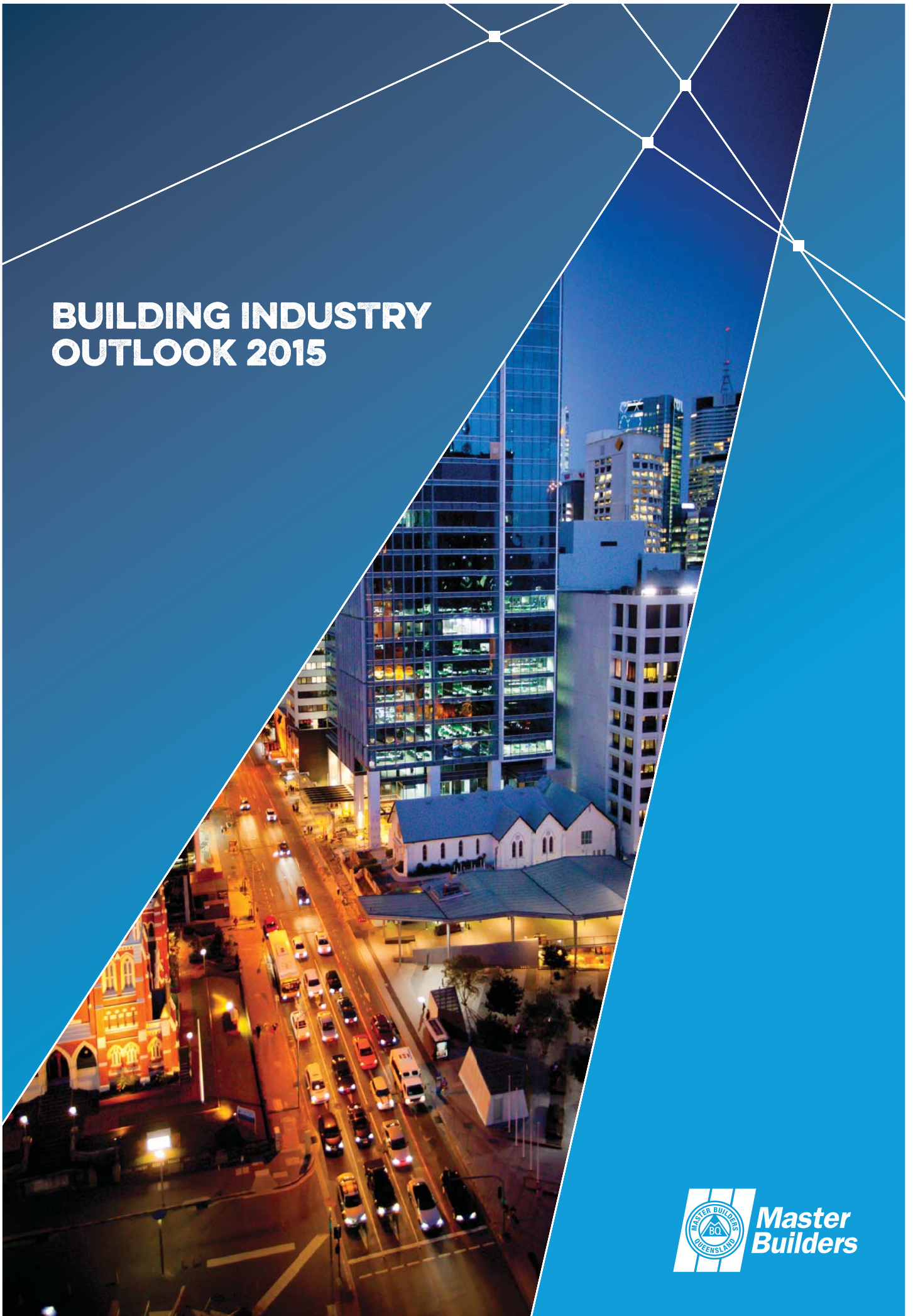


BUILDING INDUSTRY OUTLOOK 2015





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FOREWORD

Welcome to Master Builders' *Building industry outlook 2015*, a timely and comprehensive snapshot of the state of Queensland's building and construction industry: an assessment of business sentiment and outlook for the medium term.

As the peak industry association representing building and construction in Queensland since 1882, Master Builders is well placed as a commentator and information source for building and construction issues.

We hope that you find this report an informative and useful resource and that it serves as a valuable tool in navigating the challenges and seeking out the opportunities that our industry is currently experiencing.

Paul Bidwell
Deputy Executive Director
Master Builders

John Crittall
Director Construction Policy
Master Builders

A MESSAGE FROM OUR PARTNER, THE COURIER-MAIL

As proud supporters of Master Builders, we share the same passion for Queensland, the same vision for a strong and prosperous state where the building and construction industry continues to be an integral part of our local economy.

