2016

State of the South African Civil Engineering Contracting Industry

SAFCEC

2nd Quarter 2016

SOUTH AFRICAN FORUM OF CIVIL ENGINEERING CONTRACTORS | www.safcec.org.za | 011 409 0900
Physical address: 3rd Floor - SAFCEC House P O Box 644 12 Skeen Boulevard Bedfordview, 2008

Contents

Executive Summary

There has been no significant change in global developments since our last review, although the struggle amongst emerging markets to cope with rising debt and revenue contractions due to the lower commodity price cycle, has intensified. Domestic economic growth disappointed with a 1.2 percent contraction in the 1st quarter of 2016, due to a further contraction in the agriculture sector, while the mining sector plummeted by 18 percent, despite a small improvement in commodity prices.

Investment performed poorly in the 1st quarter as total gross fixed capital formation fell by 1.3 percent in the 1st quarter. Investment in buildings fell by between 4 and 5 percent, while some growth was reported in construction works, up 6 percent y-y in nominal terms, supported by investment in renewable energy projects. Inflation remains at above target levels, while producer inflation showed some improvement although still well above the upper inflationary target. The exchange rate has recovered since the beginning of the year, but remains at around R15/US Dollar, while Brent crude oil prices increased to around $50/barrel, putting upward pressure on the cost of fuel and thereby input costs and secondary inflation. The Reserve Bank has not raised the repo rate, while the US Federal Reserve also delayed their rate tightening cycle, giving some respite to the South African (and other emerging markets) economy.

Conditions in the civil engineering contracting industry remains under pressure. The latest survey may have shown a slowdown in the rate of decline or levels of pessimism, but the overall sentiment remains deeply concerning by the lack of growth experienced in the industry. The poor state of affairs are evident by a further contraction in revenue and employment in the 1st quarter of 2016 compared to the last quarter of 2015. Confidence levels regarding tendering and award activity remained weak, but fortunately the rate of decline (or level of pessimism) seems to have reached a lower turning point. Late payments were also reported to have increased more robustly in the 1st quarter, and now represent 22 percent of total turnover in the industry. The value of payments outstanding for longer than 90 days increased to 4.1 percent, with no real legislative progress in terms of the Prompt Payment Regulations, issued by the CIDB for public comment in July 2015. Competition for tenders remain fierce, while satisfaction rates regarding tender prices vary from firm to firm, majority of the larger firms regard tender prices as being low. No improvement is expected in profit margins, as majority of firms expect margins to stabilise (at least not further deteriorate), but this comes at a price, as firms are resorting to restructuring measures to improve profitability in view of weak construction activity levels. Unless expectations regarding improved profitability do not start to increase, the outlook on employment will remain dim. The nominal value of civil contacts awarded increased by only 4 percent in the 1st quarter of 2016, following the 10 percent increase reported in 2015, which in real terms, allowing for construction cost inflation of 5 percent, suggest negative real growth of 1 percent in the 1st quarter.

On the upside, there has been a marginal increase in the value of two year forward order books, also confirmed by various financial results from listed construction companies, although contractors' confidence remain largely negative regarding the outlook for order books. There was a 32 percent increase in the value of estimated tenders published in the 1st quarter of 2016. Although this growth comes off a low base in the 1st quarter of 2015, it remains encouraging. Construction cost inflation accelerated in the 1st quarter of 2016, to an average of 5.2 percent from 1.2 percent in the previous (4th) quarter. Contribution factor to the higher inflation was a slowdown in the deflation of material prices, (from -7.0 percent to -0.6 percent), higher labour costs (measured by the CPI), a slowdown in the deflation of fuel

prices to -0.6 percent on average, and an acceleration in the plant index, from 5.2 percent in the 4th quarter to an average of 9.5 percent in the 1st quarter. Higher steel prices in May will put some pressure on material costs in the 2nd quarter, while the cost of fuel and plant equipment is expected to start increasing more robustly, averaging construction cost inflation at between 8 and 10 percent in 2016, before stabilising at between 3 and 5 percent in the next two years. Input costs however are subject to further price developments on the currency and oil markets.

Economic Background

Global growth recovery slower than expected, while outlook for the South African economy deteriorated.

The International Monetary Fund (IMF) and other organisations have downgraded the outlook for growth in the global economy since our last report. This comes as little surprise, as there are only a handful of bigger economies that are looking healthy, let alone offering excellent growth opportunities. Global growth is projected to be 0.2 percent less than the initial forecast by the IMF in January. Growth is now projected to be 3.2 percent in 2016, recovering slightly to 3.5 percent in 2017.

Among advanced economies, the United States has just experienced two quarters of growth averaging 1.0 percent, and has again opted to leave the federal funds rate unchanged. The world's biggest economy is expected to have a relatively flat performance this year, growing just 2.4 percent, with a modest recovery in 2017. Because of the low oil price, the US dollar has strengthened considerably in the period post commodity slowdown. This had led to more modest demand for US exports, the manufacturing industry is also relatively stagnant. Growth in the housing market, as well as a projected improvement in the government's finances are expected to boost the economy in 2017. Further monetary easing has boosted a cyclical recovery in the Eurozone, although the outlook in most of the Eurozone countries is below 1 percent. Low investment, high unemployment and weak balance sheets weigh down growth potential. Growth in the Euro Area is expected to remain modest at about 1.5 percent in 2016.

Among the four BRIC countries, Brazil and Russia are in recession, while China is experiencing a sharp structural slowdown. India is the only BRIC country still doing relatively well. Many other emerging markets have slowed since 2013, owing to weak external conditions, economic fragility (stemming from loose monetary fiscal, and credit policies in the good years) and, often, a move away from market-oriented reforms and toward variants of state capitalism. Weak growth is forecasted in most of Latin America, as well as in the Middle East. Most of Africa is being negatively affected by global developments. The continent has proved not to be insulated from these developments.

Overall, emerging markets do still make up the highest proportion of the 3.2 percent growth that is forecasted for the world economy. Prospects do however remain uneven, with growth definitely looking weaker over the past 2 decades. Growth for emerging markets is forecasted to be 4.1 percent this year, increasing modestly to 4.6 percent next year.

The IMF argue that since their last update in January, risks to the global growth outlook has become more pronounced. These include a protracted period of low oil prices, which could further worsen the outlook to the very many countries that depend on some sort of recovery in the oil price, even modest. A sharper slowdown in China than currently expected could have strong international spill overs through trade, commodity prices and confidence, and lead to a more generalised slowdown in the global economy. The risk of further geopolitical shocks loom over several countries that have left issues unchecked, which could lead to further spill overs.

		Projections		Difference from January 2016 *WEO Update*[1]		Difference from October 2015 WEO[1]	
	2015	2016	2017	2016	2017	2016	2017
World Output	**3.1**	**3.2**	**3.5**	**–0.2**	**–0.1**	**–0.4**	**–0.3**
Advanced Economies	**1.9**	**1.9**	**2.0**	**–0.2**	**–0.1**	**–0.3**	**–0.2**
United States	2.4	2.4	2.5	–0.2	–0.1	–0.4	–0.3
Euro Area	1.6	1.5	1.6	–0.2	–0.1	–0.1	–0.1
Germany	1.5	1.5	1.6	–0.2	–0.1	–0.1	0.1
France	1.1	1.1	1.3	–0.2	–0.2	–0.4	–0.3
Italy	0.8	1.0	1.1	–0.3	–0.1	–0.3	–0.1
Spain	3.2	2.6	2.3	–0.1	0.0	0.1	0.1
Japan	0.5	0.5	–0.1	–0.5	–0.4	–0.5	–0.5
United Kingdom	2.2	1.9	2.2	–0.3	0.0	–0.3	0.0
Canada	1.2	1.5	1.9	–0.2	–0.2	–0.2	–0.5
Other Advanced Economies[2]	2.0	2.1	2.4	–0.3	–0.4	–0.6	–0.5
Emerging Market and Developing Economies	**4.0**	**4.1**	**4.6**	**–0.2**	**–0.1**	**–0.4**	**–0.3**
Commonwealth of Independent States	–2.8	–1.1	1.3	–1.1	–0.4	–1.6	–0.7
Russia	–3.7	–1.8	0.8	–0.8	–0.2	–1.2	–0.2
Excluding Russia	–0.6	0.9	2.3	–1.4	–0.9	–1.9	–1.7
Emerging and Developing Asia	6.6	6.4	6.3	0.1	0.1	0.0	0.0
China	6.9	6.5	6.2	0.2	0.2	0.2	0.2
India[3]	7.3	7.5	7.5	0.0	0.0	0.0	0.0
ASEAN-5[4]	4.7	4.8	5.1	0.0	0.0	–0.1	–0.2
Emerging and Developing Europe	3.5	3.5	3.3	0.4	–0.1	0.5	–0.1
Latin America and the Caribbean	–0.1	–0.5	1.5	–0.2	–0.1	–1.3	–0.8
Brazil	–3.8	–3.8	0.0	–0.3	0.0	–2.8	–2.3
Mexico	2.5	2.4	2.6	–0.2	–0.3	–0.4	–0.5
Middle East, North Africa, Afghanistan, and Pakistan	2.5	3.1	3.5	–0.5	–0.1	–0.8	–0.6
Saudi Arabia	3.4	1.2	1.9	0.0	0.0	–1.0	–1.0
Sub-Saharan Africa	3.4	3.0	4.0	–1.0	–0.7	–1.3	–0.9
Nigeria	2.7	2.3	3.5	–1.8	–0.7	–2.0	–1.0
South Africa	1.3	0.6	1.2	–0.1	–0.6	–0.7	–0.9

Figure 1: IMF Global Economic Outlook January 2016

Domestic Economy

Economic growth contracted by 1.2 percent in the 1st quarter of 2016 (seasonally adjusted annualised rate), following a revised 0.4 percent increase in the previous quarter. Growth was largely dragged down by a significant contraction in the mining sector, down 18.1 percent (following marginal growth of 1.5 percent in the previous quarter), while the agriculture sector, plagued by the persistent drought, declined for the 5th consecutive quarter, down 6.5 percent y-y. Electricity and water, as well as transport and communication also contracted during the 1st quarter, down 2.8 percent and 2.7 percent respectively. Marginal growth was recorded in the manufacturing sector (0.6 percent), while growth in construction slowed to 0.5 percent. The poor performance of the economy in the first quarter raises fears of an imminent recession, worsened by threats of a possible credit downgrade, weaker investor confidence and expectations of higher lending rates. Economic growth has been revised down to 0.8 percent for 2016, with many expecting growth to be even lower.

Stats SA is now also responsible for the expenditure estimates, previously released by the South African Reserve Bank. Gross fixed capital formation fell by 1.3 percent y-y in the 1st quarter (sea. adj. ann rates), following an increase of 0.9

percent in the previous quarter. Investment in housing and other buildings fell 3.7 percent y-y (to R19 bn) and 4.3 percent y-y (to R17.7 bn) respectively, while investment in construction works rose 6.2 percent y-y in the 1st quarter to R60 bn. Stats SA published revised estimates for investment in construction, including revisions to residential buildings, non-residential buildings and construction works. According to the revised estimates, R75bn was spent on housing in 2015 (current prices), R71 bn on non-residential building, and close to R250 bn on construction works. In nominal terms, investment in housing rose 12 percent in 2015, while no growth was reported in non-residential buildings and a 7 percent increase in construction works.

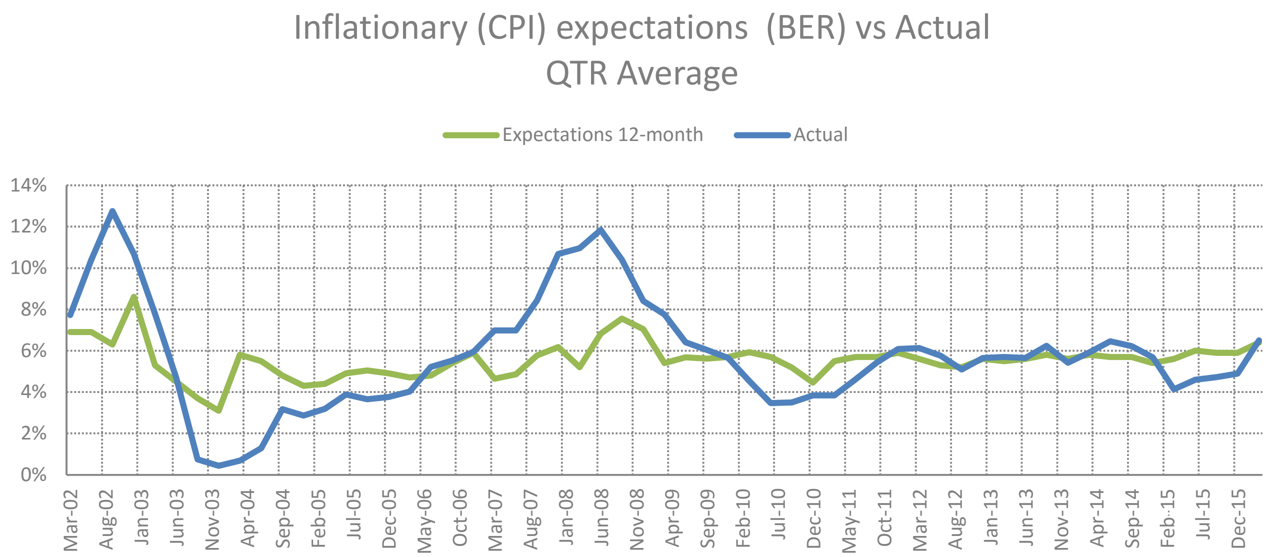
For a review of the revisions by Stats SA to GDP and GFCF estimates please use the following link: http://industryinsight.co.za/reports/Construction_Pulse__Stats_SA_Revisions.pdf

GDP growth has now slowed to below population growth, resulting in declining per capita incomes, or otherwise put, the average South African is becoming poorer. Global conditions have exposed South Africa's, as it did for many countries on the African continent, own economic weakness, exacerbated by policy uncertainty, political instability, and violent protest action. South Africa's GDP growth is currently well below the average for the world, advanced economies, as well as for developing economies, and showed considerably weakness in the last two years. South Africa is facing serious structural constraints, with frustratingly little done to improve South Africa's ability to increase private sector participation, increase foreign direct investment, support industrialisation, increasing global competitiveness, limit debilitating energy constraints and deal more effectively with rigid labour regulations.

