

AUSTRALIAN Performance of Construction Index



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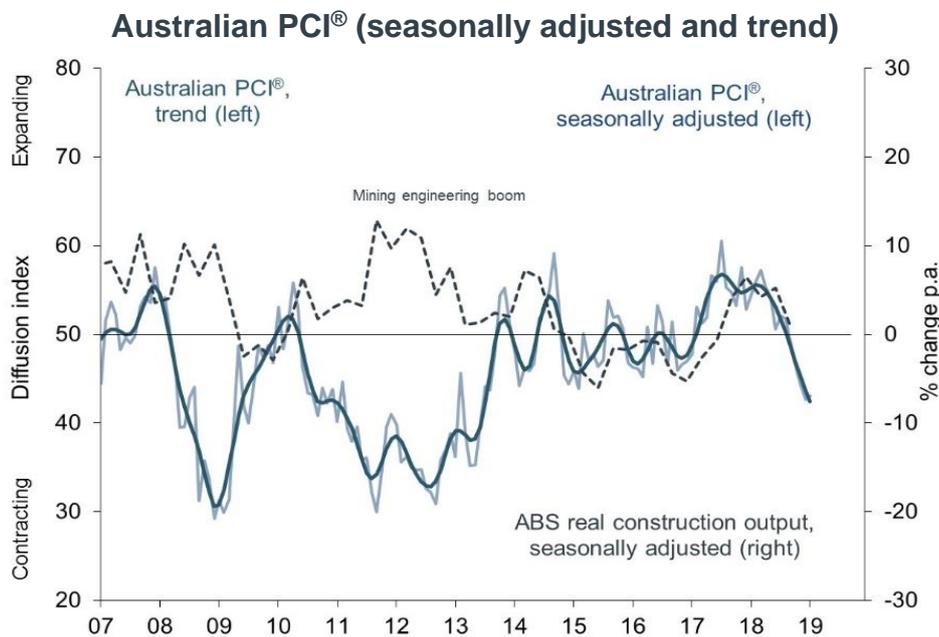
CONSTRUCTION FALLS AGAIN IN JANUARY AS HEADWINDS PERSIST

The Australian Industry Group/Housing Industry Association Australian Performance of Construction Index (**Australian PCI®**) registered 43.1 points (seasonally adjusted) in January. This was an increase of 0.5 points from December, indicating only a marginal easing in the rate of decline for the industry on aggregate.

The slightly milder decline in the **Australian PCI®** in January reflected less pronounced reductions in activity and new orders. However, highlighting the soft overall state of business conditions heading into 2019, both employment and deliveries from suppliers contracted at steeper rates during the month.

All four sectors of the **Australian PCI®** contracted in January. Weighing heavily on overall industry conditions was a further weakening in the house and apartment building sectors where rates of decline in activity and new orders were the most marked in over six years. Commercial construction was again subdued while engineering construction declined for a second month amid reports of a lower volume of new work in January to replace end-of-year completed projects.

House building respondents to the **Australian PCI®** commented on slower market activity due to soft new orders, tighter lending conditions and falling prices which had made prospective buyers more cautious. Apartment builders continued to indicate that activity was being driven lower by soft investor demand and over supplied markets.



AUSTRALIAN PCI®
43.1
 ↑ 0.5 POINTS
 (seasonally adjusted)

ACTIVITY
39.4
 ↑ 3.7 POINTS
 (seasonally adjusted)

NEW ORDERS
44.1
 ↑ 3.1 POINTS
 (seasonally adjusted)

EMPLOYMENT
44.4
 ↓ 5.0 POINTS
 (seasonally adjusted)

HOUSE BUILDING ACTIVITY
34.4
 ↓ 1.9 POINTS
 (trend)

APARTMENT ACTIVITY
24.9
 ↓ 1.6 POINTS
 (trend)

ENGINEERING ACTIVITY
43.3
 ↓ -3.2 POINTS
 (trend)

COMMERCIAL ACTIVITY
44.9
 ↓ 0.5 POINTS
 (trend)

Australian PCI® summary

Construction sectors: Apartment building (24.9 points trend) was the weakest performing sector, declining for a tenth consecutive month and at the sharpest rate since July 2012. House building (34.4 points trend) also remained in negative territory with its rate of contraction the most marked in close to six and a half years. Across the major project areas, commercial construction (44.9 points trend) recorded a sixth month of contraction amid a continued decline in overall demand for commercial projects. Engineering construction (43.3 points trend) was also weaker at the start of 2019, falling for a second month and recording its lowest activity reading in three years.

