

Escalation in New Zealand Construction

Rider Levett Bucknall, Steve Gracey and Bradley Coley recently undertook industry engagement research to understand what the key factors are causing escalation in the NZ construction market and what effects these have on current projects.

A summary of the findings was presented at the NZIQS Conference in June 2017. The findings were based on a combination of discussions with Suppliers, Sub Contractors, Main Contractors and a review of internal projects. The following are the key points from the industry research:

What is escalation?

- From a Construction Industry perspective “The anticipated increase in cost of constructing a project over a period”
- In its purest sense, the change in cost of materials, plant & labour

What are the Key factors causing cost escalation?

- Labour demand issues - wages and salaries increasing to a premium
- Raw materials
- Volatility in sub-sub contractors pricing
- Skilled labour diluted causing increase management and support
- Capability of Main Contractors diluted
- New contractor entrants to the market at all levels
- Traffic and parking congestion
- Poor quality design information - more time sorting design issues out
- Allocation and pricing of risk at a premium
- H&S reporting and compliance
- Managing poor workmanship / subcontractors
- Programme risk and LD'S
- Unwillingness to take on risk, or very expensive
- Lack of or late trade pricing

What are the key effects of cost escalation risk going forward?

- Higher prices
- Delays in starting projects
- More Main Contractor risk due to subs over committing
- Less tender pricing received
- Lower productivity and quality
- Staff poaching from a limited skilled pool
- Longer construction programmes
- P&G increases
- Financial strain on subs / main contractors
- “Bow wave” in escalation profile

How to manage cost escalation

- Make the project look attractive to get interest from the market
- Make the contractors and subcontractors tendering easier by producing a schedule of quantities
- More reliable budgeting to the client from inception
- Have a clear project brief and scope
- Define who owns the risk and allocate the risk items accordingly
- Realistic project start dates and construction programmes
- Early engagement with industry
- A move toward negotiating with contractors, sub contractors and suppliers where applicable
- Self perform works rather than contract out

The market look ahead

- Not all projects are equal
- Escalation likely to continue through to 2018/2019
- Major projects still yet to hit the market
- Some projects may start being shelved to balance supply and demand

NZIQS Research Group in conjunction with RLB, Steve Gracey and Bradley Coley.