Table 1: Gross Domestic Product, production estimates Year on Year percentage change (sea. adj. annualised)

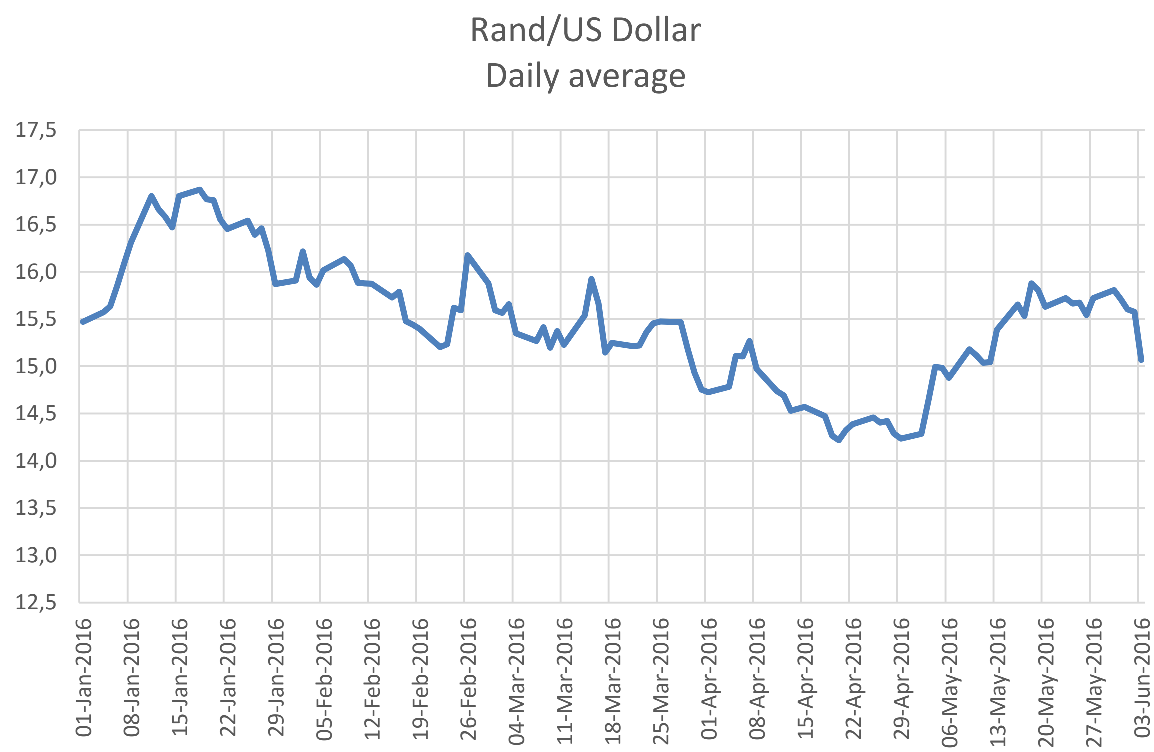
	2013 Annual	2014 Annual	2015 Annual	1st Quarter 2015	2nd Quarter 2015	3rd Quarter 2015	4th quarter 2015	1st Quarter 2016
Agriculture, forestry and fishing	1.5%	5.6%	-8.4%	-11.28%	-20.38%	-11.83%	-6.73%	-6.47%
Mining and quarrying	4.0%	-1.6%	3.0%	12.70%	-7.80%	-10.51%	1.45%	-18.07%
Manufacturing	0.7%	0.0%	0.1%	-2.14%	-6.32%	4.71%	-2.49%	0.57%
Electricity and water	-0.6%	-0.9%	-1.0%	4.59%	-6.88%	-7.15%	0.96%	-2.78%
Construction	2.7%	2.9%	1.9%	2.78%	1.62%	1.23%	1.44%	0.52%
Wholesale and retail trade; hotels and restaurants	1.9%	1.3%	1.4%	3.19%	-0.85%	1.25%	2.60%	1.28%
Transport and communication	2.0%	2.3%	1.4%	0.78%	0.08%	0.00%	-0.29%	-2.71%
Finance, real estate and business services	3.0%	2.2%	2.8%	2.87%	2.31%	2.54%	1.70%	1.90%
General government services	3.1%	3.0%	0.9%	-0.49%	0.88%	1.28%	1.18%	1.09%
Total value added at basic prices	2.3%	1.6%	1.2%	1.76%	-1.71%	0.26%	0.64%	-1.18%
Taxes less subsidies on products	1.3%	1.1%	1.7%	4.39%	-5.08%	0.12%	-1.50%	-1.86%
GDP at market prices	**2.2%**	**1.5%**	1.3%	**2.0%**	**-2.0%**	**0.3%**	**0.4%**	**-1.2%**

Headline inflation breached the upper 6 percent target in January 2016 and reached 7.0 percent by February 2016, before slowing to 6.2 percent in April 2016. According to BER's inflationary expectation survey, financial analysts expect inflation to average 6.4 percent this year, in line with the current inflationary trend, but slow to an average of 5.7 percent in the next two years. Inflation is currently fuelled by the nationwide drought, pushing food prices higher, while the weaker currency elevated import prices. Collective bargaining in the public sector is also adding to the inflationary pressures.



Brent crude oil prices collapsed in the second half of 2014, reaching a low of $33/barrel in December 2015. Oil prices are expected to remain subdued in view of weak global growth and an increase in supplies from the US. Lower oil prices have a direct impact on inflation. However, the benefit of the lower oil price to the South African economy has been diluted due to the increase in fuel levies imposed in April 2015 and again in April 2016, as well as currency weakness. The price of Brent crude oil did however recover to an average of $47.6/barrel in May 2016, the highest level since October 2015 ($49/barrel).

Following the rocky start to the year, the exchange rate recovered to R14.2/$ by end of April after reaching close to R17/$ around the 15th of January 2016. During the month of May there was some rand weakness and the currency depreciated to R15.8/$ in anticipation of a possible downgrade by S&P, which was narrowly avoided this time around. Following the announcement by Standard & Poor's (S&P) that South Africa will not be downgraded on the 3rd of June, although the outlook remains negative, the currency gained some ground and recovered to R15.0/$. However, the currency will remain vulnerable to any developments that could distract government from meeting their financial targets, as well as political instability and global developments.



The SARB leading indicator showed no real improvement after the 2010 World Cup, and started to decelerate at a faster pace from 2012. Because of the close correlation between SARB's leading indicator and GDP growth, the slowdown in the SARB's index implies further pressure on the economy. This indicator is now at the lowest level since 2009, and suggest possible further weakening in economic activity.

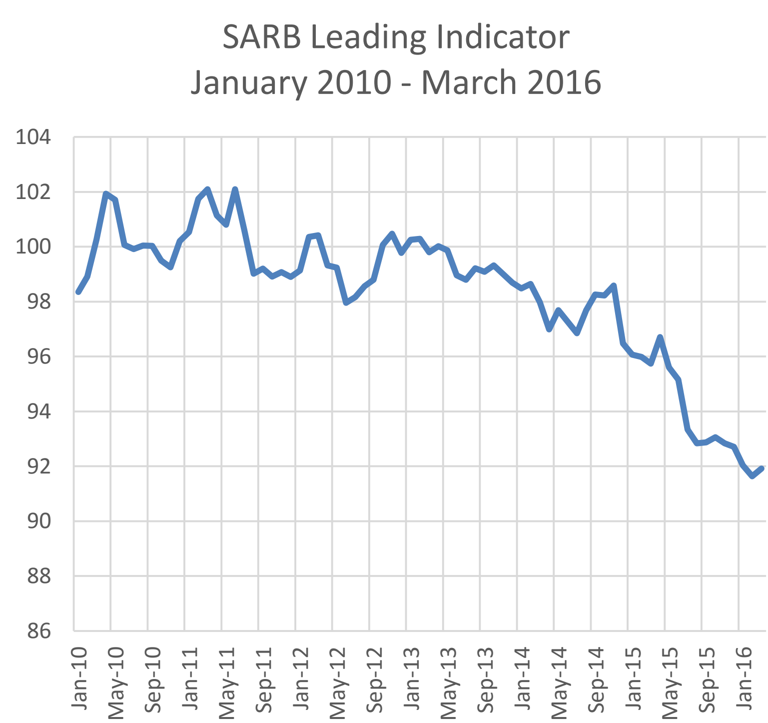


Figure 2: SARB leading indicator

Note: The leading business cycle indicator is a composite index comprising of time series, which tend to shift direction in advance of the business cycle.

Table 2: Macroeconomic performance and projections (Source Industry Insight estimates)

Macro-Economic Forecasts	2013	2014	2015	2016f	2017f	2018f
GDP	2,2%	1,5%	1,3%	0,8%	1,2%	2,2%
Household consumption	2,9%	1,4%	2,2%	0,5%	1,8%	2,7%
Government consumption	3,3%	1,9%	2,0%	0,7%	0,7%	1,0%
Gross Fixed capital formation	7,6%	-0,4%	2,3%	-0,5%	0,2%	2,1%
Imports	1,8%	6,0%	6,4%	2,5%	3,8%	5,0%
Exports	4,6%	4,5%	3,0%	3,5%	4,0%	4,7%
Prime Rate	8,50%	8,50%	9,25%	10,75%	11,50%	11,50%
Rand/Dollar	8,21	9,70	10,80	16,0	15,7	16,3
CPI Inflation	5,80	6,20	5,20	6,20	6,00	5,80
Current Account Deficit	-5,2	-5,9	-5,5	-5,1	-5,3	-6,3

THE POSITION OF THE CIVIL ENGINEERING INDUSTRY

Background

- Questionnaires were distributed to all SAFCEC members during May 2016.
- It is important to increase the usability of the industry report for all SAFCEC members, including small, medium and large enterprises. For this reason more focus is given to the developing trends within the defined employment categories. The categories are as follows:
    - Small : Employing less than 100 people
    - Medium: Employing between 100 and 1000 people
    - Large: Employing more than 1000 people
- Responses are weighted according to employment only where applicable. Comparisons between the different firm-size categories are not weighted as responses between the firm sizes have already been categorised.

Sample profile

Survey participation rose by 21 percent in the 2nd quarter of 2016, due to an increase in participation by larger companies. Larger firms contributed 52 percent to the 2nd quarter survey (from 42 percent in the previous survey), medium size firms 22 percent and smaller firms 26 percent.

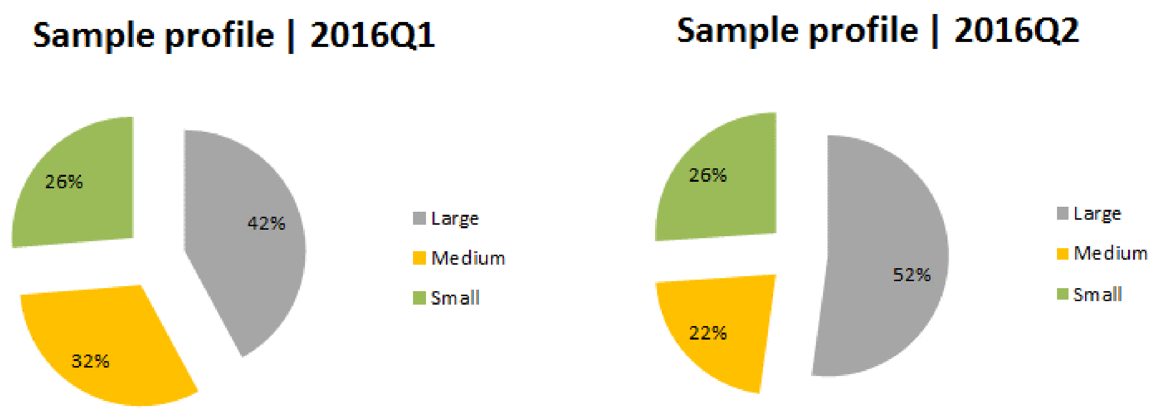


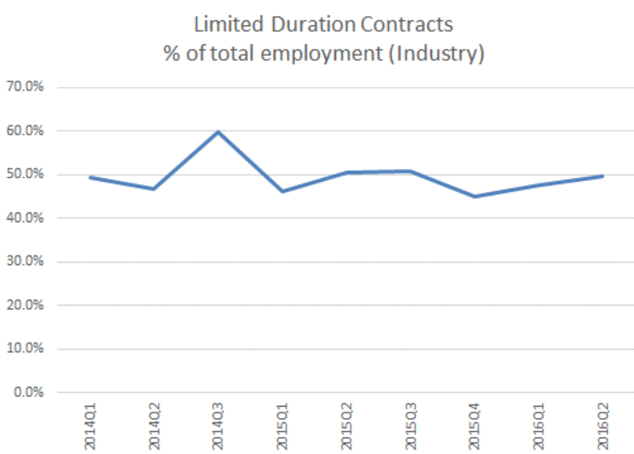
Figure 3: Profile of respondents

Key observations

Human Resources

- Employment fell by 1.0 percent q-q in the 1st quarter of 2016, following a decrease of 5.9 percent, and 8.3 percent in the previous two quarters. Both large and medium size firms reported a drop in employment, (down 1.0 percent and 3.5 percent respectively), while smaller firms reported an increase of 32.4 percent since the last quarter of 2015.
- Limited duration employment did however increase, up 2.2 percent q-q, due to a 2.5 percent increase reported by larger firms, and a 64 percent increase reported by smaller firms. Employment of limited duration employees by medium size firms fell by 6.7 percent since the 4th quarter of 2015.
- Employment of permanent employees contracted by 3.6 percent q-q, due to 4.0 percent decrease reported by larger firms. Both medium and smaller firms reported a small increase in permanent employees, up 0.6 percent and 1.7 percent respectively.
- Limited duration contributed 49.6 percent of total employment in the 1st quarter of 2016, compared to 47.6 percent in the 4th quarter of 2015. In larger firms limited duration contributed 49 percent, slightly higher compared to the last survey. Medium size firms were represented by 54 percent (slightly lower than last survey of 60 percent but still higher compared to the 35 percent in the 3rd quarter of 2015), whereas smaller firms reported the highest contribution of 61 percent.

Firm Size Category	*Limited Duration*	*Permanent Employees*	*Total*	*% Limited Duration of total workforce*
Large	2.5%	-4.0%	-0.9%	49.0%
Medium	-6.7%	0.6%	-3.5%	54.0%
Small	64.1%	1.7%	32.4%	61.0%
Total	2.2%	-3.6%	-0.8%	49.6%



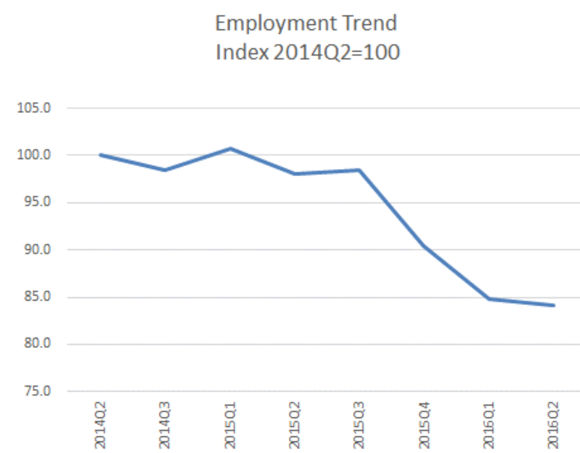
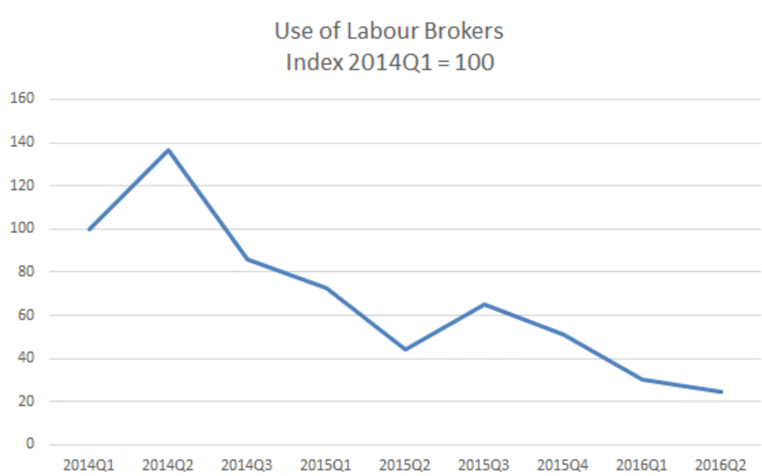


Figure 5: Employment trend Index 2014Q2



- Labour brokers represented 4 percent of the total workforce, well below the trend in the last few years, but has increased from 3 percent in the 4th quarter of 2015. Medium and small size firms did not report any use of labour brokers in the past two surveys. The use of labour brokers by larger firms rose by 29 percent q-q, following a decrease of 17 percent in the previous quarter.