Construction prices and wages: Input price inflation in the Australian remained elevated in January. The input prices index increased by 2.6 points to 74.6 points, indicating that cost pressures in the construction of building projects lifted during the month. The selling prices sub-index in the **Australian PCI®** increased by 3.6 points to 44.2 points in January, signaling a slightly slower rate of contraction in output prices. However, this negative reading continues to indicate that rising input prices and other costs are not, on average, being passed on to customers, reflecting the strong competition among builders in securing work. The wide gap between these price series in the **Australian PCI®** demonstrates that profit margins remain tight for many businesses in the construction industry.

Construction activity: Across the overall construction industry, both activity (39.4 points) and new orders (44.1) continued to contract in January, although at slower rates relative to the previous month. This was associated with a steeper fall in deliveries of inputs from suppliers (46.5 points) while employment also recorded a sharper rate of contraction (44.4 points) indicating a general reluctance by businesses to increase their workforce capacity amid ongoing soft demand at an aggregate level.

Construction highlights: Across the residential construction sectors, the influence of the downtrend in approvals from historic highs is continuing to have a negative impact on overall industry conditions. Commercial construction is also detracting from industry-wide performance. While businesses in the engineering construction sector have experienced a soft patch in the uptake of new work in recent months, the pipeline of public infrastructure works (including transport, wind and solar projects) remains solid and is likely to underpin more robust conditions for this sector in coming months.

Construction concerns: Respondents are continuing to indicate significant cost pressures in the construction of building and infrastructure projects due to elevated energy prices and supplier price rises, some of which are related to higher commodity prices. There is also widespread reporting of difficulties in recruiting skilled labour, particularly in occupations central to infrastructure activity. Other concerns included the sourcing building materials in the volumes required for major projects and accessing funding for investment and business expansion purposes.

AUSTRALIAN PCI® KEY NUMBERS	Index this month	Change from last month	12-month average		Index this month	Change from last month	12-month average
<i>Seasonally adjusted</i>				<i>trend</i>			
Australian PCI®	43.1	0.5	50.2	Australian PCI®	42.4	-1.3	50.1
Activity	39.4	3.7	48.7	House building	34.4	-1.9	47.0
Employment	44.4	-5.0	50.5	Apartments	24.9	-1.6	38.8
New Orders	44.1	3.1	50.2	Commercial construction	44.9	-0.5	51.8
Supplier Deliveries	46.5	-1.9	53.0	Engineering construction	43.3	-3.2	52.9
Input Prices	74.6	2.6	76.1				
Selling Prices	44.2	3.6	50.6	<i>Seasonally adjusted</i>	%	ppt	%
Average Wages	63.7	2.8	62.9	Capacity Utilisation (%)	77.6	3.1	76.8

Results above 50 points indicate expansion. All indexes for sectors in the Australia PCI® are reported in trend terms (Henderson 13-month filter).

CONSTRUCTION REPORT CARD: Latest ABS data	Level	change q/q	change y/y	Share of total, %
<i>Latest ABS data, seasonally adjusted</i>	\$bn	%	%	%
Nom. value of residential building approvals, \$bn, year to Dec 2018	76.0	-	-2.0	63.8% of building approvals
Nom. value of non-residential building approvals, \$bn, year to Dec 2018	43.0	-	-10.6	36.2% of building approvals
Real value of building work done, \$bn, year to Sep 2018	119.0	-1.5	4.5	56.7% of all construction done
Real value of engineering work done, \$bn, year to Sep 2018	94.0	-4.5	-7.9	43.3% of all construction done
Real value of all construction work done, \$bn, year to Sep 2018	213.9	-2.8	-1.4	-
Real value-added output, \$bn, year to September 2018	141.2	-2.2	4.2	7.6% of total GDP
Number of employed persons, '000, November 2018	1,156	-1.6	-0.6	9.1% of employed persons

ABS data sources: *National Accounts; Business Indicators; Labour Force Quarterly Detail; Building Approvals; Construction Work Done.*

For more detail about the Ai Group Australian PCI® visit: www.aigroup.com.au/policy-and-research/economics/

House building activity

The volume of new house building work done fell by 3.2% q/q but rose by 7.4% p.a. to \$9.2bn in the September quarter of 2018 (seasonally adjusted and inflation-adjusted), accounting for 17.3% of all construction work done.