Since this influential and respected peak industry association was formed in 1882, there have been countless changes in the world of building and construction, in the same way that there have been countless changes to the media industry since The Courier-Mail was first published in June 1846. Regardless of these changes, the way forward is always clear. Continuing innovation, an ongoing dialogue with government and business leaders, and forceful advocacy for our audience on the issues that matter to them. We have a lot in common. Master Builders 8,500 members rely on them to be their voice, as do millions of Queenslanders rely on us.

As the promises of the recent world trade agreements become reality, we look forward to partnering with Master Builders on the new challenges and opportunities that lie ahead.

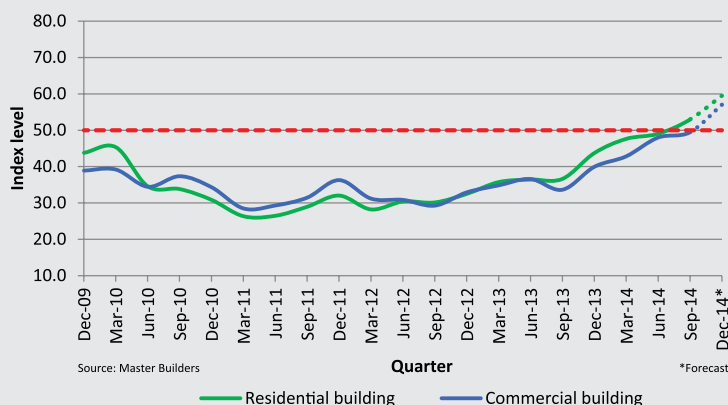
The Courier-Mail

WHERE WE FIND OURSELVES AT THE END OF 2014

The big picture for 2014 has been a return to growth.

The construction industry has maintained a sustained upward trajectory for over 12 months now. The latest Master Builders' *Survey of Industry Conditions* (September 2014 quarter) puts the building industry conditions for the residential sector in positive territory for the first time in the five year history of the survey and the commercial sector not far behind. Similarly, the key business performance benchmarks of turnover and profitability have improved over the year to finally return to satisfactory levels.

Queensland building industry conditions



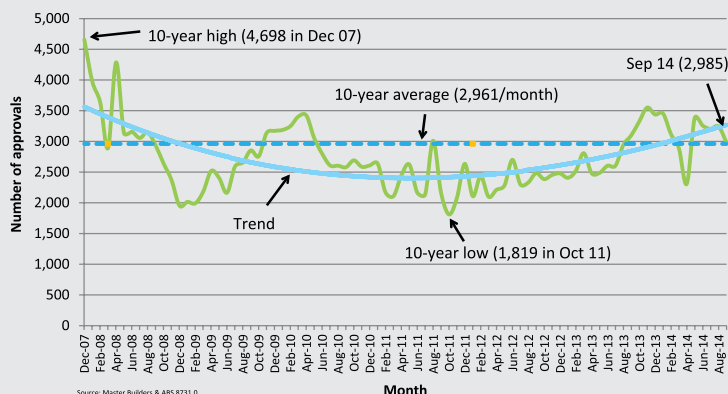
Strong results from the Australian Bureau of Statistics' data on building and finance approvals confirm that we are into a period of sustained recovery.

Still, while things have improved, the news is not positive across the state or all areas of construction. Much of the good news is being driven by the residential multi-unit sector in the south east corner of the state. The commercial sector and the resource-driven areas of Central Queensland and Mackay continue to struggle with a lack of demand.

RESIDENTIAL

Activity in the residential sector continued to pick up over 2013–14 as low interest rates were maintained and consumer confidence returned. For the 12 months to September 2014, dwelling unit approvals are up 22%. The lion's share of these approvals are multi-unit developments, up 32.5% over the year, while approvals for detached house grew by 14.5%.

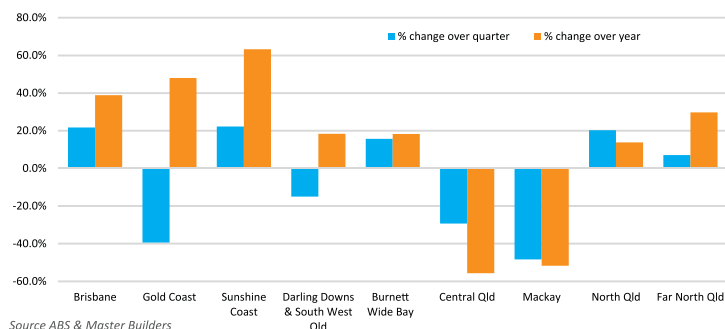
Dwelling unit approvals – Queensland (number; seasonally adjusted)



Similarly, dwelling unit commencements surged ahead in 2013–14. At June 2014, Queensland's total dwelling unit commencements for the year were 35,318. A full 20% higher than the 2012–13 figure of 29,364.