Financial Statistics

Turnover, Wages and Order Books

- The total value of civil engineering construction certified for payment fell by 8 percent q-q in the 1st quarter of 2016, following the decrease of 11.5 percent in the 4th quarter of 2015 and a marginal increase of 0.5 percent in the 3rd quarter.
- Larger firms reported a 8.5 percent decrease (following the 12.5 percent decrease in the previous quarter), while medium size firms fell by 19 percent after having reported no change in the previous quarter. Smaller firms again reported a notable increase, of 195 percent, following the 32 percent increase reported in the previous survey.

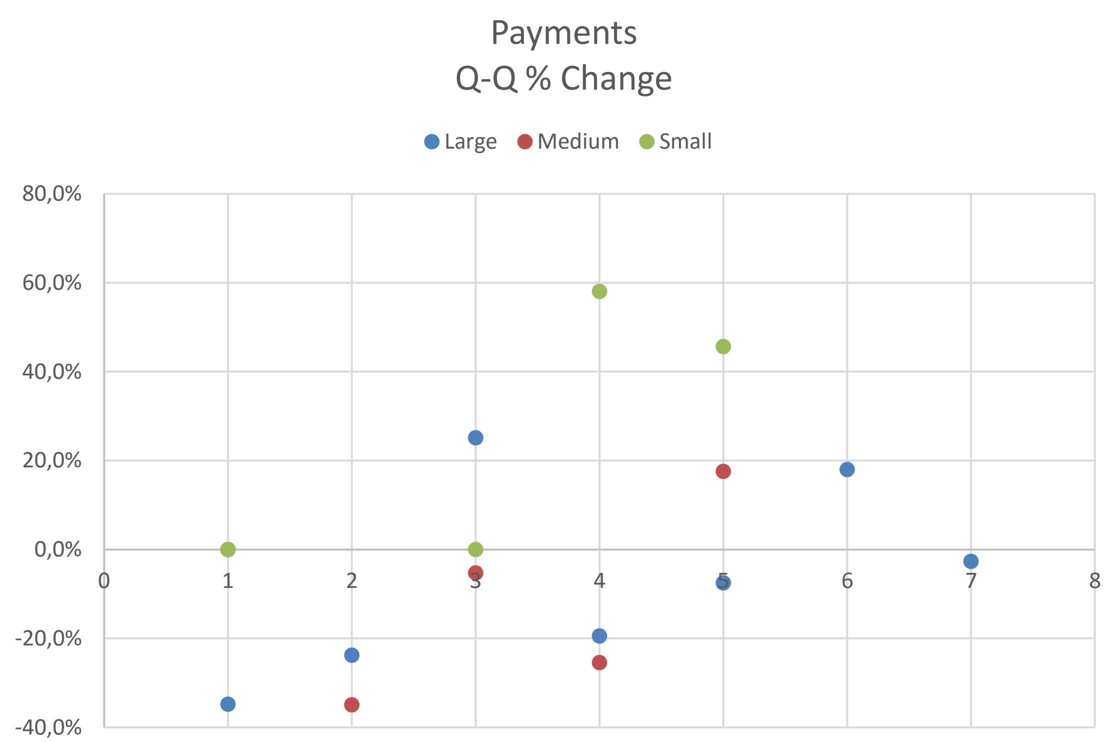


Figure 6: Civil Engineering certified payments, q-q percentage change, matrix

- The cumulative salary and wage bill represented 28 percent of total turnover, from 23 percent and 21 percent in the previous two quarters, but with some dubious results reported by the smaller firms. However, due to its size it has no real impact on the overall trend.
- Although employment fell in the 1st quarter, the salary and wage bill increased by 1 percent, with a 3.4 percent increase reported by larger firms. Medium size firms reported a 28 percent drop in their salary and wage bill (alongside a 3.5 percent contraction in employment), while smaller firms also reported a decrease of 14.5 percent in their salary and wage bill, although employment has reportedly increased.
- On the upside, the value of the two-year forward order book rose 5 percent q-q in the 1st quarter of 2016, following the 14 percent decrease reported in the previous quarter. All firm categories reported an increase,

with a 5 percent increase reported by larger firms, a 23 percent increase reported by medium size firms and a 120 percent increase reported by smaller firms. Smaller firms don't generally report on order book values, and may therefore be somewhat distorted by a limited response rate.

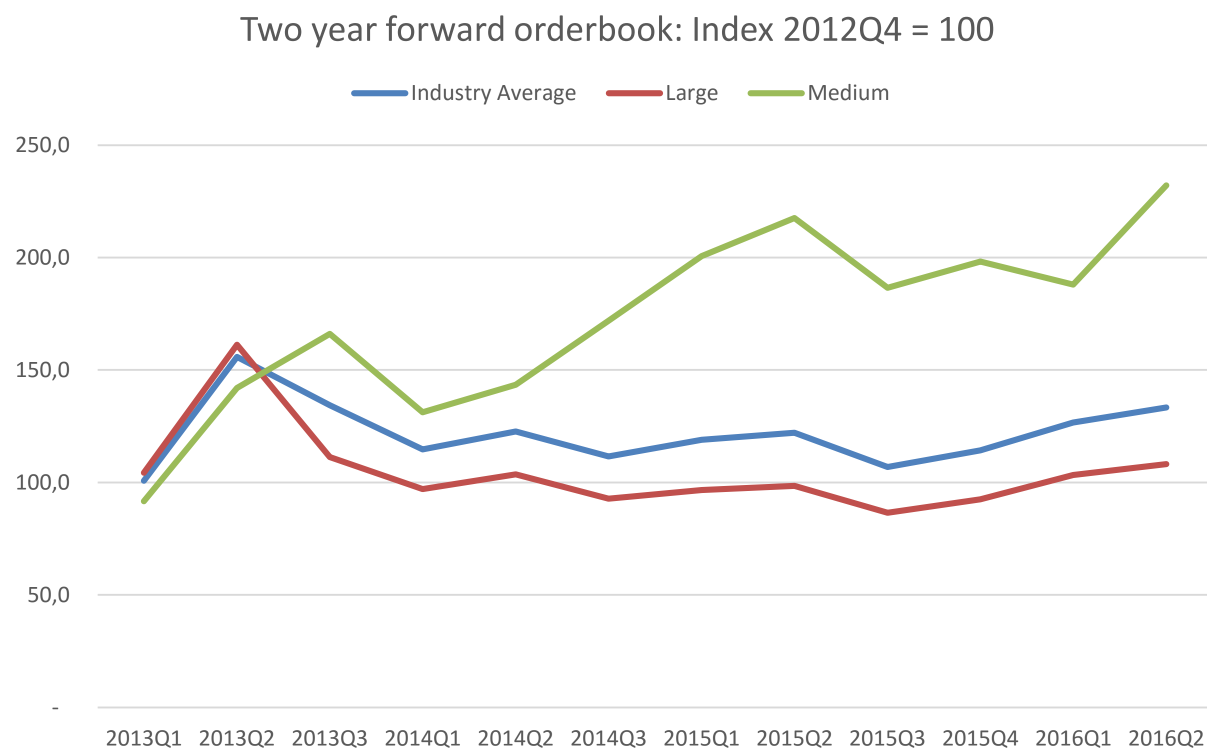


Figure 7: Value of two year forward order book, Index 2012Q4=100

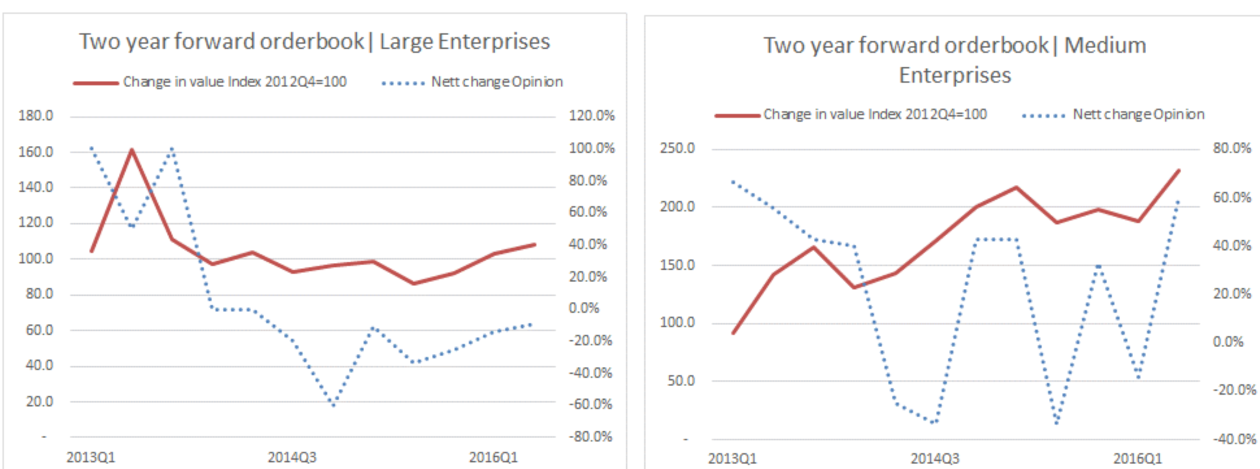
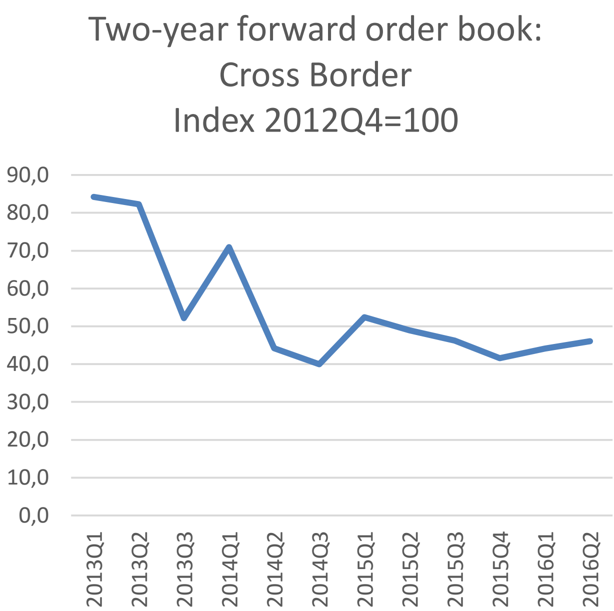
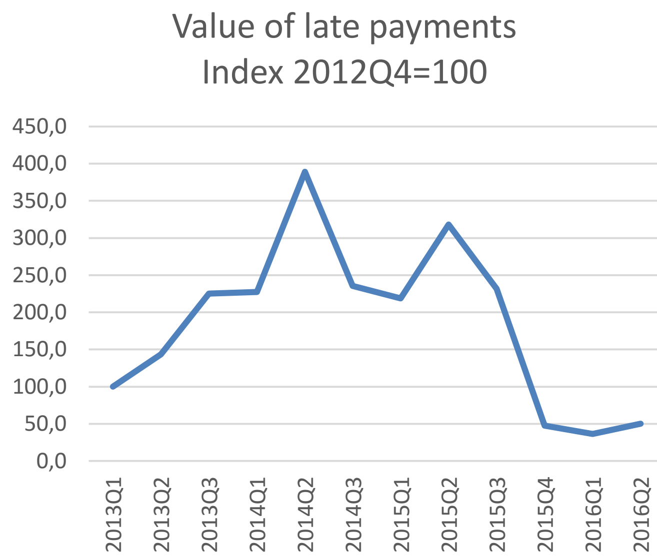


Figure 8: Two year forward order book, Large vs Medium Enterprises

- The order book for activities outside of RSA rose 4 percent q-q, from a revised 6 percent increase in the previous quarter. This is the second consecutive increase in the value of cross border order book. The index has been on a decline since 2013 but is currently showing some signs of stabilising.





Late Payments

- After having shown relatively consistent improvement in the value of late payments reported by contractors, late payments increased more significantly this quarter, up 37 percent since the 4th quarter of 2015. The index measuring late payments peaked at 38.9 in the 2nd quarter of 2014, but improved to 36 in the previous quarter, before rising to 50 in the current survey.
- The rise in this quarter's survey was largely due to an increase in late payments reported by larger firms (up 38 percent – with majority of firms having reported an increase) while medium and smaller firms reported a decrease in late payments, down 3.7 percent and 42 percent respectively.
- The value of late payment as a percentage of turnover subsequently increased to 22 percent from 15 and 17 percent in the previous two quarters. Large firms reported an increase in the representation of late payments to 24 percent (from 15 percent), while medium and small size firms reported that late payments represented less than 8 percent of turnover. Late payments would include any payments outstanding for 30 days or more.

- Of those payments outstanding for more than 90 days, the private sector contributed 51 percent, followed by SOE's at 42 percent, provincial government at 4.7 percent and local government 1.6 percent. The good news is that none of the contractors reported on payments outstanding for longer than days from central government. .
- The value of payments outstanding for longer than 90 days represented 4.1 percent of turnover, affecting mainly the larger firms. Medium size firms reported 1.4 percent of turnover still outstanding after 90 days, while none of the smaller firms reported any payments outstanding for that period of time.
- The CIDB legislation regarding Prompt Payment Regulations were submitted for public comment in July 2015 and are expected to be finalised later this year, but doubts regarding the implementation of these new regulations are rising. According to the CIDB, the Prompt Payment Regulations have regrettably been delayed as the CIDB may face a possible constitutionality conflict should the regulations be published in its current form, as the CIDB Act / mandate does not explicitly make reference to issues of payment. The Office of the Chief State Law Advisor has advised accordingly in this regard. The CIDB is awaiting a ruling by the National Department of Public Works regarding the way forward, and will endeavour to put out a notification to industry once we are in receipt of same