House building contracted for a sixth consecutive month in January. The sector's activity sub-index decreased by 1.9 points to 34.4 points (trend), indicating a sharper rate of decline relative to December. It was also the softest reading on housing activity since September 2012 and was associated with a sixth month of contraction in new orders. The house building activity index is currently tracking at a level which is 12.6 points below its 12-month average.

House building new orders

The total number of private house approvals fell to 9,261 in December 2018 (trend).

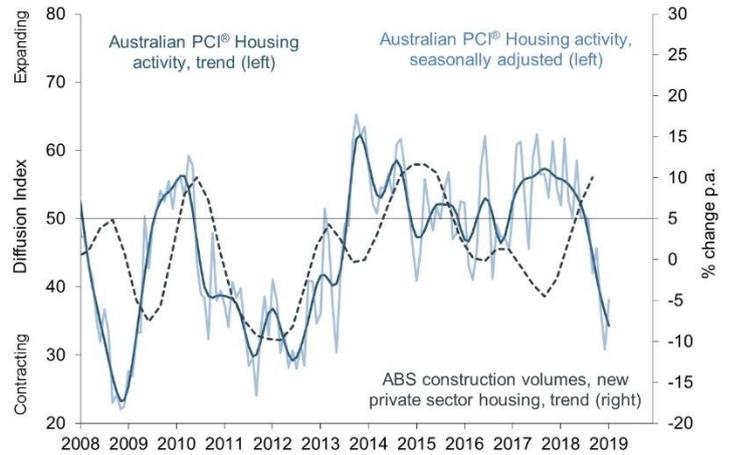
New orders in the house building sector continued to contract in January, and at slightly sharper rate. The sub-index drifted lower by 0.8 points to 43.0 points, placing it below the critical 50-points no change threshold for six consecutive months. It points to a further softening in housing conditions in coming months and follows the 1.1% m/m fall (-9.4% p.a.) in private sector house approvals in December (ABS, trend data).

Apartments activity

The volume of new multi-unit dwelling building work done fell by 0.1% q/q but increased by 1.9% p.a. to \$8.1bn in the September quarter of 2018 (seasonally adjusted and inflation-adjusted), accounting for 15.3% of all construction work done.

Apartment building activity declined for an 10th month in January, and at a steeper rate. The sector's sub-index registered 24.9 points in January, a fall of 1.6 points from the previous month and the most subdued reading since contracting at the same sharp rate in July 2012. The apartment sector has now experienced steady or declining activity in 15 of the past 18 months following a weakening in new orders commencing from September 2017.

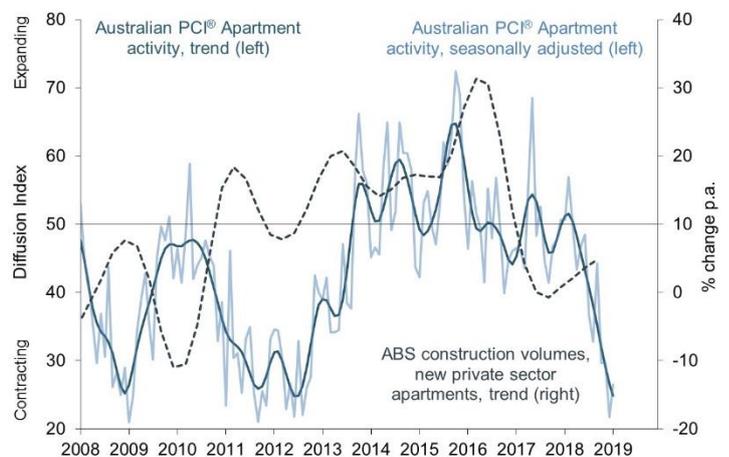
House building activity and ABS construction volumes



House building new orders and ABS building approvals



Apartments activity and ABS construction volumes



Australian PCI® sectors

Apartment new orders

The total number of private 'other dwellings' approvals (apartments, flats and townhouses) fell to 5,467 in December 2018 (trend).

In the apartment building sector, new orders contracted for a 10th month with the sector's sub-index registering 32.3 points in January. This was a decrease of 2.4 points from December, signaling a steeper pace of contraction. This reflects ABS data showing that apartment ('other dwellings') fell 8.5% m/m in December 2018 to be down sharply by -41.2% p.a. over the year to December.