Drilling down into the detail, much of the growth in building approvals has been experienced in south east Queensland. Exceptional growth has been recorded for the Gold and Sunshine Coasts, while the resource regions of Mackay and Central Queensland continue to struggle. The high rise (multi-unit) sector in the inner Brisbane suburbs has performed strongly. Over the course of the year, growth has become more widespread with Wide Bay, North Queensland and Far North Queensland recording better numbers.

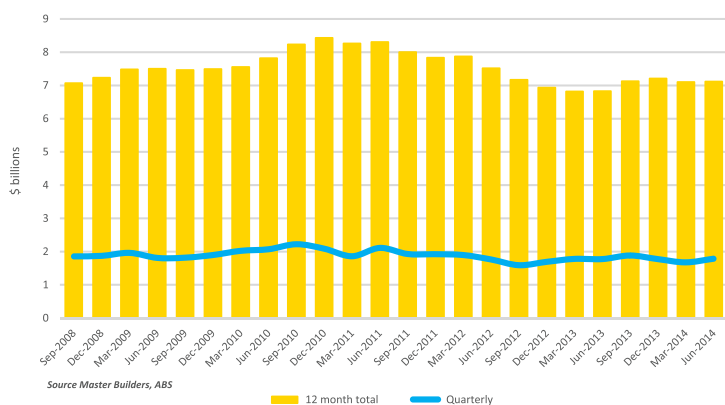
Regional building approvals – percentage change



COMMERCIAL

The commercial (non-residential) sector was flat over the year, delivering \$7.1 billion in construction work. Over the year private sector-funded work remained weak as over-supply and the patchy domestic economy continued to stifle recovery in demand. Many businesses still lack the confidence to make substantial capital investments. The softness in private sector-funded work has been compounded by the sharp downturn in mining investment and continued brakes on public sector expenditure.

Non-residential construction work done, Queensland (seasonally adjusted)



While the challenging conditions have affected most areas of commercial construction, the retail sector has benefited from a number of major shopping centre projects. The tourism industry is beginning to pick up, initiating new investment in hospitality and accommodation infrastructure but most projects are still at the planning stage. Office vacancy rates remain high, hindering growth in that area and the industrial segment remains flat.

The tough conditions have meant that competition for the limited pool of available work remains strong, with businesses holding profit margins to razor thin levels in order to win contracts. This pressure on contractors is clearly not sustainable in the long term.

Engineering construction, which is largely attributable to mining related activity, continued to weaken in 2013–14 as major projects moved out of the investment stage and mining companies cut costs in response to falling coal prices. Looking forward, Master Builders Australia predicts that engineering construction will fall a further 30% or \$10.8 billion over the three years to 2016–17 as mining related activity continues to decline.



CONTEXT FOR THE YEAR AHEAD

ECONOMIC GROWTH

There is good news in the global and national drivers for growth.

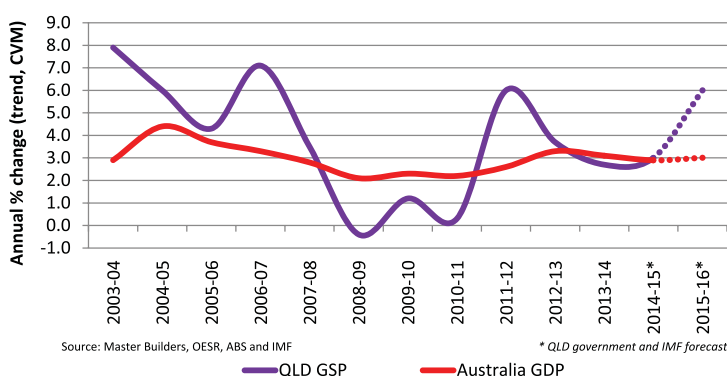
The International Monetary Fund expects global growth to continue to improve in 2014–15, moving from 3.7 % in 2014 to 3.9 % in 2015. While China’s rate of growth has fallen, it is in line with policy maker objectives for a more sustainable level. The United States is also expected to continue at a respectable rate of growth.

The Australian economy is in good shape with GDP sitting on 3.1 % (ABS). The Reserve Bank of Australia (RBA) reports that markets are feeling more confident, pricing the risk of an adverse event as a very low probability.

For Queensland, the good news is still to come. While the Queensland economy has maintained a growth rate of 2.7 %, this is a drop from 3.7 % in 2012–13 and from 6 % in 2011–12. The Queensland economy has been hit hard by the slowdown in the investment in the resource sector.

However, that looks set to change. The Queensland Government forecasts an upturn in economic growth as the government’s debt is brought under control. Deloitte Access Economics predicts that Queensland will be the stand out performer as it “reaps the rewards of a rising Chinese middle class” with a gross state product double that of Victoria and New South Wales. The major LNG projects will begin production and their exports will help to bolster the state’s economic performance. A falling Australian dollar and record low interest rates is particularly good news for Queensland tourism, manufacturing and agriculture.