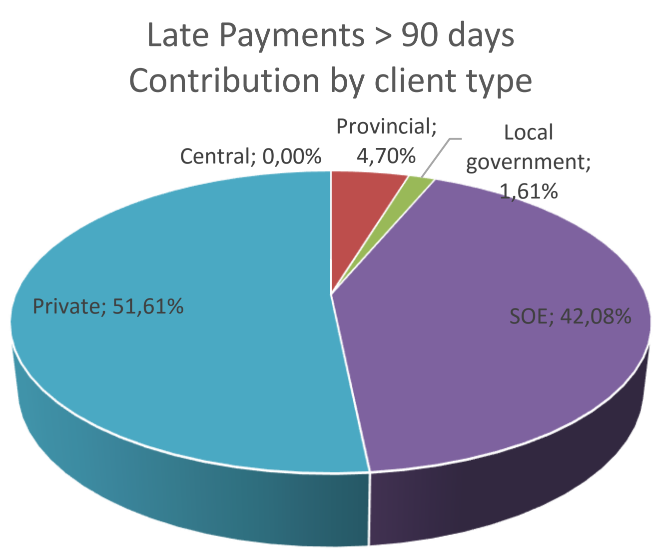


Figure 9: Late payments > 90 days, contribution by client

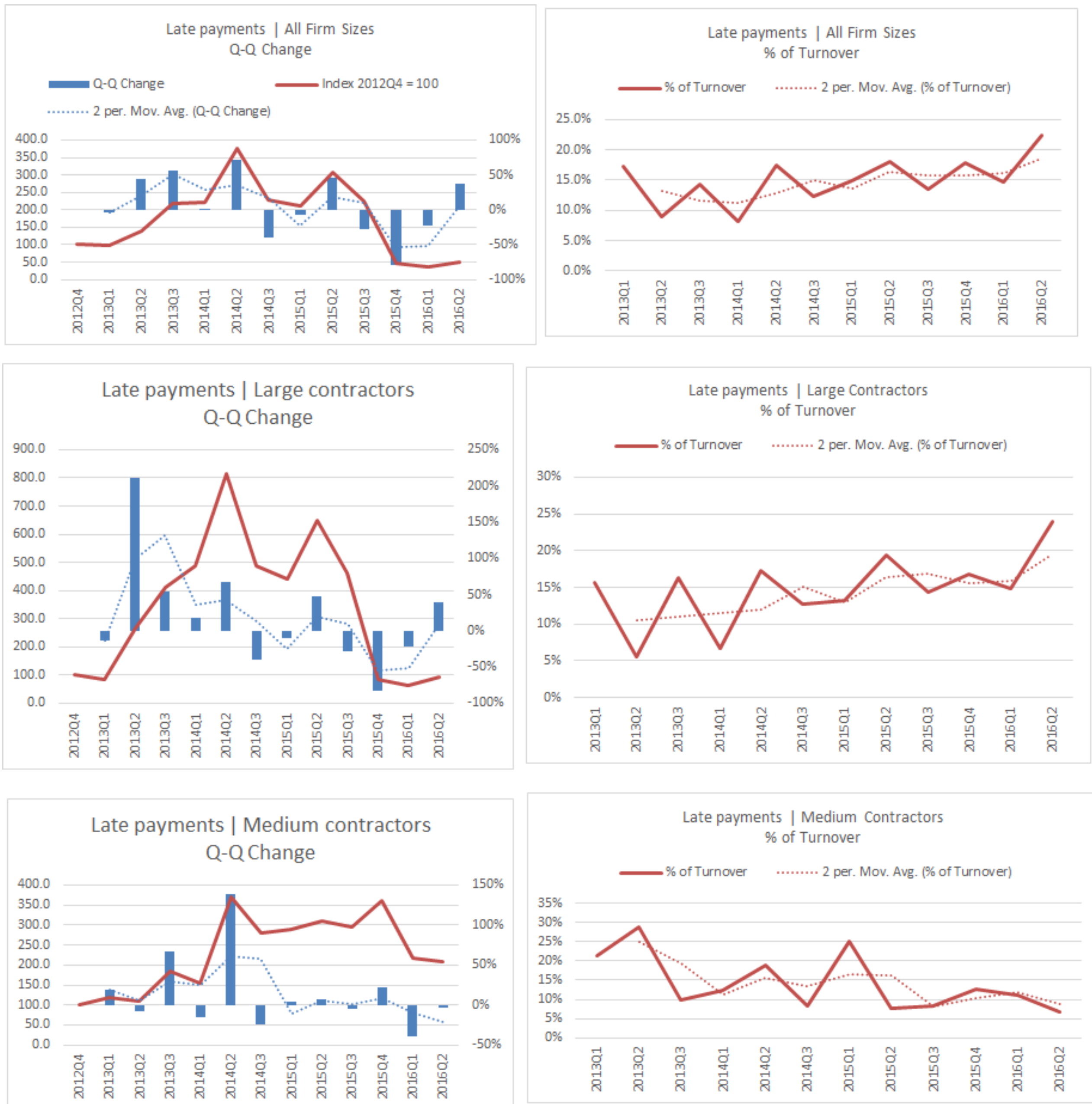


Figure 10: Late payments

Industry Profile

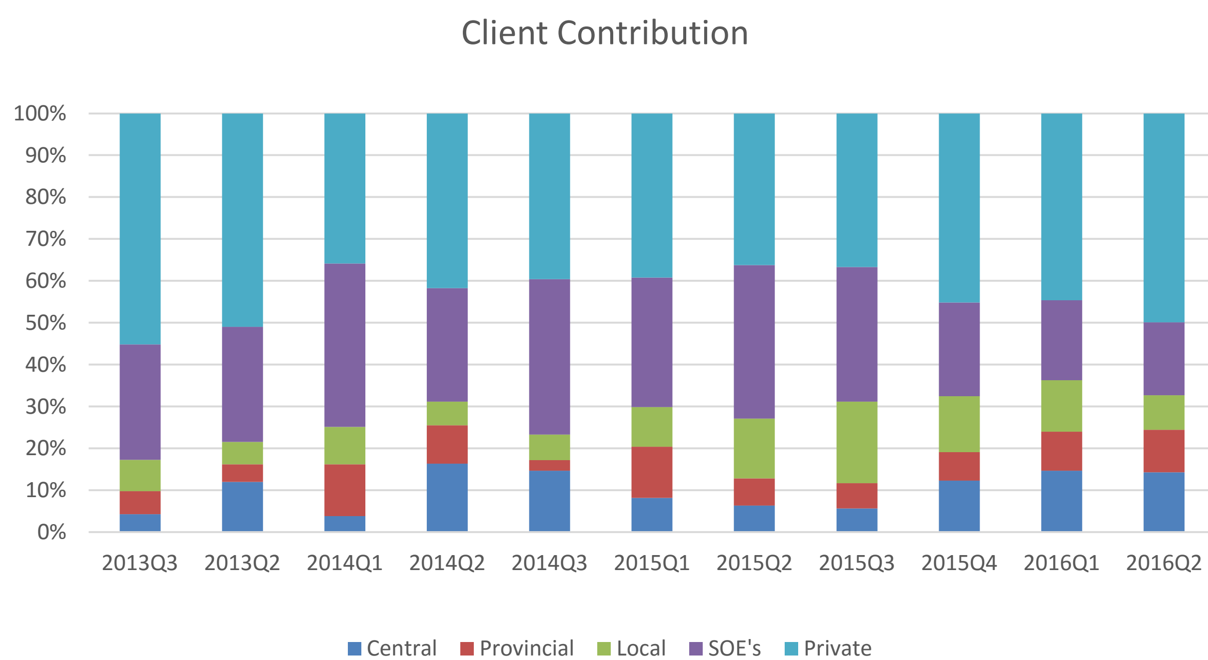
- The following section provides a snapshot view of responding firms' turnover earned by project type, client and province during the 1st quarter of 2016 (surveyed in the 2nd quarter of 2016). This is not necessarily representative of the entire industry, but again shows the significant contribution by the roads segment.
- In this survey, roads contributed 59.8 percent to total turnover, with medium size firms highly exposed to road contracts earning 74.2 percent of turnover from this market segment.
- Road works represent a significant portion of total payments received by the civil engineering contracting industry, and although the Department of Transport has increased its transfers to SANRAL over the medium term expenditure framework (MTEF) period (2016/17 – 2018/19), revenue constraints due to the lower than expected toll revenue collected, is likely to have a negative impact on new road projects announced by SANRAL over this period.

Table 3: Turnover distribution by sub-discipline

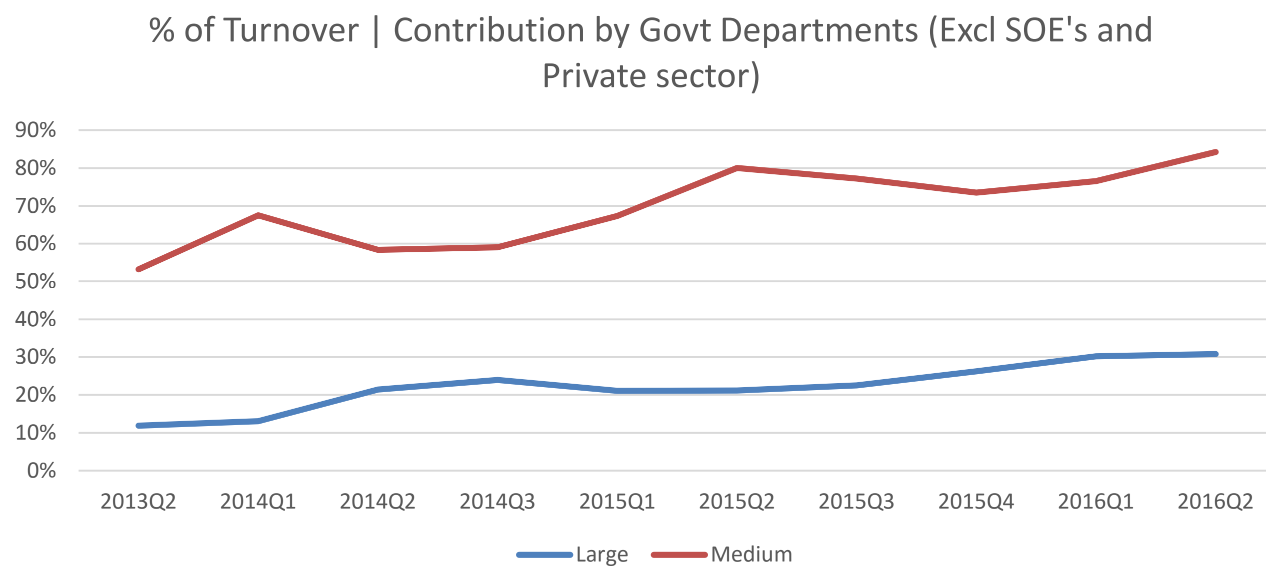
Discipline	Large	Medium	Small	Total 2015Q2	Total 2015Q3	Total 2015Q4	Total 2016Q1
Roads	60.0%	74.2%	4.5%	42.5%	45.7%	55.3%	59.8%
Earthworks	5.6%	6.7%	5.6%	5.6%	4.2%	3.5%	5.7%
Water Bulk Infrastructure	2.8%	8.9%	12.7%	9.6%	15.0%	2.6%	3.3%
Water and Sanitation	1.3%	10.2%	5.7%	6.7%	3.9%	3.6%	2.0%
Rail	0.6%	0.0%	0.0%	3.4%	2.1%	1.7%	0.6%
Harbours	2.3%	0.0%	0.0%	1.4%	1.1%	2.0%	2.1%
Power (bulk)	8%	0.0%	0.0%	12.3%	11.7%	15.0%	7.7%
Power (services)	5.1%	0.0%	0.0%	0.0%	1.7%	2.3%	4.7%
Airports	0.0%	0.0%	0.0%	0.0%	0.3%	0.2%	0.0%
Mining Infrastructure	3.3%	0.0%	15.5%	5.6%	5.2%	4.6%	3.4%
Mining (Surface earthworks)	1.5%	0.0%	0.0%	0.0%	0.6%	1.6%	1.4%
Other	9.0%	0.0%	56.1%	13.0%	8.6%	7.8%	9.4%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Table 4: Turnover distribution by client

	Large	Medium	Small	Total 2015Q2	Total 2015Q3	Total 2015Q4	Total 2016Q1
Central	13.4%	31.4%	0.0%	2.2%	12.3%	14.7%	14.3%
Provincial	10.1%	13.8%	2.9%	6.6%	6.8%	9.3%	10.1%
District/Local/Metropolitan Councils	6.1%	38.0%	16.5%	25.2%	13.4%	12.3%	8.3%
Parastatals	18.5%	7.3%	0.0%	35.7%	22.4%	19.0%	17.4%
Private	52.0%	9.6%	80.6%	30.3%	45.2%	44.7%	49.9%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%



- The contribution by the private sector in this survey increased to 50 percent, because of the higher exposure by the larger firms to private sector infrastructure. Medium size firms in this survey were more exposed to local government (compared to previous surveys where provincial government represented the largest share of turnover), while smaller firms surprisingly earned a higher portion of turnover from the private sector (in particular mining).
- In the 2016 Budget, infrastructure allocations to provincial government increased at a faster pace compared to allocations made towards local authorities. This is a significant change from the 2015 Budget where local government was earmarked to become the largest client to the construction industry by 2017/18.



Medium size firms are more actively involved in government departments, and will benefit from the medium term budget where government expenditure will increase at a stronger pace compared to spending by SOE's.

Table 5: Geographic distribution of the value of civil engineering construction work (turnover)

Province	Large	Medium	Small	2015Q2	2015Q3	2015Q4	2016Q1
GAU	21%	21%	7%	33%	23%	16%	21%
WC	10%	25%	0%	15%	12%	15%	11%
EC	9%	13%	20%	10%	8%	9%	10%
NC	5%	1%	0%	2%	4%	5%	5%
MPU	14%	18%	0%	11%	18%	18%	14%
FS	10%	0%	0%	6%	11%	6%	9%
LIM	5%	0%	67%	12%	8%	7%	6%
NW	5%	0%	0%	1%	5%	2%	5%
KZN	20%	21%	4%	9%	12%	23%	20%
Total	100%	100%	100%	100%	100%	100%	100%

- Gauteng contributed 21 percent to this survey, followed by 20 percent in KwaZulu-Natal, 14 percent in Mpumalanga, 11 percent in Western Cape and 10 percent in the Eastern Cape. Larger firms reported a more diverse geographical profile of turnover, while medium size firms were most active in Western Cape, Gauteng and KwaZulu-Natal. Because of the influence of the private mining sector, smaller firms had the highest share in Limpopo in this quarter's survey.

Economic Indicators

Economic indicators generally depict the "opinions" of respondents related to work conditions, tempo of work activity, competition for tenders, profitability and prices. It measures contractors' sentiment during the survey period (2nd quarter 2016).

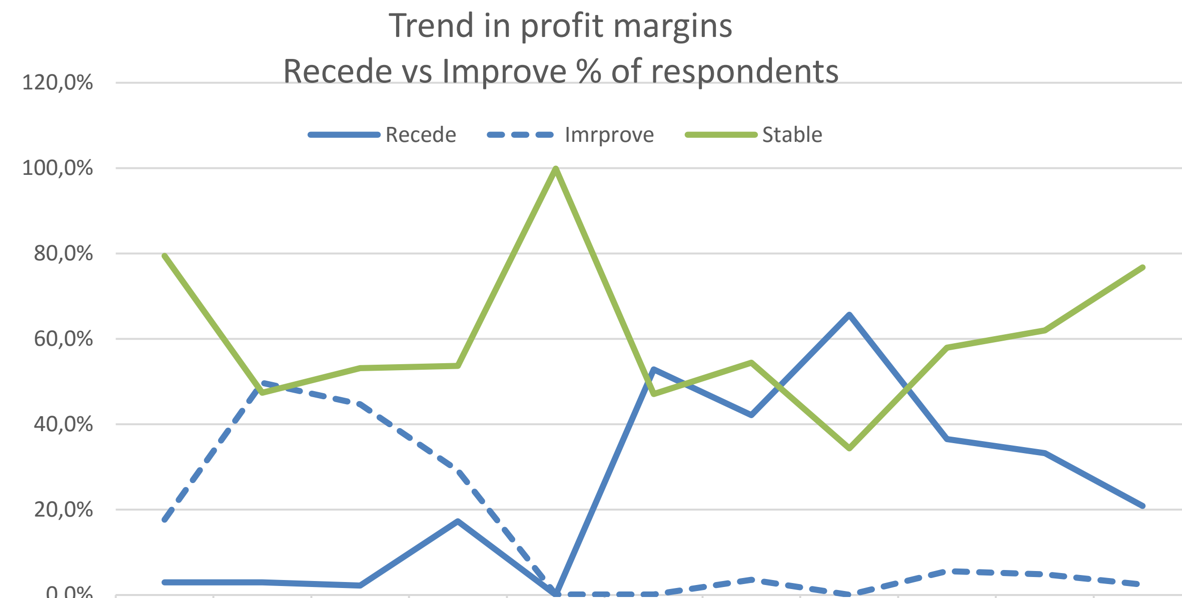
The mostly negative market sentiment continued to prevail since 2009, and although the level of sentiment expressed by respondents reached new lows during the 2nd quarter of 2015 there was a marginal improvement in the 4th quarter, but not enough to lift the overall sentiment out of the red. The outlook for the next quarter however remains deeply concerning.

A positive rate implies more firms reported improved business conditions, while a negative rate implies majority of firms reported a more pessimistic outlook on the industry.

Please note that these calculations are weighted according to a firm's total reported work force in RSA.

