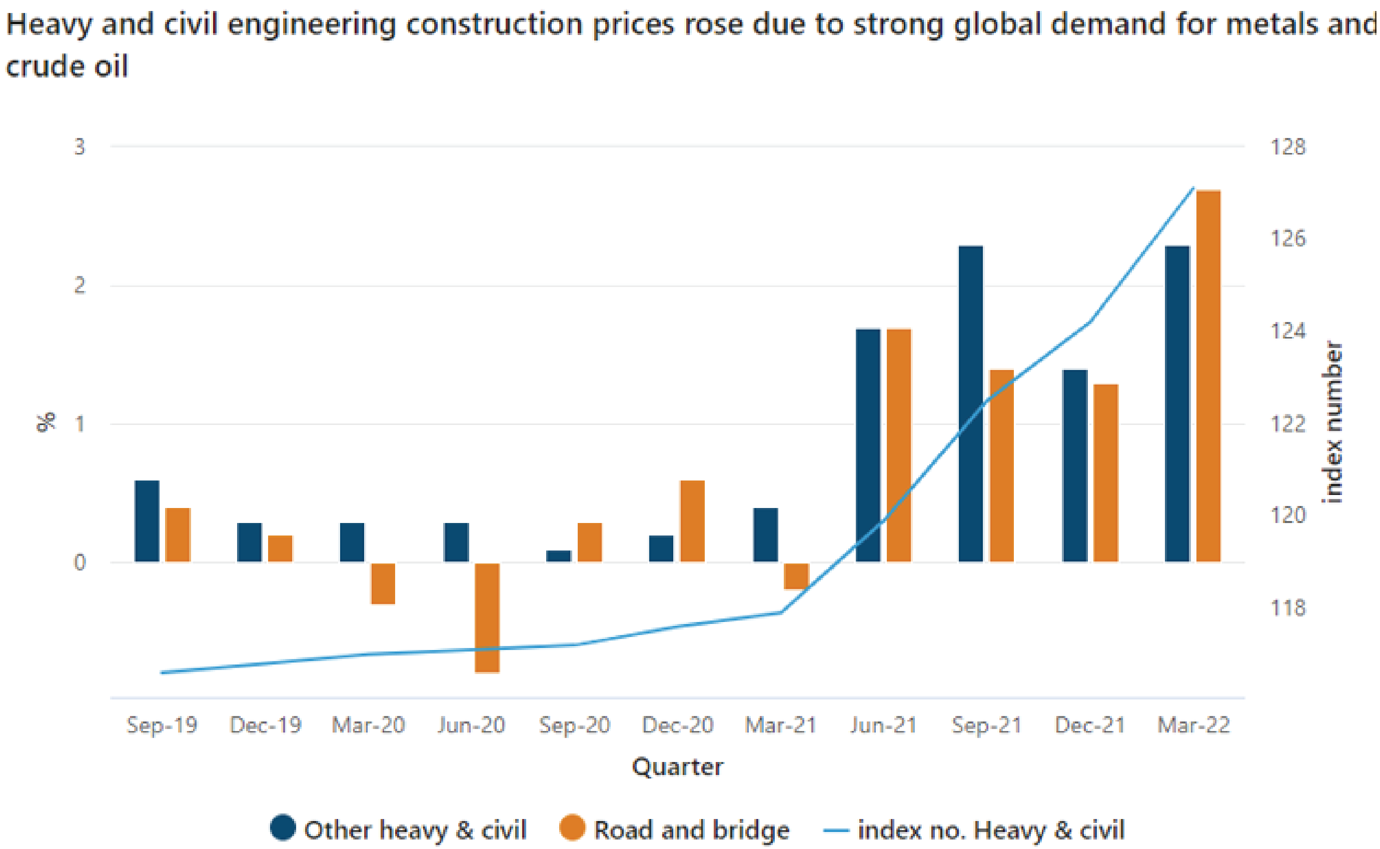



**Figure 4:B** (source ABS)

## Industry responding

The Construction Industry and state and federal governments remain active with this challenge. Coordinated discussions continue across industry and industry bodies such as Master Builders and the Housing Industry Association, whom are producing thought leadership papers to inform contractors and consumers alike. The peak regulators continue to produce fact sheets and other publications to inform the industry and best equip contractors and consumers to prepare and mitigate supply and cost challenges.

In Queensland specifically, the QBCC has introduced the *Accelerated Builder/Consumer Dispute Framework* to assist contracted parties resolve disputes impacted by construction industry labour and building material shortages.

Unfortunately, we continue to see building companies facing insolvency, including Privium, Probuild, Condev and, more recently, in Queensland - Pivotal Homes. We have witnessed Snowden Developments and Norris Constructions, a Hotondo franchise both go insolvent in Victoria and Tasmania. Insolvency of building companies is not a 2022 phenomenon. However, the rate at which they are falling indicates of the serious headwinds the building industry is currently facing.

Typically, when projects are abandoned, the contract values cannot be honoured by the second Builder appointed to finish the projects; whilst there are warranty products available from state governments, there is often a shortfall the consumers face with funding to complete their build. As the full weight of these insolvencies is felt further down the supply chain, we can expect to see additional contractors and sub-trades out of pocket and saddled with debt, creating even greater uncertainty and volatility in an already strained environment.