Queensland’s gross state product and Australia’s GDP



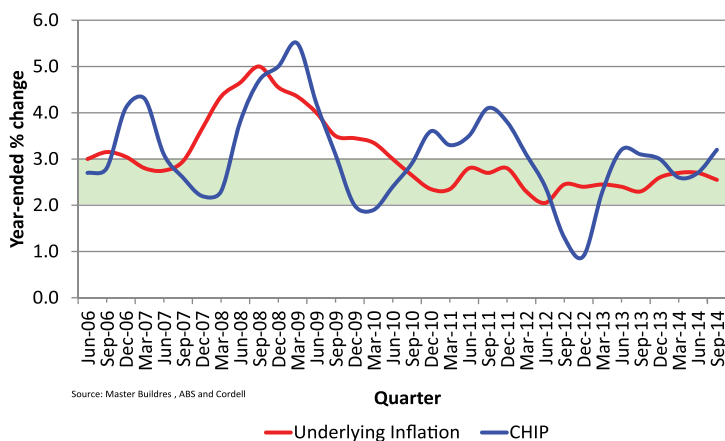
INFLATION & CONSTRUCTION COSTS

Inflation remained subdued over the year and well within the RBA's target range of 2–3%. Looking ahead, the RBA expects the underlying inflation rate to remain moderate with there being “ongoing spare capacity in the labour and product markets”.

The low inflation rate has helped to build confidence that the RBA will not move to raise interest rates in the short term. Beyond that, it is likely that the cash rate will begin to rise sometime well into 2015. In the meantime, retail rates have continued to move lower as the competition from lenders has increased.

Construction costs have been growing at a faster rate for the Queensland residential construction industry. The Cordell Housing Index Price (CHIP Report) reports that the cost of residential building work has risen by 3.3% over the year. As demand strengthens this is expected to continue.

Inflation – Australia and housing construction



While the commercial sector has also been subjected to similar cost increases, especially with respect to materials, it is not expected, in light of the continued weak demand, that this will be reflected in higher contract prices for at least the next 12 months.

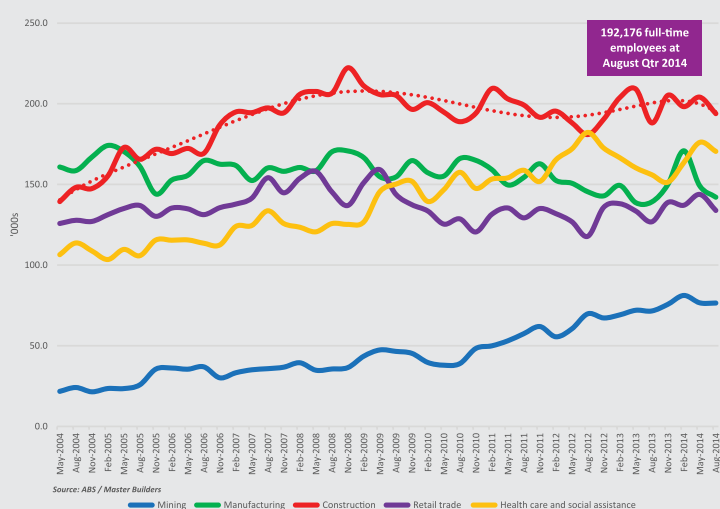
EMPLOYMENT

Hampering the demand for new construction is Queensland's weak employment numbers.

The unemployment rate rose to 7 %, seasonally adjusted, in October 2014 (ABS). Jobs are being created, with 424,000 over the past 12 months, but not at a rate to accommodate the increased number of people looking for work. Weak employment in the wider economy is also leading to lower levels of wage growth, stifling demand for new construction. With continued spare capacity in the labour market it will be some time before this begins to turn around.

Total employment in the construction industry has also dropped over the year, falling by 3.3 % from 234,500 to 226,800. Full-time employment has suffered a larger 6.4 % drop, down from 205,200 to 192,200 (ABS). This is largely attributable to the resource sector which has experienced heavy job losses over the year.

Total number of full-time employed persons in Queensland by industry (original)



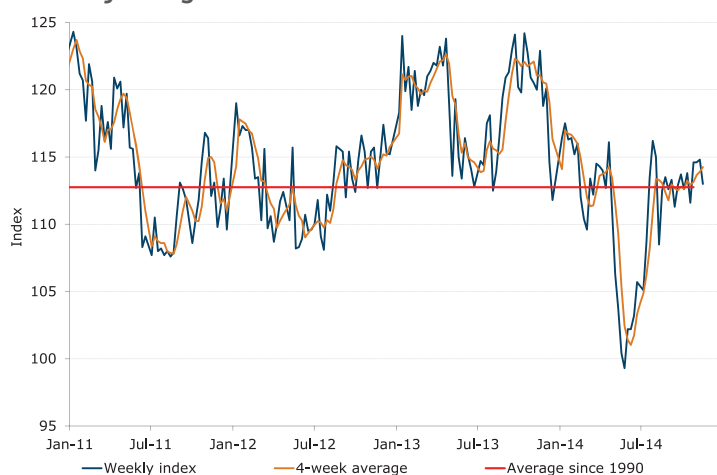
The residential and commercial sectors have seen a growth in employment and this is expected to continue. Reports of shortages of specific trades within the growth areas are emerging. While this will be accommodated in part by employees and contractors moving to the new growth areas, there is likely to be an increasing shortage of skills into 2016.