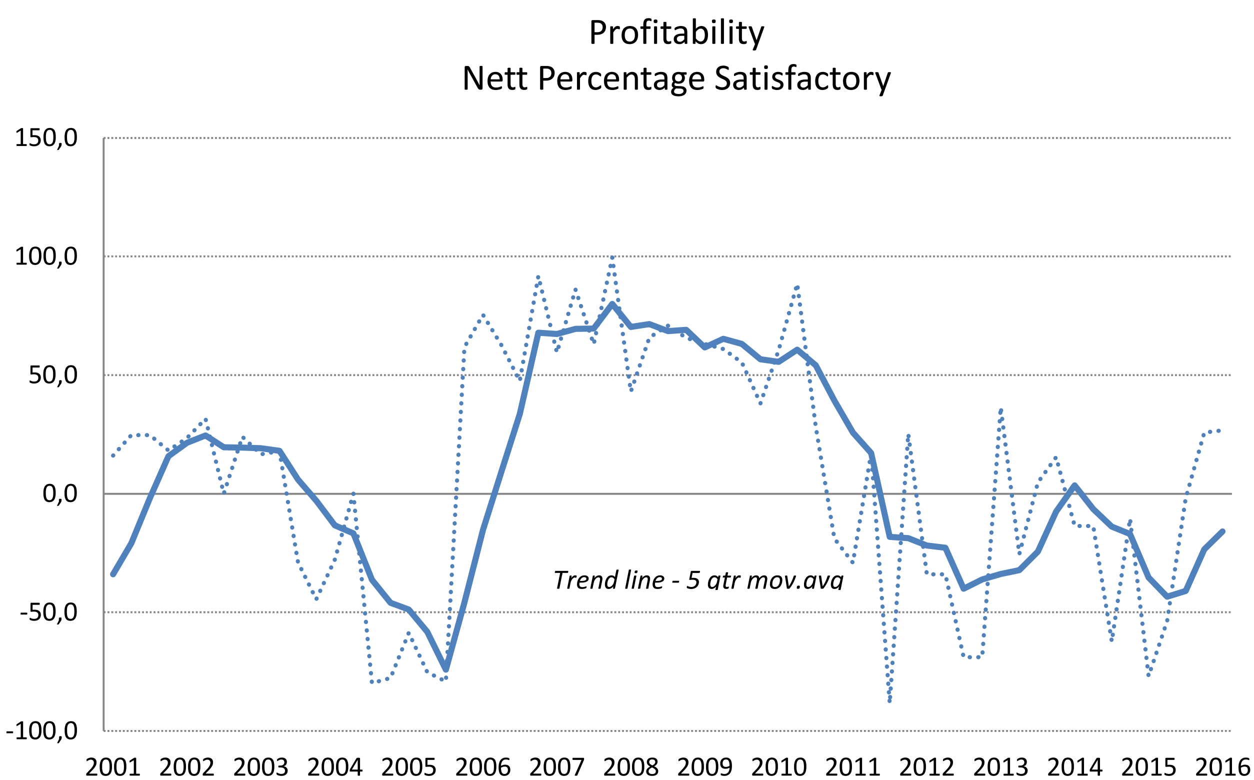
- **The nett % satisfied with working conditions** during the 1st quarter of 2016 (past quarter), remained in deep negative territory -50.0, although this was an improvement from -52.9, and -60,8 reported in the previous two surveys. 22 percent of respondents reported very quiet conditions, with a marginal improvement expected for the current quarter (2nd quarter of 2016) as 18 percent reported on very quiet conditions. Majority of contractors reported quiet conditions for the 1st quarter (36 percent) and this follows through to the 2nd quarter of 2016.
- Of concern is the increase in the number of contractors expecting very quiet conditions in the next quarter, up from 18 percent to 25 percent, suggesting a weaker business environment in the next 3 to 6 months.
- **Competition for tenders** remain fierce. 70 percent of the contractors said that there were more than 11 bids per contract, and this rises to 80 percent when focussed on the larger firms.
- **Tender prices** remain under pressure, although fewer contractors (40 percent compared to 41 percent, and 48 percent in the previous two surveys) reported very low prices. Again, the larger firms are more severely affected as 60 percent of the larger firms reported very low prices, compared to on average 20 percent of the medium and smaller size firms.
- Larger firms have seemingly become more comfortable with the (lower) levels of profitability, as 50 percent reported satisfactory levels, a sentiment not shared by medium or smaller contractors. Majority of medium size firms (60 percent) reported low profitability while 33 percent of smaller firms also felt profitability levels were low.
- Majority of contractors (supported mainly by medium size contractors) expect profitability trends to stabilise (52 percent), while less than 5 percent expect improved margins.

- Around 30 percent of the larger firms expect a further deterioration in profitability, while 70 percent expect it to stabilise.
- The overall nett-satisfaction rate improved from 25.7 percent in the previous quarter to 26.7 percent. The second consecutive quarter of positive nett satisfaction rates since 2014 and an improvement on the more dismal sentiment expressed during 2015. However, based on the responses, the likelihood of a recovery in margins is unlikely.

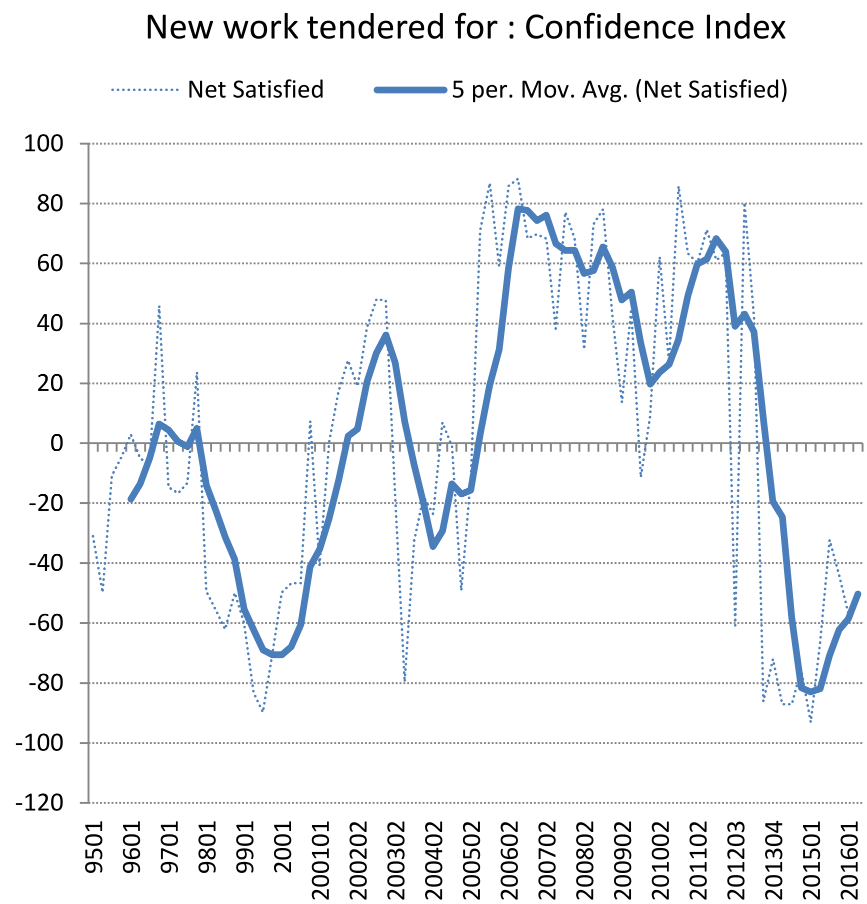


	2013Q2	2013Q3	2014Q1	2014Q2	2014Q3	2015Q1	2015Q2	2015Q3	2015Q4	2016Q1	2016Q2
Recede	3,0%	2,9%	2,2%	17,2%	0,0%	52,9%	42,1%	65,7%	36,5%	33,2%	20,9%
Imrprove	17,6%	49,7%	44,7%	29,1%	0,1%	0,1%	3,5%	0,0%	5,6%	4,8%	2,4%
Stable	79,4%	47,3%	53,1%	53,6%	99,9%	47,1%	54,4%	34,3%	57,9%	62,0%	76,8%

Figure 11: Opinions related to Profitability



Opinions related to tenders, awards, order books and turnover



Explanatory note: Tender activity is a crucial indicator, being a first warning of the potential volume of work. The confidence reflected by companies regarding this indicator is therefore crucial and often deviates from the actual physical number of tenders during a period. The rate of involvement in cross border activity of larger contractors has increased in recent quarters, to counter act the impact of the dearth in work opportunities domestically in which they can compete. Some larger companies recently announced that the percentage contribution of work outside of South Africa is larger than revenue generated inside the country. Because these indicators are weighted, the opinions and perceptions of larger firms impacts quite heavily on the overall trend, and the impact of "cross border" activity must not be undermined in the movement of these indices.

Tender activity

Figure 12: Opinions of new work tendered for

- The negative sentiment towards tenders continued in this survey, although there was a slight improvement in the negative nett satisfaction rate from -57.0 percent in the previous survey to -51.9 percent. This is mainly as a result of 75 percent contractors reporting on low tender volume conditions (compared to 78 percent in the previous survey) while 21 percent felt that tender activity was satisfactory (compared to 8 percent in the previous survey).
- There was some improvement in the estimated value of tenders published during the 1st quarter of 2016, which increased by 32.9 percent y-y compared to the first quarter of 2015. This follows a nominal decrease of 5.6 percent y-y during 2015. The higher values in the 1st quarter of 2016 was supported by a 85 percent increase in the value of road projects out to tender, while the estimated value of water projects were down by 10 percent. The weaker performance in tender values in 2015 (and in particular the 11 percent y-y decline in Q4) suggests weaker performance in construction activity in 2016. Estimated tender values of road projects fell 1 percent y-y while the value of water projects declined by 18 percent. Please note that this does not include mining infrastructure or bulk infrastructure projects.

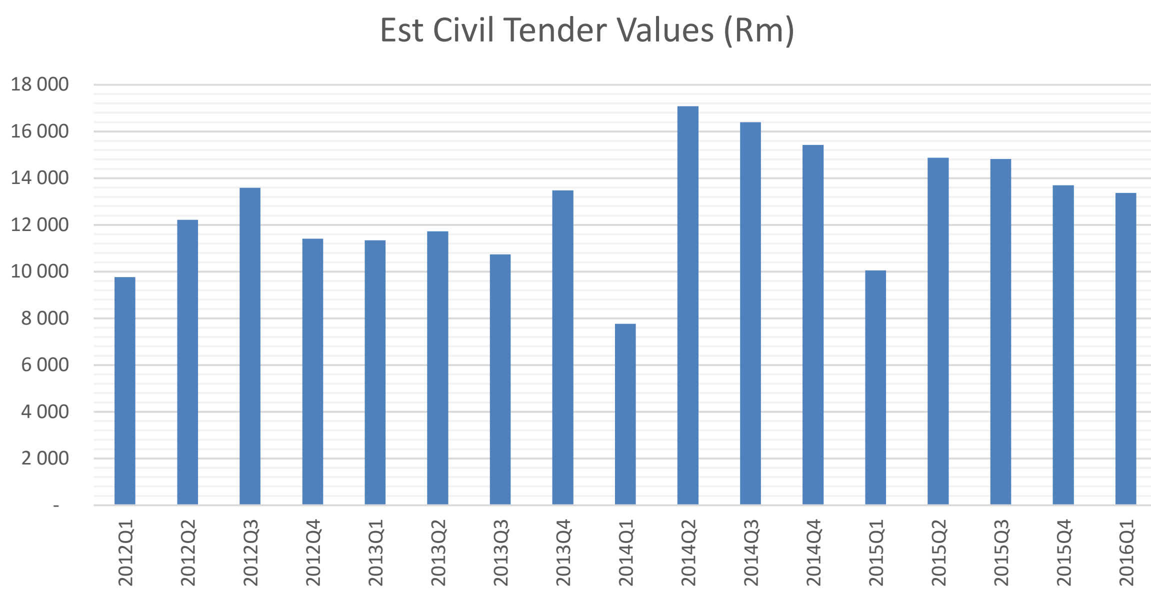


Figure 13: Estimated Tender Values (RM)

Table 14: Estimated civil tender values, by project type, by quarter (Rm, current prices- not adjusted for inflation)

Source: Industry Insight Project Database, Databuild

	Air	Bridges	Civil Other	Power	Rail	Road	Water	Grand Total	Y-Y Per. Change (Nominal)
2013Q2	24	107	1,023	578	184	5,153	4,658	11,726	-4.1%
2013Q3	18	102	205	334	0	5,676	4,403	10,738	-21.0%
2013Q4	4	73	185	288	-	9,662	3,261	13,473	18.1%
2014Q1	-	287	423	285	9	3,886	2,871	7,760	-31.5%
2014Q2	4	232	432	456	97	8,270	7,584	17,074	45.6%
2014Q3	129	211	534	600	121	8,174	6,620	16,389	52.6%
2014Q4	-	306	489	366	104	7,668	6,489	15,421	14.5%
2015Q1	16	192	553	455	152	4,205	4,486	10,059	29.6%
2015Q2	102	467	418	476	153	9,252	4,006	14,875	-12.9%
2015Q3	128	380	388	765	108	8,924	4,129	14,822	-9.6%
2015Q4	4	492	365	700	277	5,245	6,615	13,697	-11.2%
2016Q1	-	467	495	516	50	7,789	4,048	13,364	32.9%