Engineering construction activity

The volume of engineering construction work done fell by 4.5% q/q and by 34.4% p.a. to \$23.0bn in the September quarter of 2018 (seasonally adjusted and inflation-adjusted), accounting for 43.3% of all construction work done.

Engineering construction activity contracted for a second month in January, and at a steeper rate. The sector's sub-index decreased by 3.2 points to 43.3 points.

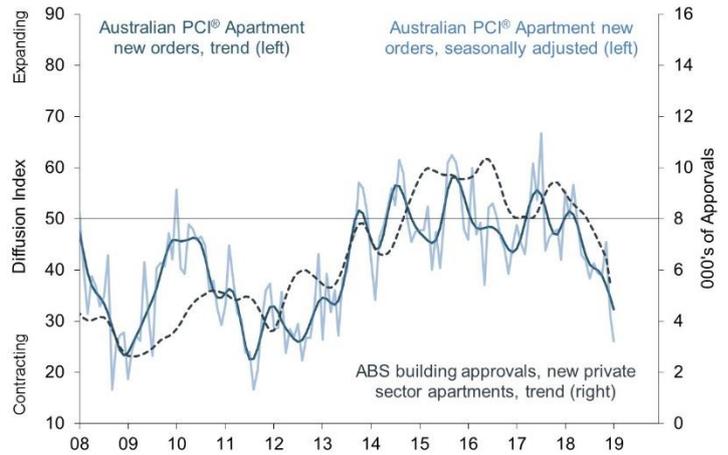
This reflects a soft patch for new work with businesses reporting a weaker volume of new work in January following the completion of contracts towards the end of 2018.

Engineering new orders

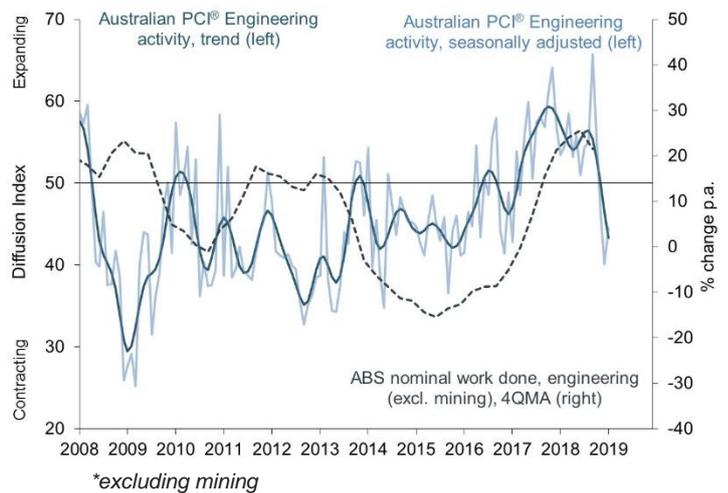
In the engineering construction sector, new orders remained in negative territory for a third month with this sub-index decreasing by 2.2 points to 43.7 points. Whilst this points to a steeper rate of decline in January, activity should continue to be supported over 2019 by the general strength in new orders evident in 2018 and the elevated pipeline of public funded infrastructure projects.

ABS data shows that engineering work in the pipeline (excluding mining related projects) was valued at \$38.3 billion in Q3 2018 (nominal, unadjusted data). While this is below the record high of \$46.4 billion in Q3 2012, it remains solid and is set to underpin strength in engineering construction activity through 2019, particularly as Governments commit to new projects.

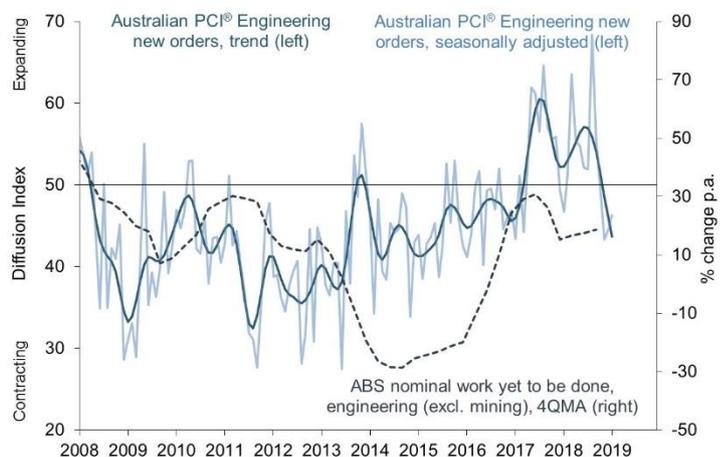
Apartments new orders and ABS building approvals



Engineering construction activity and ABS work done*



Engineering construction new orders and ABS work yet to be done (excluding mining)



Commercial construction activity

The volume of non-residential building work done declined by 1.5% q/q in the September quarter of 2018, but was 4.3% higher over the year (seasonally adjusted and inflation-adjusted), accounting for 19.7% of all construction work done.