CONSUMER CONFIDENCE

Meaningful improvement in building activity and industry conditions will require a sustained improvement in consumer and business confidence.

Following the post-election high and the post-Budget low, consumer sentiment appears to be settling comfortably above long-term averages. The *ANZ-Roy Morgan Consumer Confidence Survey* reports that consumers are beginning to feel more confident in their household finances but remain wary of the future economic outlook. Despite record levels of wealth, savings rates remain high as consumers are reluctant to spend.

ANZ-Roy Morgan consumer confidence levels



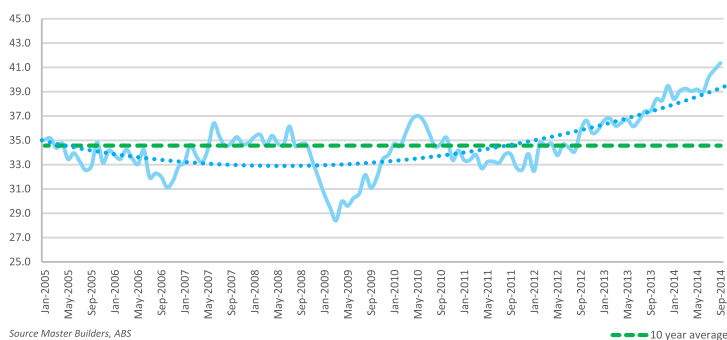
Source: ANZ-Roy Morgan

INVESTMENT

In the commercial sector, business investment is crucial for demand. While business investment has been increasing, NAB's *Quarterly Business Survey* reports that it will not be enough to offset the slump in mining investment that is still to come. The Queensland Government expects a drop in business investment of 20% over 2014–15 and a further drop of 7% in 2015–16. Public spending is also expected to remain subdued with modest investment intentions from both the federal and state governments.

Increase in demand for housing as an investment is a significant positive for the residential sector. ABS data shows a surge in housing finance for investment purposes, currently 41.4% of total housing finance, well above the 34.6% long-term average. It is likely that this understates the amount of investment housing as it does not fully capture the significant amount of foreign investment in new construction (where there is often no Australian lender finance) that is driving the markets in the major capital cities, including Brisbane.

Percentage of housing finance for investment (seasonally adjusted)

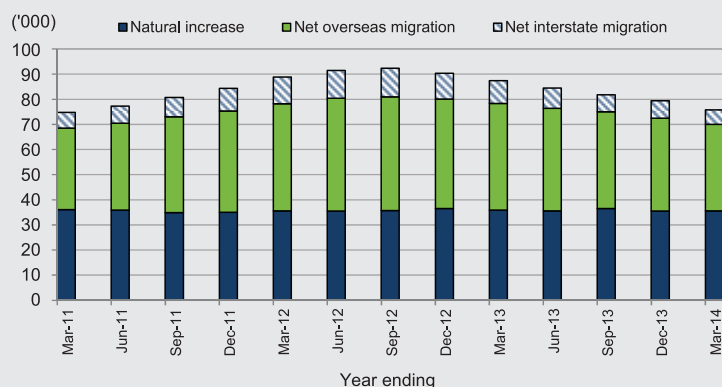


Source: Master Builders, ABS

POPULATION GROWTH

The current state-wide rate of population growth is modest by historical standards. In particular, interstate migration is relatively low. There are expectations that Queensland population growth will pick up once again as the house price gap rises with respect to the southern states and economic and employment growth returns.

Annual population increase – Queensland

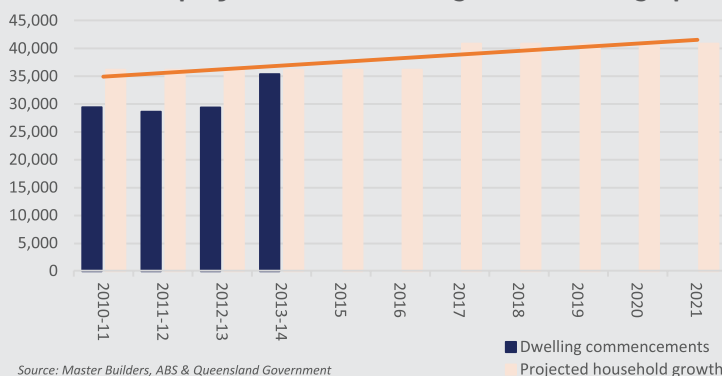


Source: Queensland Trade and Treasury

The government projects Queensland's population to grow at an average of 989,264 people each year out to 2016. Assuming an average household size of 2.6, as recorded at the last census, this will mean 36,000 new households each year up to 2016. Following a 20% increase in dwelling commencements over 2013–14, at 35,318 we are now just short of meeting this increased housing need.