Awards

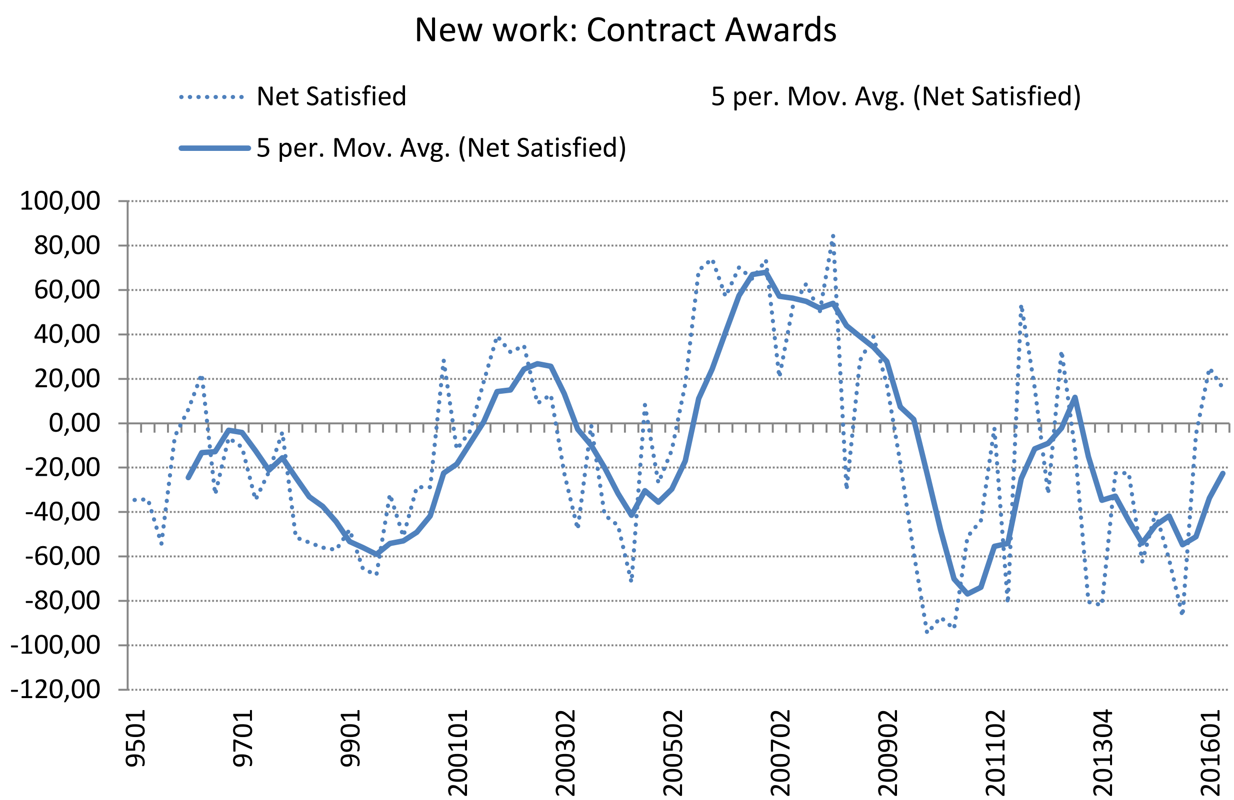
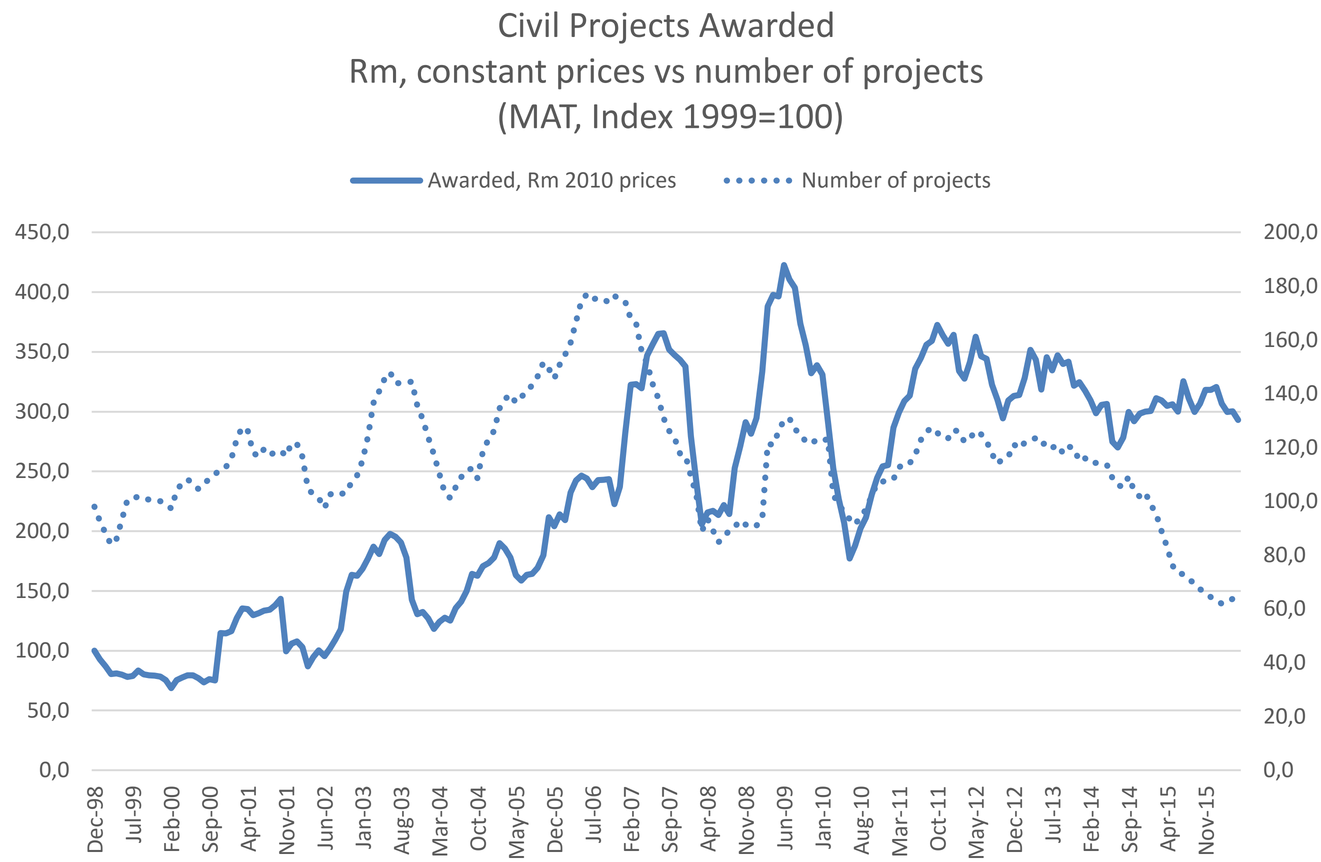
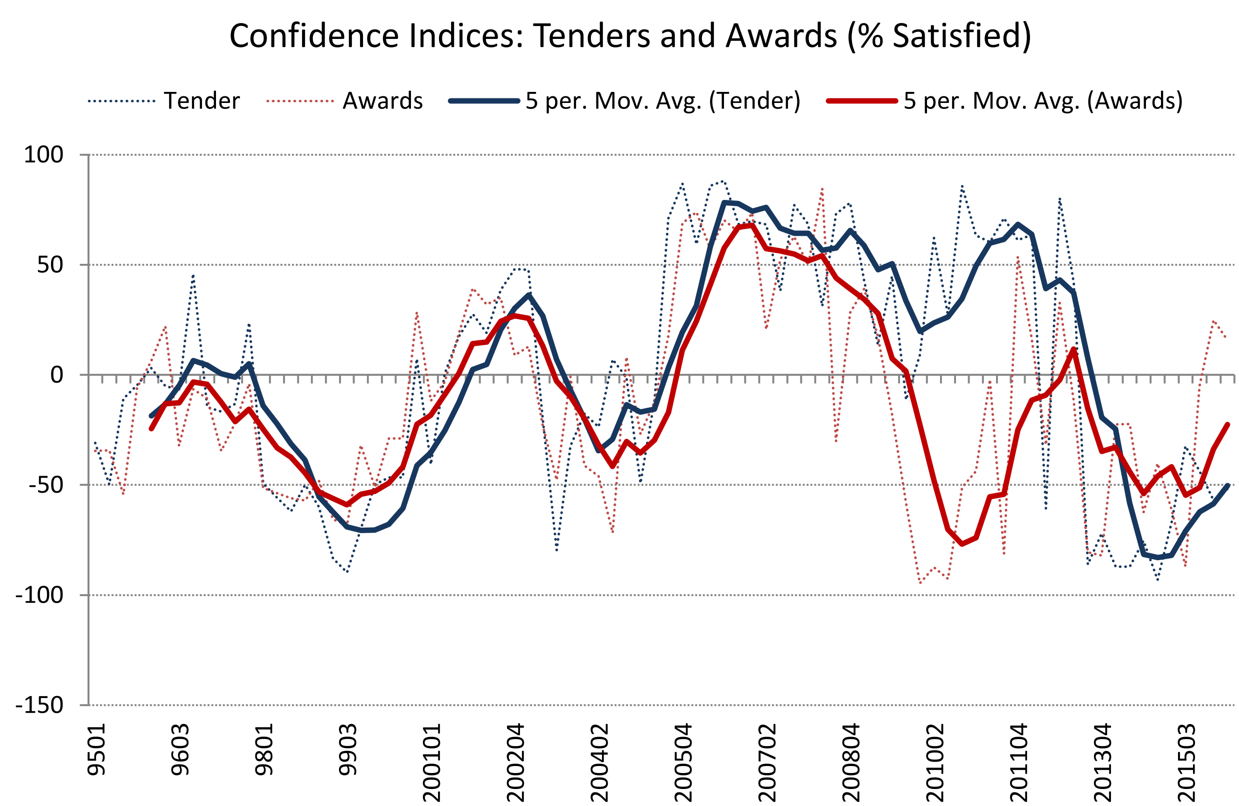


Figure 14: Opinions related to Awards

- The nett satisfaction rate regarding opinions related to the awarding of contracts improved to 24.9 in the previous survey, after several quarters of negative nett satisfaction rates, and although it maintained a positive rate, it slowed to 15.8 percent in the current survey. The trend over the last five quarters remain in the red, due to the high levels of negativity over the last since 2012 and the slow pace of recovery.
- The nominal value of civil contracts awarded increased by 4 percent y-y in the 1st quarter of 2016, following the 10 percent y-y increase reported in 2015, coming off a low base in 2014. Values for April and May suggest a weaker performance in the 2nd quarter with no growth thus far reported (for the first two months of the 2nd quarter of 2016) in the nominal value of civil contracts that have been awarded.
- During the same quarter the number of civil projects awarded fell by 8 percent y-y in the 1st quarter of 2016. However the first two months of the 2nd quarter has shown a more robust increase of 26 percent y-y compared to the same two months in 2015 (April and May). Although the annual growth in the award index remains negative over the last 12 months, the rate of decline has slowed from 38 percent y-yin 2015 to -15 percent y-y in the 12 months up to May 2016.


Civil Projects Awarded
Rm, constant prices vs number of projects
(MAT, Index 1999=100)
Awarded, Rm 2010 prices
Number of projects
450,0
400,0
350,0
300,0
250,0
200,0
150,0
100,0
50,0
0,0
200,0
180,0
160,0
140,0
120,0
100,0
80,0
60,0
40,0
20,0
0,0
Dec-98
Jul-99
Feb-00
Sep-00
Apr-01
Nov-01
Jun-02
Jan-03
Aug-03
Mar-04
Oct-04
May-05
Dec-05
Jul-06
Feb-07
Sep-07
Apr-08
Nov-08
Jun-09
Jan-10
Aug-10
Mar-11
Oct-11
May-12
Dec-12
Jul-13
Feb-14
Sep-14
Apr-15
Nov-15


Confidence Indices: Tenders and Awards (% Satisfied)
Tender
Awards
5 per. Mov. Avg. (Tender)
5 per. Mov. Avg. (Awards)
100
50
0
-50
-100
-150
9501
9603
9801
9903
200101
200204
200402
200504
200702
200804
201002
201104
201304
201503

Order books

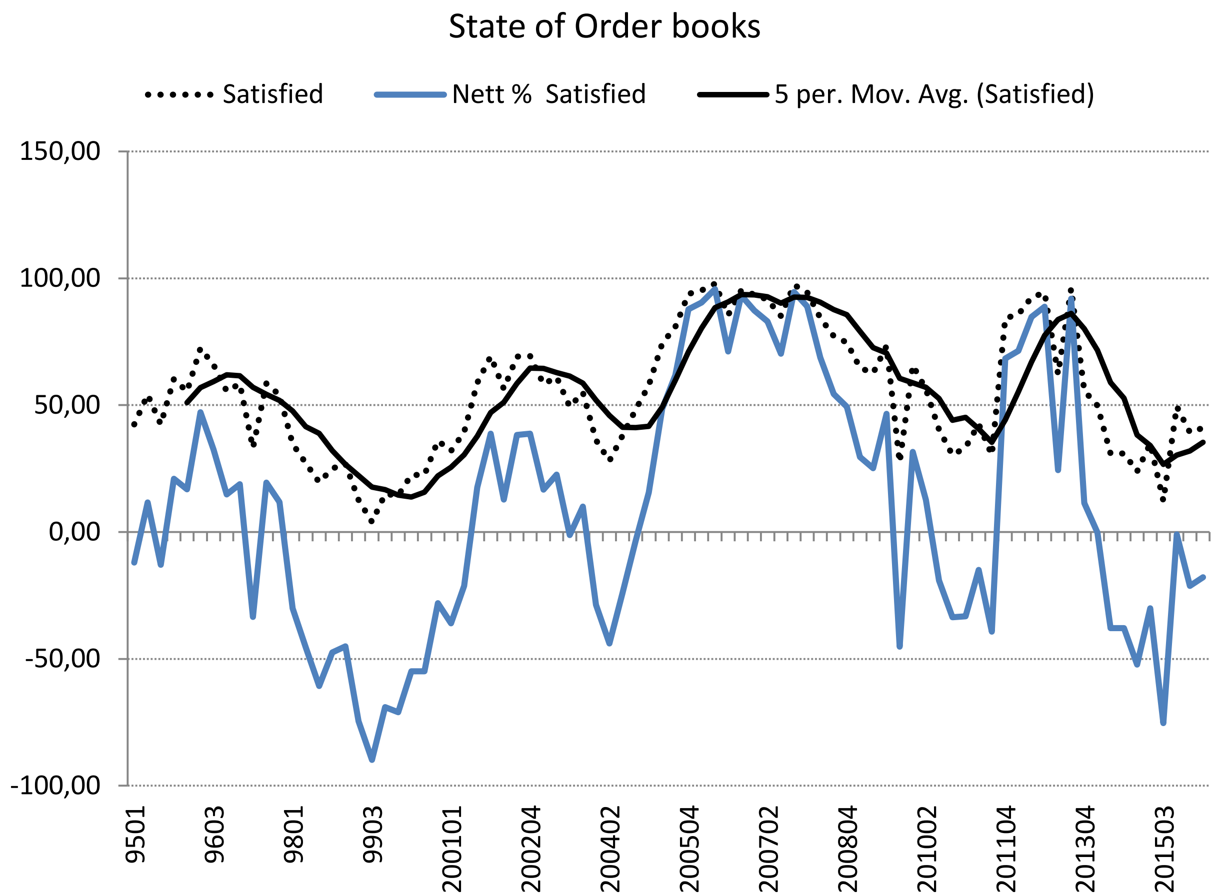
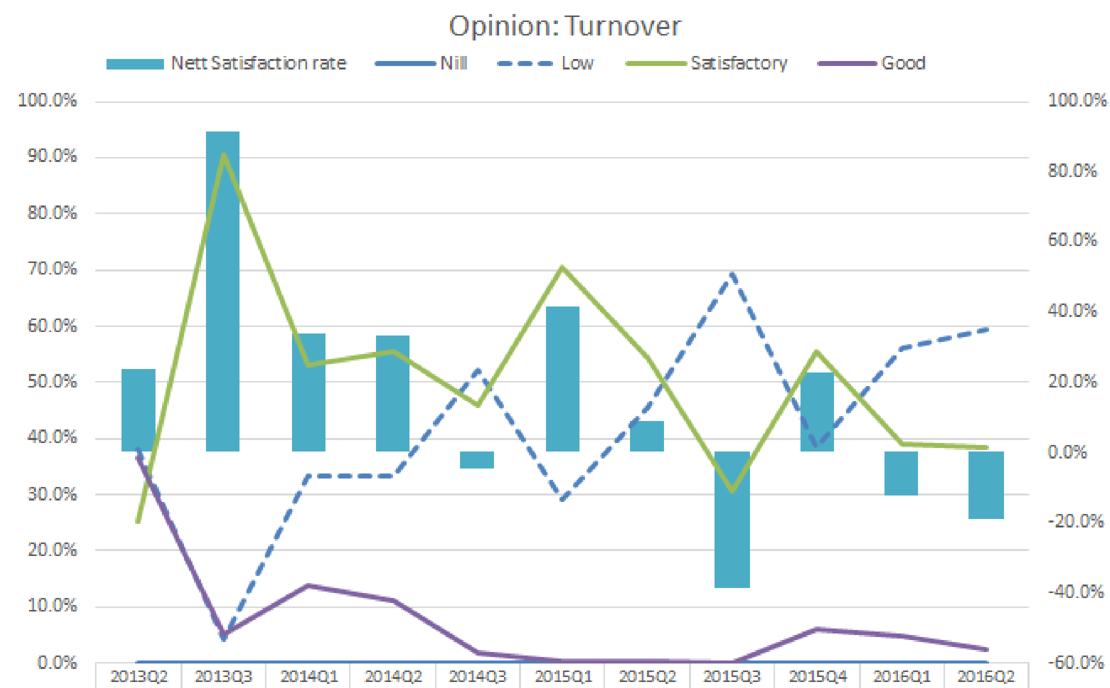


Figure 15: State of Orderbooks

- A more negative sentiment towards order books was maintained in this survey, with only a slight improvement in the negative nett satisfaction rate to -17.8 from -21.3 in the previous survey. Majority of contractors reported low order book values but did improve slightly from 60.5 percent in the previous survey to 58.6 percent. Only 40 percent reported satisfactory levels, and less than 1 percent fell that the values were good (down from 4.8 percent and 7.1 percent in the previous two surveys).