Commercial construction recorded a sixth consecutive month of contraction in January. The rate of decline was also marginally steeper with the sector's sub-index decreasing by 0.5 points to 44.9 points. Although approvals are off their highs, conditions are mixed with businesses continuing to report growth opportunities across key commercial and social building categories.

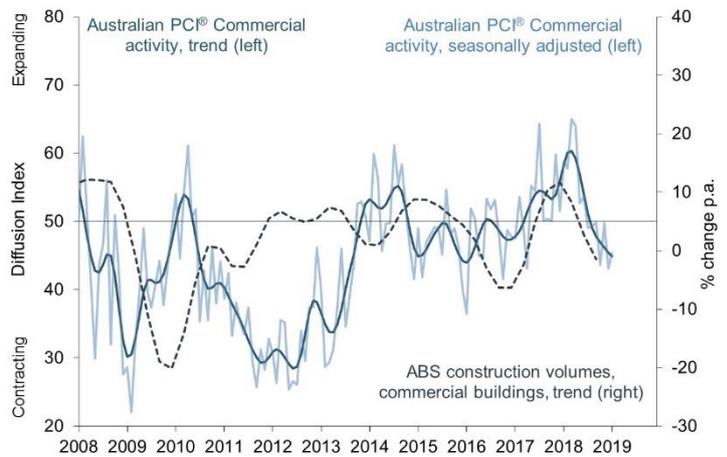
Commercial new orders

The real value of non-residential building approvals increased by 1.5% q/q but was down by 16.8% p.a. to \$10.1bn in the September quarter 2018 (seasonally adjusted).

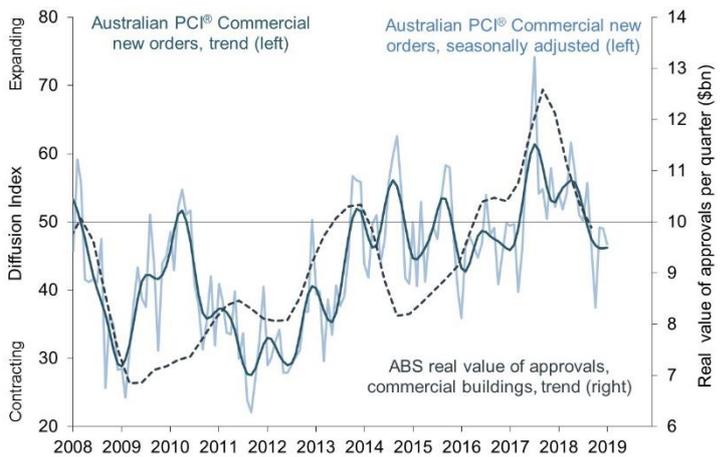
New orders in the commercial construction sector recorded a sixth consecutive month of decline in January. However, the rate of contraction was broadly unchanged, with the sub-index increasing by just 0.1 points to 46.2 points.

The sector also experienced a sustained period of growth in new orders over the 16 months to July 2018 which is reflected in a relatively healthy pipeline of work in project areas including accommodation, offices and aged care. This and the demands of a growing population, particularly in the eastern states, are set to support relatively healthy activity over the year ahead.