## Macro influences

Shipping costs continue to affect timber and steel pricing in addition to goods manufactured overseas such as ceramic tiles, plumbing and electrical fixtures and fittings. Public commentary shows that shipping costs have increased from USD$1,500 for a forty-foot container to a staggering USD$10,500. Similar figures are reported across the shipping industry. Yet it is important to note the values fluctuate depending on the departure and receiving ports and the shipping lanes utilised. Whilst accurate figures cannot be determined, it is apparent that increased costs and delays in getting goods to Australia are having a flow-on effect on consumers.

The Consumer Price Index (CPI) rose 1.8% through Quarter 2, whilst it rose 6.1% over the twelve (12) months to the June 2022 quarter. The most significant price rises were new dwelling purchases by owner-occupiers (+5.6%), Automotive fuel (+4.2%) and furniture (+7%) (source ABS).
The Reserve Bank of Australia increased the official cash rate by 50 basis points to 1.85% on 2 August 2022 (Q3). Inflation is now at its highest level since the early 1990's.RBA attributes global factors and local domestic factors, including the strong demand, a tight labour market currently -3.5% unemployment rate and capacity constraints, but also specifically calls out the impact the 2022 floods are having.

The war in Ukraine is not helping matters either. Although we are on the other side of the planet, the increased oil, gas and fuel charges will ultimately affect the cost of transporting goods and services. Australia has lost a major supply of aluminum, which will negatively impact on material shortages. Additionally, approximately 40% of Australia's Engineered Wood Products (EWP) is sourced from Russia or Belarus of which trade is difficult/suspended due to the ongoing war and sanctions imposed.

## Construction Cost indices – (CCI)

- Across the industry, the construction cost indices is produced by several reliable sources. On average various CCI sources are showing an average rise in prices of approx. 9% since the start of covid and 5% since the start of the year.
- Although some trades have seen significant increase, other trades have remained competitive lowering the overall average.

| Time | BRIS | SYD | MEL |
|---|---|---|---|
| 2020 - Start of Covid | 0% | 0% | 0% |
| June 2021 | 4% | 6% | 2% |
| June 2022 | 5% | 3% | 4% |

## Industry feedback

Burnout is the word on the street these days with professionals, trades and everyone in between exhausted and feeling stressed. Various builders have reached their capacity and are booked out till the end of the year resulting in longer wait times and increased costs.

With the significant inflation over the last two years, underinsurance of residential and commercial buildings will become a major concern and warrants calculated consideration.

We are also seeing a large disconnect in replacement cost values from brokers and insureds to establish sums insured on agricultural buildings. Structure needs to be insured on a "like for like" basis with similar materials and not on a cost-effective replacement option. Essentially, a timber shed cannot be insured on the value of a modern steel shed which can be a 1/3 of the price.

Non-Insurance builders who have merged into the Insurance market due to demand are charging significant costs for standard restoration and drying works and referring to it as 'high-risk' work.

Trades in short supply;

Carpentry gangs, specifically structural carpentry gangs are in short supply, however flood affected properties usually mostly required fit off and finishing trades which is manageable at present.

Cabinetry and Joinery manufactures are in high demand and expect to pay a premium on kitchens and custom flouts.

Block and Bricklayer are still at premium and in short supply.

### What is a PROVISIONAL SUM (PS) ALLOWANCE?

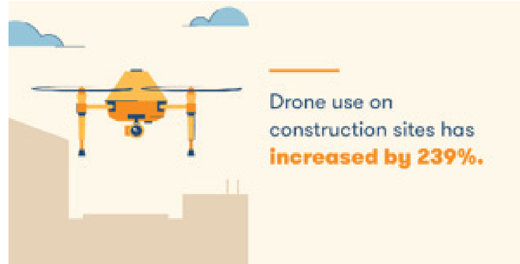
A Provisional Sum is a monetary allowance for works that will be carried out, however cannot be quantified accurately at the time of pricing the works or executing the contract.

A PS must be nominated and referenced in the contract, however, should include all attributable costs in the sum such as- materials, labour costs, sub-contractor costs, delivery, site handling and supervision relevant to that PS activity.

The PS nominated must be accurate within reasonability and on completion of the contract, the PS allowances must be quantified and validated. This often results in a variation or credit under the terms of the contract.

A PS is an effective method of managing rising supply and trade costs under a building contract.

## FUN FACT





Did you know there are an estimated 6 million rivets in the Sydney Harbour Bridge – all of which were installed manually....Imagine the labour cost in 2022!

## Helpful links

https://www.qbcc.qld.gov.au/sites/default/files/2021-09/policy-accelerated-builder-consumer-dispute-framework.pdf

https://www.mbqld.com.au/__data/assets/pdf_file/0019/210682/MBQ-Statement-Material-and-Trade-shortages-June.pdf

https://www.mbqld.com.au/__data/assets/pdf_file/0023/190760/MB_HotTopic_March2021.pdf sedgwick

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