After 2016, population growth is expected to pick up, increasing to an average of 40,282 households each year to 2021.

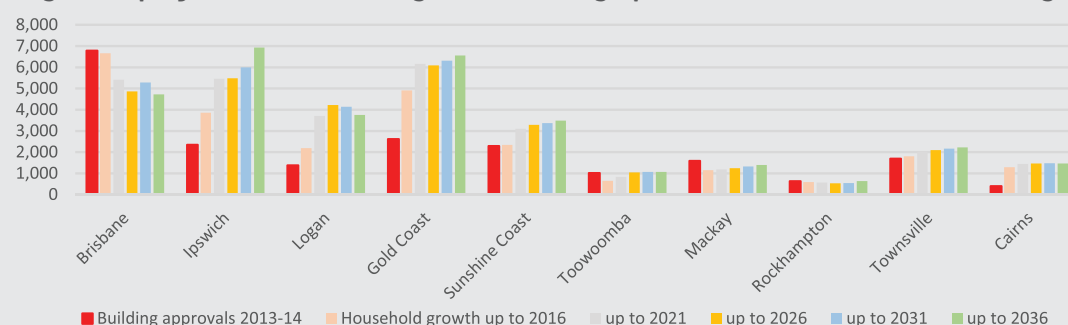
Queensland: projected household growth (average per annum) and dwelling commencements



Source: Master Builders, ABS & Queensland Government

Looking to the regions, this rate of growth will not be experienced evenly. Ipswich, Logan, the Gold and Sunshine Coasts are all expected to experience a significant population increase. Currently, building approvals (and consequently dwelling commencements) are a long way short of the projected household growth for these regions.

Regional: projected household growth (average per annum) and current building approvals



Source: Master Builders, ABS & Queensland Government



INDUSTRY OUTLOOK 2015

RESIDENTIAL

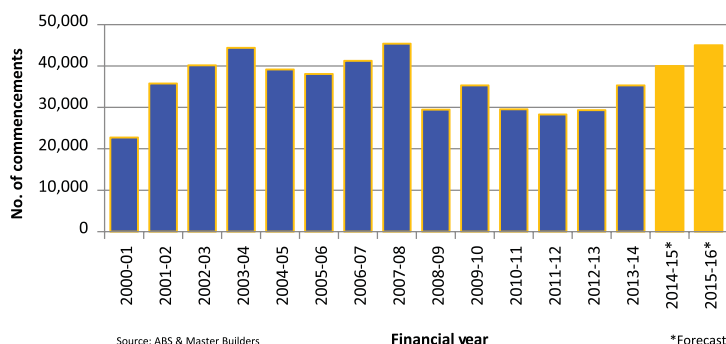
Looking forward, the prospects for the residential sector over the next 12 to 24 months are strong.

Low interest rates are helping to stimulate demand and the global economic environment is more settled. Consumer confidence has improved and the prospect of economic growth is ramping up once more. While unemployment remains high and income and population growth subdued, this is expected to improve. Continued house price growth and low interest rates will help to attract both owner occupiers and investors into the market.

Master Builders forecasts 40,000 dwelling unit commencements in 2014–15 which equates to a rise of 14% on the 35,318 starts in 2013–14. In 2015–16 we estimate dwelling unit commencements will increase a further 10% to 45,000 starts.

The growth will spread further into the regions and across housing types, particularly detached houses. Owner occupiers will increasingly move into the market, while investors will become more cautious. High-rise residential will continue to be a strong performer as the large number of projects approved in 2014 move into the construction stage.

New dwelling unit commencements & forecast (Queensland)



Unfortunately, affordability of new housing will remain an ongoing problem for the industry over the longer term. This is despite the fact that it has improved slightly over the last 12 months thanks to lower mortgage rates. Supply constraints such as those imposed by planning laws will compound affordability problems, as will the significant 'on-costs' of government taxes and charges. Material and labour costs are also expected to continue to rise at a rate faster than inflation as demand picks up.