Commercial construction activity and ABS work done



Commercial construction new orders and ABS commercial building approvals

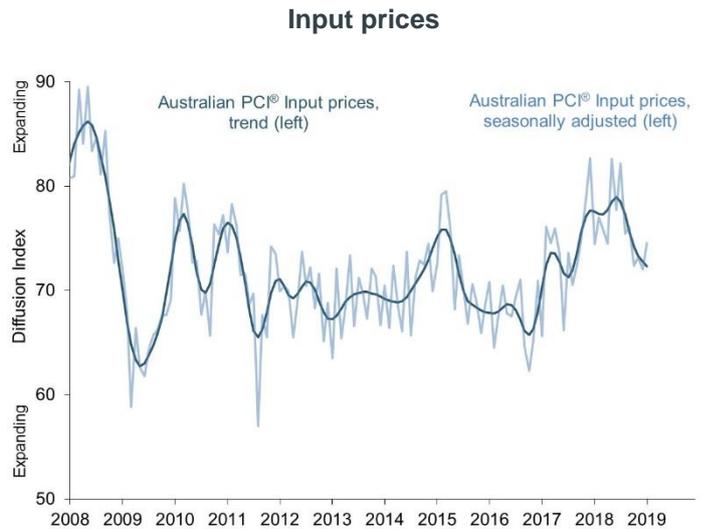


Australian PCI[®] prices and wages

Input prices

The **Australian PCI[®]** input prices sub-index registered 74.6 points in January. This was an increase of 2.6 points from December, indicating that cost pressures in the construction of building projects lifted during the month.

These sustained cost pressures are due to elevated energy costs and supplier price rises, some of which are related to the rising trend in commodity prices. Demand for engineering-related construction materials is especially strong, due to solid pipeline of infrastructure activity).



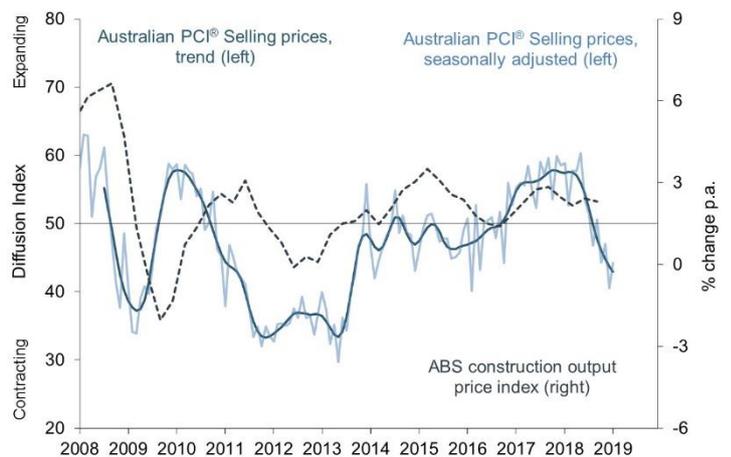
Selling prices

The **ABS construction industry's output price index (PPI)** rose by 0.4% q/q and 2.3% p.a. in the December quarter of 2018.

Selling prices continued to contract in January, albeit at a slower rate. The selling prices sub-index in the **Australian PCI[®]** increased by 3.6 points to 44.2 points in January. However, this negative reading indicates that rising input prices and other costs are not, on average, being passed on to customers. This reluctance to raise prices reflects the strong competition among builders in securing work.

The ongoing gap between these price series in the **Australian PCI[®]** demonstrates that profit margins remain tight for businesses in the construction industry. This is consistent with reports of a highly competitive quoting and tendering environment.

Selling prices and ABS construction industry output prices



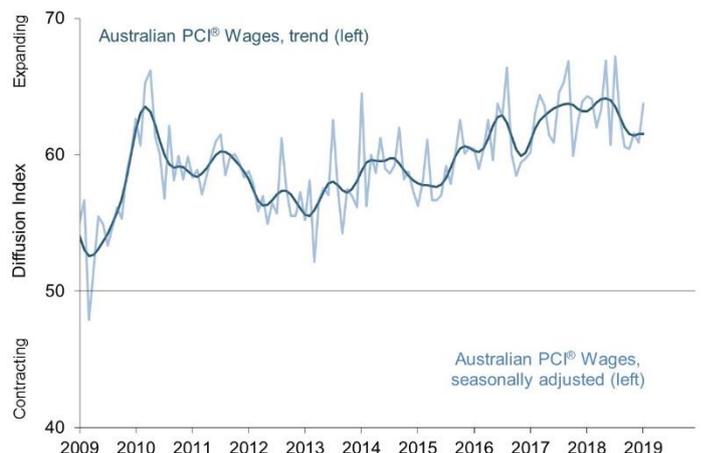
Average wages

The **ABS wage index for private sector construction** rose by 0.5% q/q and 2.0% p.a. in the June quarter of 2018.

Growth in wages continued in January and at a higher rate than the previous month with the wages sub-index increasing by 2.8 points to 63.7 points. This provides further evidence that overall wages growth remains relatively high, particularly due to increasing skill shortages in occupations central to infrastructure activity.