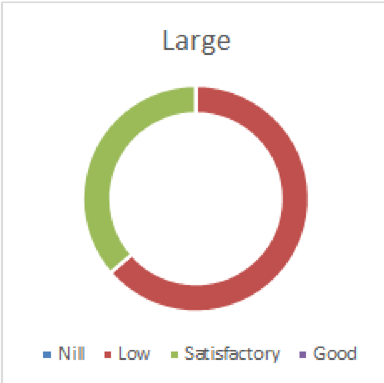
Turnover

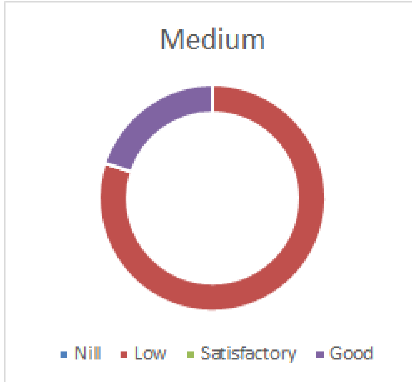
- The nett satisfaction rate in terms of opinions related to turnover deteriorated from -12 percent (revised) in the previous survey to -18.8 percent in the current survey, with an increasing number of firms reporting low values. Around 40 percent were satisfied with turnover levels, but majority (60 percent) fell values were low.
- Details of the current sentiment levels amongst the various firm size categories (large, medium and small) are provided in the charts below.

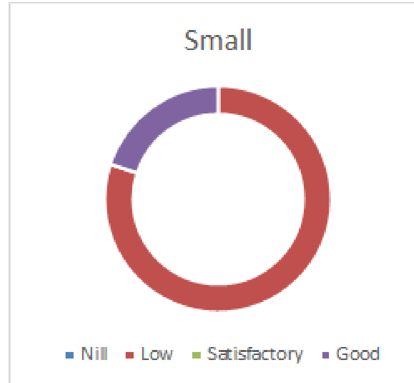


	2013Q2	2013Q3	2014Q1	2014Q2	2014Q3	2015Q1	2015Q2	2015Q3	2015Q4	2016Q1	2016Q2
Nett Satisfaction rate	23.7%	91.6%	33.6%	33.3%	-4.5%	41.5%	9.1%	-38.6%	22.8%	-12.1%	-18.8%
Nill	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	0.0%	0.0%
Low	38.2%	4.2%	33.2%	33.3%	52.2%	29.2%	45.5%	69.3%	38.5%	56.1%	59.4%
Satisfactory	25.3%	90.6%	53.1%	55.5%	45.9%	70.5%	54.2%	30.7%	55.5%	39.1%	38.3%
Good	36.5%	5.2%	13.7%	11.2%	1.8%	0.2%	0.4%	0.0%	5.9%	4.8%	2.3%

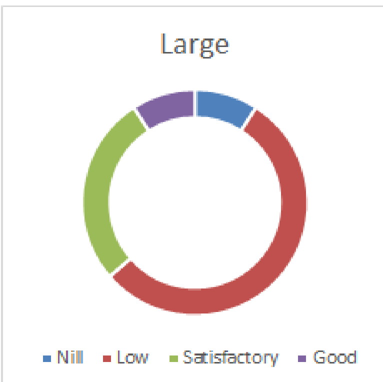
TEnder Volumes

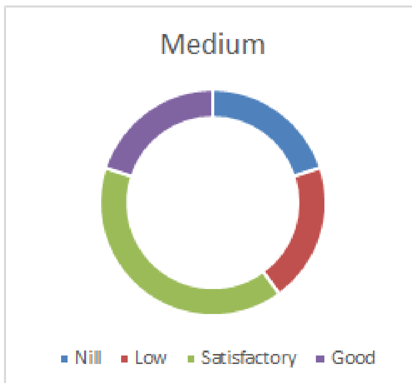


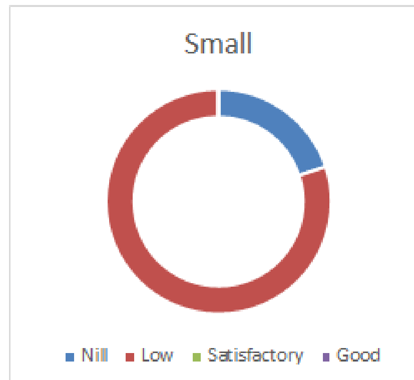




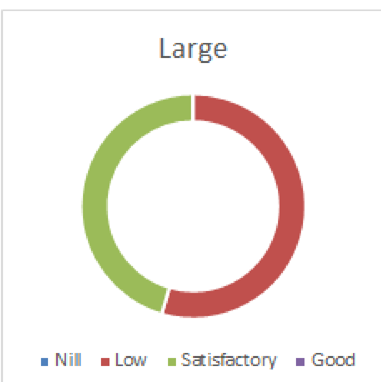
Contract Awrads

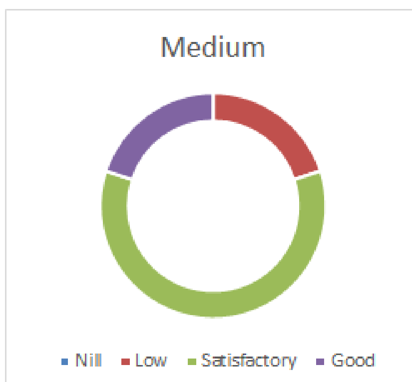


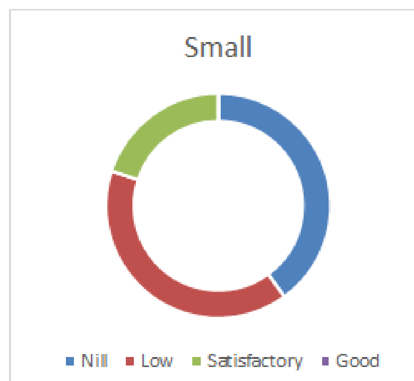




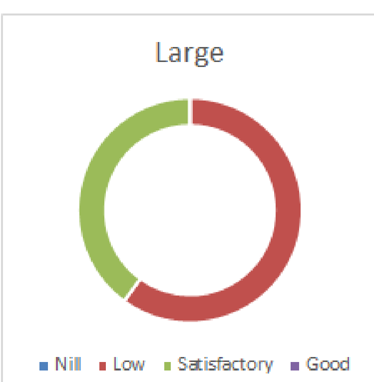
Order Book

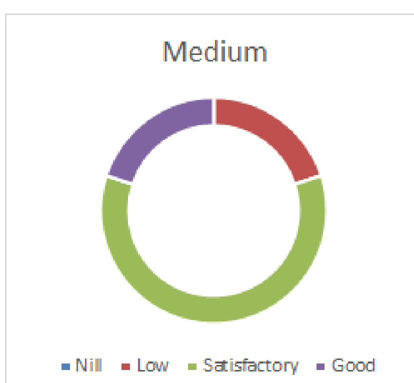


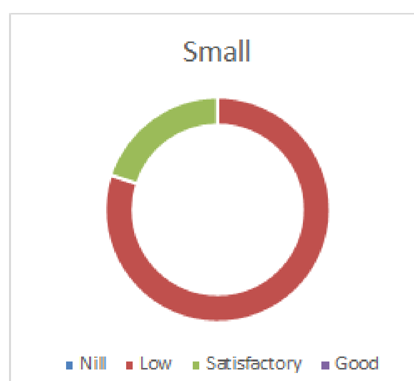




Turnover







Capacity Utilisation and Plant Equipment

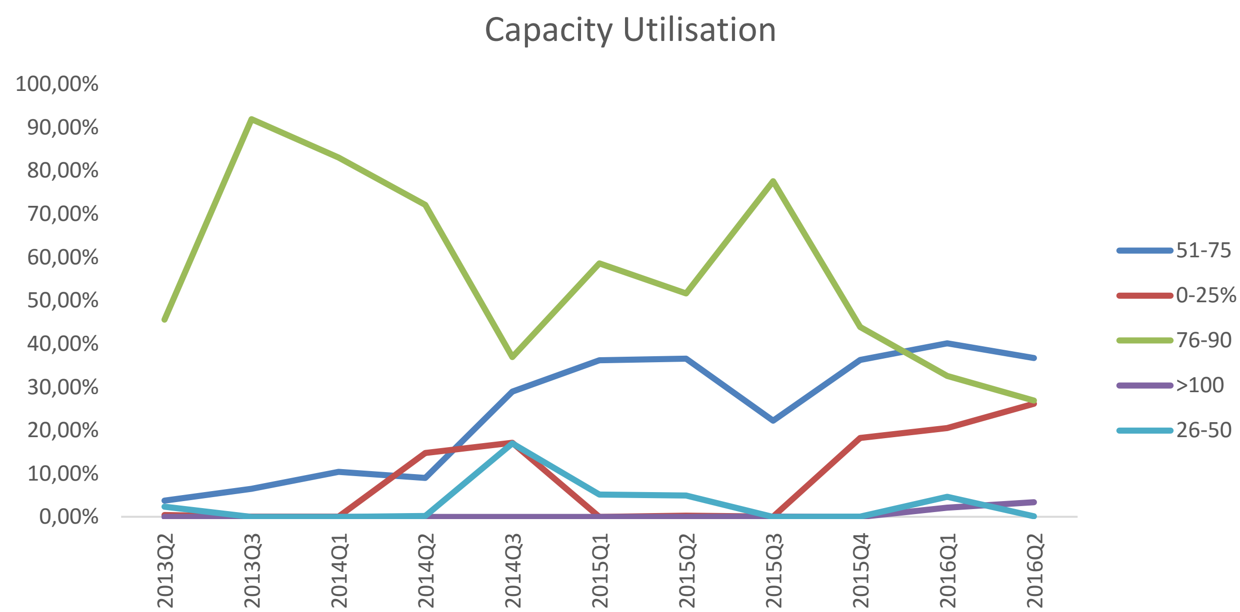


Figure 17: Capacity Utilisation, % of Respondents that reported between 51-75 percent

CAPACITY UTILISATION AND PLANT EQUIPMENT

Majority of firms (36%) reported capacity utilisation in terms of general plant and resources of between 51 – 75 percent in the 1st quarter of 2016, with an increasing number of contractors (26%) saying utilisation was less than less than 25%. Since the last survey utilisation levels have continued to deteriorate. 50 percent of larger firms reported utilisation levels below 75 percent, while all medium size firms utilised 76 percent and more.

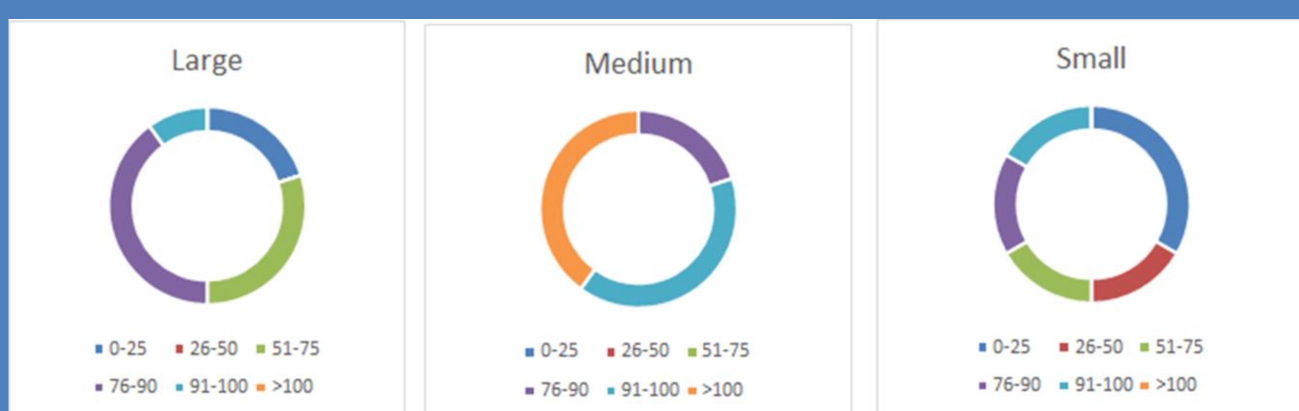


Figure 16: Capacity Utilisation by firm size

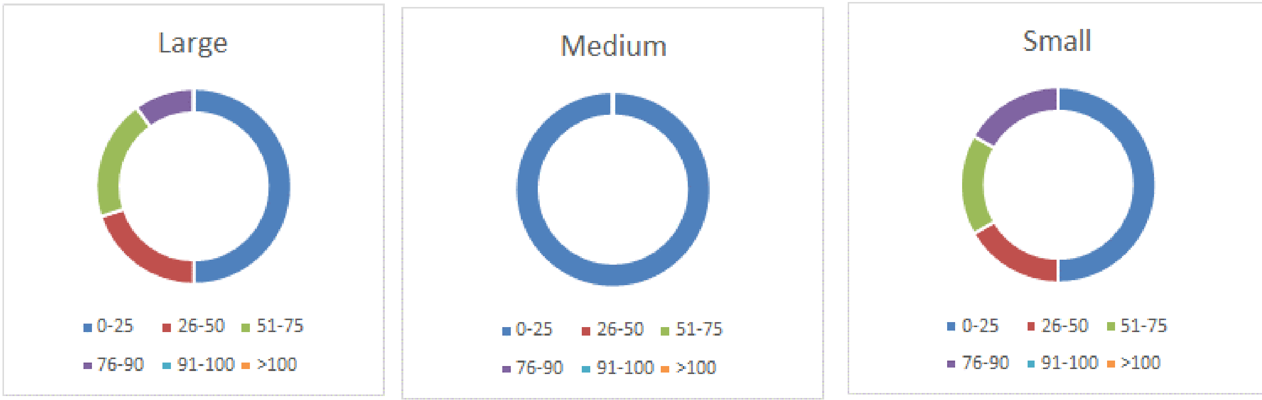


Figure 18: Percentage of company's internal plant idle, by firm size

The percentage of plant equipment standing idle increased in this survey. Although the majority still reported that less than 25 percent was idle (57 percent), there was an increase to 11 percent (from 2 percent) in the number of contractors that reported levels in excess of 50 percent.

Firm size market segmentation

Opinions and sentiment are categorised by firm size, based on reported work force including permanent and limited duration employment.

Results for various indicators are shown here, summarised by firm size.

- Working conditions for next quarter
- Competition for tenders
- Tender prices
- Profitability
- Profitability – Trend
- Capacity Utilisation
- Plant Idle

Performance of the listed sector

Several construction companies released their financial results since February 2016 (our last report), including Basil Read, Stefanutti Stocks and Raubex. While only Raubex managed to report an increase in turnover, margins showed some improvement accompanied by a marginal increase in order books.

Basil Read reported a 11.8 percent decrease in revenue for the year ended December 2015 to R5.5 bn while profitability was restored from a loss of -13.9 percent in the previous year to 4.1 percent. The company also reported a marginal increase of 1.9 percent in the value of their order book to R10.7 bn, supported by a 16.5 percent increase in their roads division and a 23.5 percent increase in their mining division. All other divisions (including building and developments, civils, plant and pipelines) reported a decrease in order books.