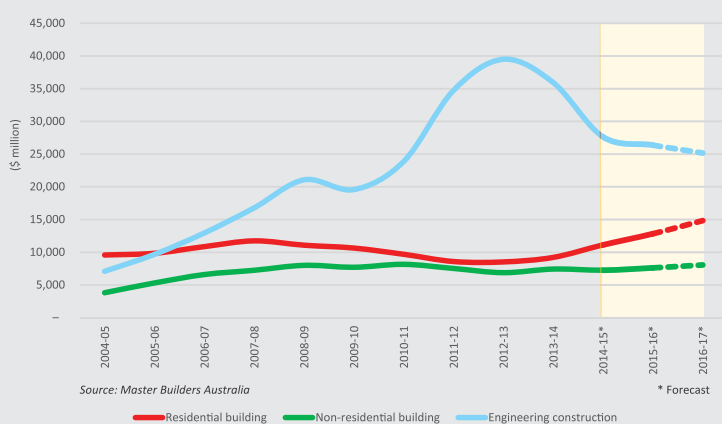
As with last year, renovation activity will remain solid. The high cost of buying a new home will encourage many owners to stay put and renovate rather than sell and upgrade to a new home. Kitchens and bathrooms are likely to remain popular options on the renovation front as they can make a home more liveable while adding value at the same time.

COMMERCIAL

The ongoing weakness in private and public sector investment is the biggest issue for the commercial (non-residential) sector and there are few signs of this turning around. Many businesses are likely to remain hesitant to expend capital on non-essential assets until there is a clear and sustained improvement in the economic outlook. While there is much talk of government investment in infrastructure, in reality this will only assist a few targeted areas and will not offset the ongoing contraction in mining investment.

2015 is forecast to remain flat for commercial (non-residential) construction.

Queensland construction activity – actual and forecast



Looking to the non-residential construction segments, there are no winners in 2015. There are a number of major retail projects coming to an end with no clear pipeline of new work. The office market continues to be over-supplied and the industrial segment will remain flat.

The tourism industry is experiencing an upturn and it is anticipated that this will gradually flow through to new investment in tourism infrastructure, though not in the short term. Over the next 12 months the health and aged-care segment will continue to benefit from demand due to an aging population and Queensland Government investment in hospital infrastructure. Into the longer term there will be a decline in public capital works funding in this area and the funding that is available will be focused on smaller regional projects.

The bulk of construction activity will continue to be in the engineering sector, despite this segment falling significantly.

REGIONAL QUEENSLAND

GREATER BRISBANE

Brisbane has been the focus of growth in multi-unit residential, securing two-thirds of all multi-unit approvals for the state. This development is predominantly occurring in the inner Brisbane suburbs and is investor driven. While there is currently a steady pipeline of new high-rise multi-unit dwellings coming on to the market, eventually there will be a saturation point.

Approvals for detached houses have also surged and will continue to be a strong area of growth for the region. Growth in this segment will be underpinned by the strong population growth and infrastructure investment underway in the Ipswich and Logan areas.

DOWNS & WESTERN

The construction industry in the region has been turning in a solid performance for some time now and this is set to continue. The Toowoomba region has a diverse economy and is a major employment hub. It is the base for significant LNG development further west, the long awaited Second Range Crossing is finally funded and underway and the new Brisbane West Wellcamp Airport is open for business.

GOLD COAST

The Gold Coast has been the standout performer of 2014 and this is expected to continue. While its growth has been led, like Brisbane, by investors in multi-unit developments, it is coming off a low base and is underpinned by a healthy population growth rate. The city has benefited from the construction of the Gold Coast University Hospital and the Rapid Transit project and will continue to benefit from venue development for the 2018 Commonwealth Games.

SUNSHINE COAST

The Sunshine Coast residential sector will be one of the standout performers over the next 12 months. The region will benefit from significant population growth, a strengthening tourism sector and the ongoing investment in the \$1.8 billion Sunshine Coast University Hospital.

While the local commercial sector will lag, there will be opportunities as projects related to the hospital get underway (hotel, accommodation and medical buildings) and in the development of the new Maroochydore city centre.

BURNETT WIDE BAY

The Sunshine Coast boom is beginning to trickle north with the Burnett Wide Bay region beginning to strengthen. The area is increasingly attractive to those seeking a sea change and to fly-in-fly-out workers. A previous oversupply of housing has now been absorbed and the region is ready to move forward again.

CENTRAL QUEENSLAND

Central Queensland will continue to struggle with the decline in mining investment. The end of this retraction has not yet been seen and it will continue to be a challenge for the region.

While other sectors of the economy will not grow to the extent that they can offset this drop, there are signs of improvement. Tourism is generating activity for the commercial sector, in particular projects for Great Keppel Island, Iwasaki redevelopment and the Yeppoon foreshore. The residential sector in the Rockhampton and Capricorn Coast areas are starting to make a slow but steady comeback. The region will also draw some benefit from the development of the Galilee Basin should the proposal for Adani's Carmichael Mine or other projects proposed for the area go ahead.

MACKAY

The Mackay region is struggling with the decline in mining investment and is now recording building approval figures at the lowest level for four years. The construction of investment housing during the high demand of 2012 has left an oversupply that is not helping the current new housing market.