This is in line with data on Federal Enterprise Bargaining Trends (Dep of Education, Employment and Workplace Relations) that new EBA's in the construction industry increased at an average annual rate of 5.9% in Q3 2018 compared with a 3.2% average increase for all industries.

Average wages



Australian PCI® activity

Activity

The activity sub-index in the **Australian PCI®** registered 39.4 points in January. This was up by 3.7 points from the previous month, signaling a slower rate of contraction in total construction activity. However, it marked the fourth consecutive month of declining industry activity.

The ongoing fall in construction activity in January reflected a continuation of soft levels of demand and new orders experienced in aggregate over the past five months.

Overall levels of activity were negatively impacted by falls recorded across all four industry sub-sectors, particularly the steeper declines in January across the housing, apartments and engineering construction sectors.

Employment

The construction sector employed 1,156,900 people in November 2018 (9.1% of total employment).

Construction employment continued to decline in January, and at a sharper rate.

The employment sub-index within the **Australian PCI®** declined by 5.0 points to 44.0 points. This marked a sixth consecutive month of contraction in employment and the seventh decline in the past eight months consistent with the more subdued readings on activity from mid-2018.

It follows a 1.6% q/q (-0.6% p.a.) in total construction employment in November 2018 (ABS original data).

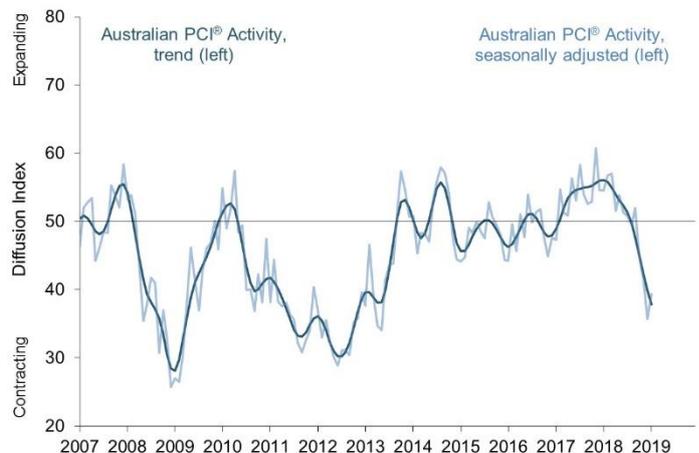
New orders and supplier deliveries

The new orders index in the **Australian PCI®** registered 44.1 points in January. This was an increase of 3.1 points from December, indicating a slower rate of decline on an aggregate industry basis.

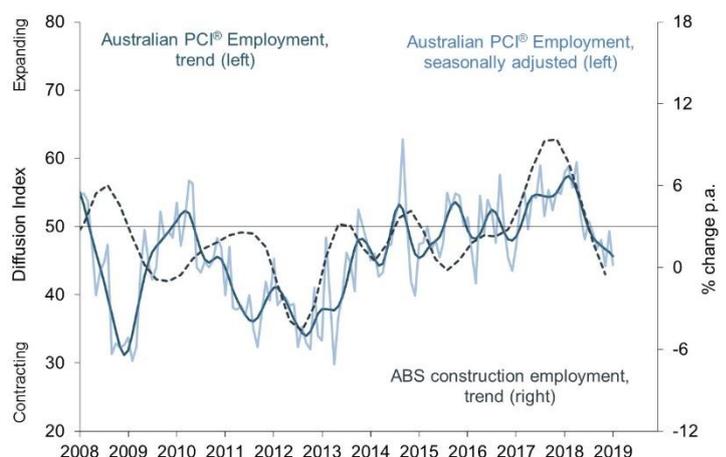
However, the on-going softness in new orders is likely to act as a headwind to stronger overall activity in coming months.

Falls in new orders (trend) were recorded in all four construction sub-sectors in the **Australian PCI®** in January. The housing, apartment and engineering construction sub-sectors all experienced steeper falls while the rate of decline in new orders in the commercial construction sector was unchanged rate relative to December.

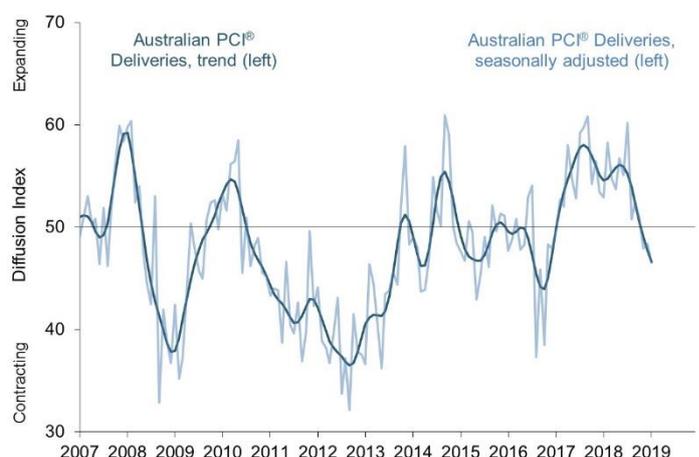
Activity



Employment and ABS construction industry employment



New orders and supplier deliveries



Australian PCI® activity

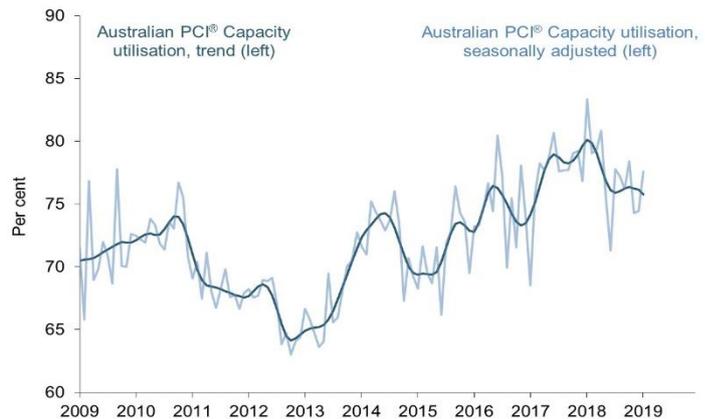
For more information about the Ai Group Australian PCI® visit:

Capacity utilisation

The rate of capacity utilisation stood at 77.6% across the construction industry, up from 74.5% in December, but only slightly higher than the 12-month average utilisation rate of 76.8%.

In trend terms, capacity utilization was at its lowest level in almost two years, further pointing to the need for increased investment in machinery and equipment and the upgrading of employee skills to meet any significant uplift in future demand.

Capacity utilisation



www.aigroup.com.au/policy-and-research/economics/

Australian PCI®: data definitions

The Australian PCI classifies each business according to their single main activity, using the industry data codes and definitions set out in the ANZSIC 2006. These classifications are comparable with all ABS data that use these same codes. For manufacturing in the Australian PCI, the definitions of the 4 sectors are:

1. House building (ANZSIC code 4111 “House construction”). Businesses involved in the construction, repair and renovation of houses (a detached dwelling predominantly used for long term purposes and consisting of one dwelling unit), or in organizing or managing these activities as the prime contractor.
2. Apartment building (ANZSIC code 4112 “Residential building construction n.e.c. (units)”). This covers buildings other than a house primarily used for long-term residential purposes (or has attached to it) more than one dwelling unit such as blocks of flats, home units, attached townhouses, semi-detached houses, maisonettes, duplexes, apartment buildings etc.
3. Engineering construction. (ANZSIC code 4121 “Road and bridge construction” and ANZSIC code 4122 “Non-building construction”). Businesses involved in the construction of engineering projects or infrastructure. This includes transport projects, telecommunications facilities, bridges, water and gas supply systems, pipelines, sports complexes, heavy industry constructions and other large-scale construction projects that do not generally involve the construction of buildings.
4. Commercial construction (ANZSIC code 4111 “Non-residential building construction”). Involves the construction of non-residential buildings such as offices, industrial premises, hotels, hospitals, aged care facilities, education buildings, entertainment and recreation developments, and in carrying out alterations, additions, renovation, and in organizing or managing these activities.

What is the Australian PCI®? The Australian Industry Group Australian Performance of Construction Index (Australian PCI®) is a national composite index based on the diffusion indices for activity, new orders, deliveries, inventories and employment with varying weights. An Australian PCI® reading above 50 points indicates that manufacturing is generally expanding; below 50, that it is declining. The distance from 50 indicates the strength of the expansion or decline. Australian PCI® results are based on responses from a national sample of construction businesses that includes all states and all sectors. The Australian PCI® uses the ANZSIC industry classifications for construction sectors and sector weights derived from ABS industry output data. Seasonal adjustment and trend calculations follow ABS methodology. For further economic analysis and information from the Australian Industry Group, visit <http://www.aigroup.com.au/policy-and-research/economics/economicindicators/>.

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