Looking forward, Mackay is projected to enjoy a healthy population growth rate of 2% per annum which will help to push residential construction along.

The Galilee Basin State Development Area is another opportunity on the horizon. Adani's Carmichael Coal Mine and Rail Project and the Abbot Port Coal Terminal will bring about the largest thermal coal mine in Australia, a new terminal at the Abbot Point port and 300km rail link. Together the three projects are expected to employ 3,500 during construction and 4,500 during operation. It could get underway as soon as early 2015 and is expected to be producing coal from 2017.

The new rail and port infrastructure will help to facilitate a number of other major resource projects currently being investigated. These include projects under investigation by Waratah Coal, Macmines Australia and GVK Hancock.

NORTH QUEENSLAND

Townsville has benefited from a diversified economy and a relatively stable level of construction activity. This is expected to continue into the next 12 months, with investment in a number of major projects and moderate population growth pushing things along.

Into the longer term, Townsville is set to benefit from the Flinders Street Mall redevelopment, the Waterfront priority development area adjacent to the CBD, and if funded, Stadium Northern Australia – the 'super stadium'.

FAR NORTH QUEENSLAND

The building and construction industry in Cairns has strengthened markedly over the past 12 months and this is set to continue as the tourism sector improves, major infrastructure projects get underway and the population grows.

Driving demand in the region is the Cairns Aquarium, Aspiat Corporation's Central Park development, the Etheridge Integrated Agricultural project, upgrade of Cairns airport, the ongoing Cairns Base Hospital redevelopment and numerous energy and mining sector projects.

However, it is the \$8.15 billion Aquis Great Barrier Reef Resort that will be the real game changer if it goes ahead. The completed resort will be of a scale not seen before in Australia and would become the largest tourist destination in the Asia-Pacific region and the largest private construction project in regional Australia. It will consist of eight new hotels, convention and exhibition centre, casino, two theatres, Indigenous cultural centre, one of the world's largest aquariums, golf course, shops and restaurants. It is expected to provide 3,750 jobs at peak construction and then have an operational workforce of 20,000, driving the construction industry in the region for years to come.



OPPORTUNITIES & CHALLENGES

In summary, the outlook for the Queensland building and construction is good. Different segments of the industry will continue to perform better than others, but growth will slowly spread as the year progresses.

Important to this growth will be a period of stability for the major economic drivers of interest rates, inflation and economic growth. It is this stability that will underpin consumer and business confidence and the confidence to invest in new construction.

It is important that we do not take growth for granted as there will continue to be many challenges for the industry to overcome. In response to these challenges, in 2015 Master Builders will focus on six key areas:

- Stimulating demand for new construction
- Providing housing at price points that are affordable and contain building costs
- Reducing the limits that industrial relations places on productivity and bring back the rule of law to all construction sites
- Winding back the highly prescriptive approach to health and safety
- Improving the capacity of contractors to better manage construction risk
- Providing training that is relevant and beneficial to the industry.

MASTER BUILDERS OFFICE LOCATIONS

Master Builders Head Office

417 Wickham Terrace
Brisbane Queensland 4000
p 3225 6444
f 3225 6545
ask@masterbuilders.asn.au

Master Builders Burnett Wide Bay

162 Boat Harbour Drive
Hervey Bay Queensland 4655
p 4303 2400
f 4148 6334
bwb@masterbuilders.asn.au

Master Builders Central Queensland

35 Derby Street
(PO Box 631)
Rockhampton Queensland 4700
p 4923 1900
f 4921 3235
cq@masterbuilders.asn.au

Master Builders Downs & Western

166 Hume Street
Toowoomba Queensland 4350
p 4699 4100
f 4641 7854
dw@masterbuilders.asn.au

Master Builders Far North Queensland

310-314 Gatton Street,
Manunda Queensland 4870
PO Box 806
Earlville Queensland 4870
p 4042 8800
f 4041 7663
fnq@masterbuilders.asn.au

Master Builders Gold Coast

18 Central Park Avenue
Ashmore Queensland 4214
p 5582 7100
f 5597 7044
gc@masterbuilders.asn.au

Master Builders Mackay & Whitsunday

Suite 2, 40 Evans Avenue
North Mackay Queensland 4740
p 4969 4500
f 4829 4184
mw@masterbuilders.asn.au

Master Builders North Queensland

Master Builders House
Unit 1, 316 Sturt Street
(PO Box 5801)
Townsville Queensland 4810
p 4417 1800
f 4771 5777
nq@masterbuilders.asn.au

Master Builders Sunshine Coast

Level 1, 91 King Street
(PO Box 1458)
Buderim Queensland 4556
p 5456 9800
f 5301 8124
ssc@masterbuilders.asn.au

www.masterbuilders.asn.au