Figure 19: Basil Read share price movement - last 3 months as at 17 June 2016

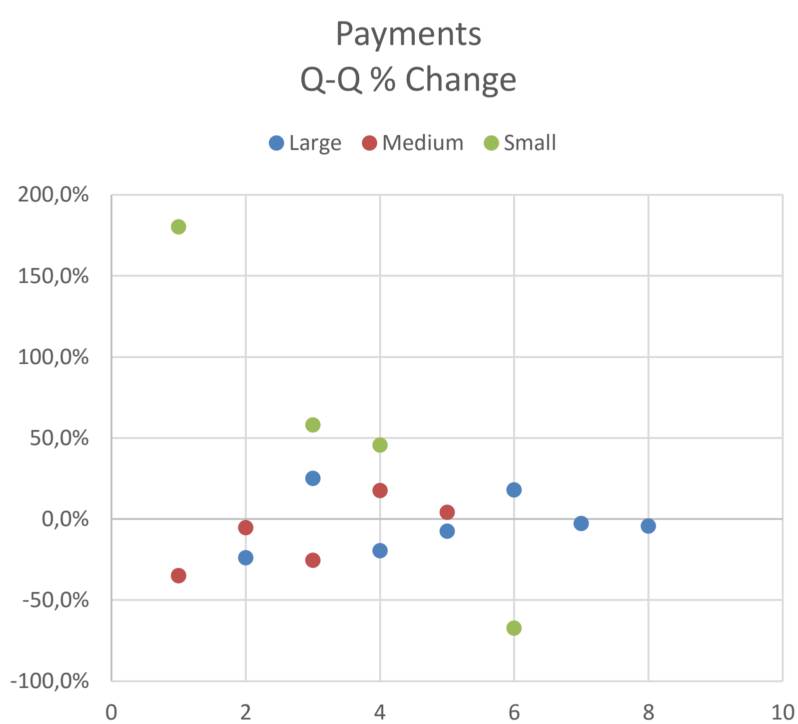
Raubex reported an increase of 9.4 percent in revenue, for the period ending 29 February 2016 to R7.93 bn. All divisions (except for road construction and earthworks) improved revenue during this period. Revenue for road construction and earthworks fell by 4.3 percent compared to the previous financial year. Operating margins improved only slightly to 8.9 percent from 8.6 percent, while operating profit rose 14.2 percent to R710.6 million. The company's order book fell 4.6 percent to R8.3 bn, due to a decrease in its materials division (down 5.4 percent) and a 28.4 percent contraction in the road construction and earthworks division.

Figure 20: Raubex share price movement - last 3 months as at 17 June 2016

Stefanutti Stocks reported a decrease of 8 percent in contract revenue in the period ended 29 February 2016 to R9.7 bn, but managed to improve operating profit by 17 percent to R391.9 million and their profit margin from 3.2 percent to 4.0 percent. All divisions, except for the mechanical and electrical division, reported a decrease in revenue. Mechanical and electrical increased revenue by 82 percent to R1.2bn, while the building division fell by 16 percent, roads, pipelines and mining services fell by 11 percent and structures fell by 17 percent. The company's order book improved by 2.4 percent to R12.7 bn and consisted mainly of medium size projects with 37.8 percent arising from work outside of South Africa.

Figure 21: Stefanutti Stocks share price movement - last 3 months as at 17 June 2016

Industry Turnover and Employment



According to responding contractors, nominal turnover based on certified payments received, fell by 8 percent q-q since the 4th quarter of 2015, following the 10 percent q-q decrease reported in the previous quarter. On a year on year basis, turnover fell by 3 percent in nominal terms (compared to the 1st quarter of 2015).

Turnover generally increases at a stronger pace in the 2nd quarter as funds have been allocated towards infrastructure allocations for the next financial year, following the release of the budget in February each year. Change in payments received fluctuated notably between the various firms, but on average, larger and medium size firms experienced more difficult period in terms of payment compared to the 4th quarter of 2015, down 8.5 percent and 19.6 percent respectively, while smaller firms reported more robust growth exceeding 100 percent.

Turnover is not expected to increase in real terms over the short to medium term, based on current movement in key economic indicators, the contraction in the estimated value of civil contracts out to tender in 2015, the overall slowdown in the number of contracts out to tender accompanied by an increase in the number of civil projects placed on hold/cancelled and the cut in projected infrastructure expenditure by government and state owned enterprises announced in the 2016/17 Medium Term Expenditure Framework.

Turnover for 2015 is estimated to have increased by between 10 and 15 percent y-y in real terms, following two years of negative real growth, down 2.6 percent and 10 percent y-y in 2014 and 2013 respectively. Turnover was boosted by the awarding of few higher value projects, and not by a broad based recovery in tender or award activity. Turnover is projected to decline by between 3 percent and 6 percent y-y in real terms during 2016, allowing for an average increase in construction cost inflation of between 8 percent and 10 percent. Construction cost inflation estimates is discussed further in the report. Estimates released by Treasury on public sector infrastructure spending for the next three years, suggest marginal growth of 1.8 percent on average over the MTEF (2016/17 – 2018/19), which in real terms will be negative growth of between 4 and 5 percent on average. Government faces a difficult period ahead as it aims to stabilise public debt, reign in government expenditure and lower the current account deficit in an attempt to avoid a further downgrade by sovereign credit rating agencies. The impact of poor economic growth on government finances will be hard felt by the local construction sector.

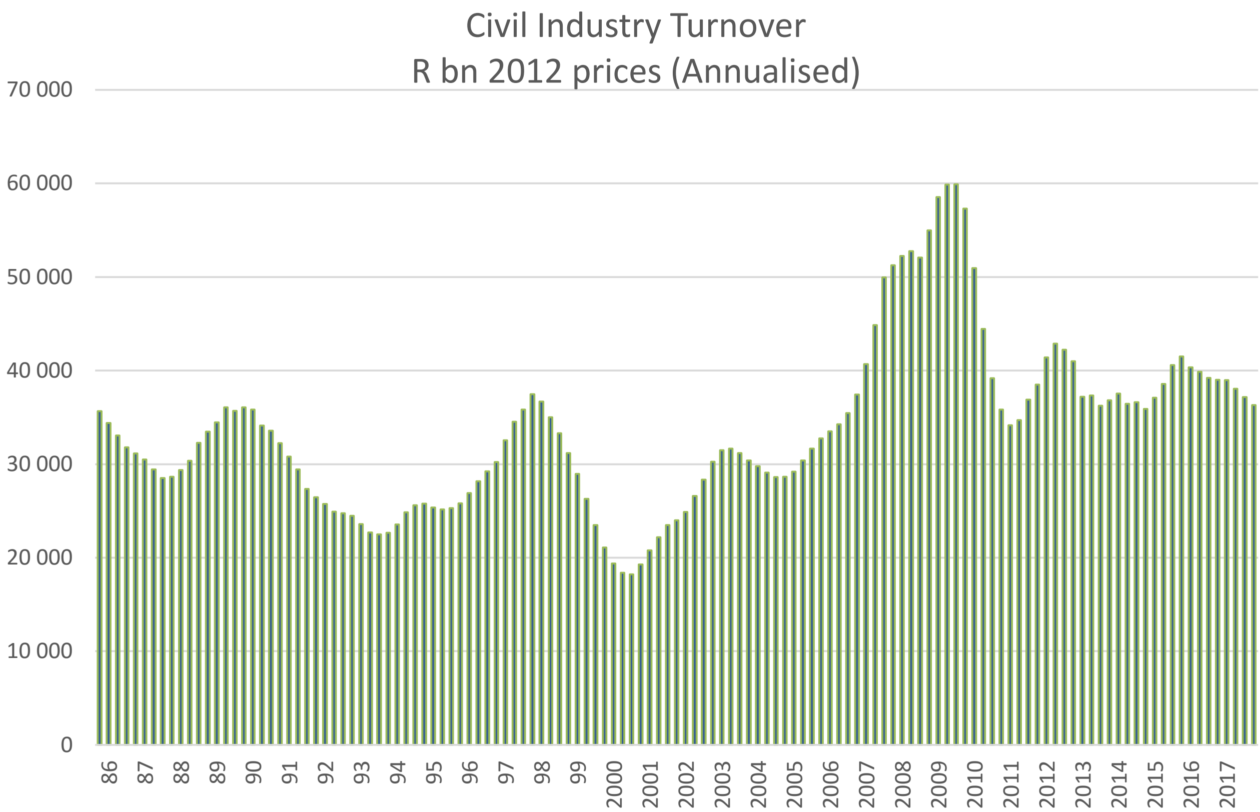


Figure 22: Civil Industry Turnover, Rm 2012 prices (annualised)

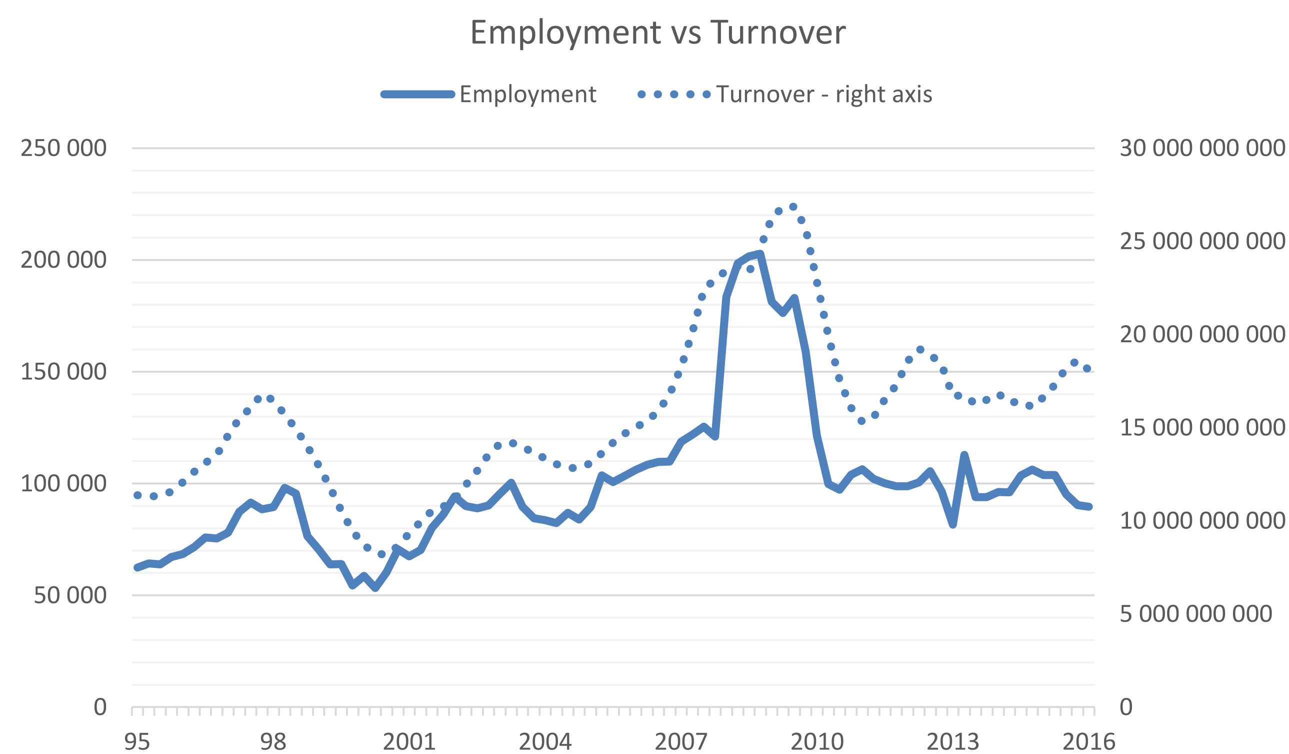


Figure 23: Employment vs Turnover

Table 15: Actual and Expected Turnover trends

	Turnover Nominal	% Change (Nominal)	Turnover 2010=100	% Change (Real)
1995	7,653,130,803		23,840,179,426	
1996	9,864,977,221	28.9%	27,485,856,690	15.3%
1997	13,282,356,448	34.6%	34,093,671,157	24.0%
1998	11,680,899,837	-12.1%	28,324,192,234	-16.9%
1999	8,600,472,761	-26.4%	19,152,137,970	-32.4%
2000	8,669,595,494	0.8%	17,588,090,052	-8.2%
2001	11,723,000,614	35.2%	21,842,034,976	24.2%
2002	17,138,501,083	46.2%	27,651,350,545	26.6%
2003	17,701,840,728	3.3%	27,666,385,851	0.1%
2004	17,180,281,073	-2.9%	26,089,962,307	-5.7%
2005	20,999,901,277	22.2%	29,825,989,361	14.3%
2006	25,783,535,490	22.8%	34,144,447,197	14.5%
2007	38,084,310,982	47.7%	46,580,085,992	36.4%
2008	58,063,639,993	52.5%	59,122,639,971	26.9%
2009	51,147,261,584	-11.9%	52,380,811,808	-11.4%
2010	32,744,103,366	-36.0%	32,744,103,366	-37.5%
2011	36,888,136,573	12.7%	35,232,222,132	7.6%
2012	40,952,061,358	11.0%	37,429,393,946	6.2%
2013	38,920,982,014	-5.0%	33,654,708,245	-10.1%
2014	39,941,145,748	2.6%	32,798,515,557	-2.5%
*2015 **	46,049,492,101	15.3%	37,928,298,093	15.6%
2016 (f)	48,351,966,706	5.0%	36,214,866,986	-4.5%
2017 (f)	45,450,848,704	-6.0%	33,037,802,443	-8.8%
2018 (f)	45,905,357,191	1.0%	31,728,498,119	-4.0%

*Provisional Figures

Table 16: Employment, Contract Awards, Turnover and Salaries and Wages

	Employment	Turnover (nominal)	Salaries and Wages (nominal)
2011.1	106,463	8,014,928,510	1,773,703,679
2011.2	102,079	8,600,000,000	1,903,180,000
2011.3	100,037	10,187,541,740	2,254,502,987
2011.4	98,837	10,085,666,323	2,231,957,957
2011	101,854	36,888,136,573	8,163,344,624
2012.1	98,837	11,324,591,712	2,506,132,146
2012.2	100,497	10,456,138,926	2,313,943,544
2012.3	105,522	9,933,331,979	2,198,246,367
2012.4	96,502	9,237,998,741	2,044,369,121
2012	96,502	40,952,061,358	9,062,691,178
2013.1	81,651	7,944,678,917	1,758,157,444
2013.2	112,823	11,122,550,484	2,461,420,422
2013.3	93,894	9,454,167,911	2,092,207,359
2013.4	93,894	10,399,584,702	2,301,428,095
2013	95,565	38,920,9982,014	8,613,213,320
2014.1	96,241	9,255,630,385	2,048,271,004
2014.2	96,048	10,643,974,943	2,355,511,655
2014.3	103,732	10,111,776,196	2,237,736,072
2014.4	106,326	9,929,764,224	2,197,456,823
2014	100,587	39,941,145,748	8,838,975,554
2015.1	103,774	10,525,550,078	2,526,132,019
2015.2	103,774	12,209,638,090	2,677,699,940
2015.3	95,161	12,270,686,281	2,455,450,845
2015.4	90,403	11,043,617,652	2,319,159,707
2015	98,278	46,049,492,101	9,978,442,510
2016	89,679	10,160,128,240	2,133,626,930

Confidence Index

The quarter on quarter movement in the index has been more erratic lately, but after some improvement in the last few quarters brought about by a more optimistic outlook from medium size contractors, the trend has reversed, showing signs of a further weakening.

Explanatory note: The civil engineering confidence index relates to the overall business outlook amongst the companies within the industry. Levels below the 50-mark indicate pessimism, 0 equals total negativity, and 100 indicates absolute optimism. This is a continuously changing weighted index.

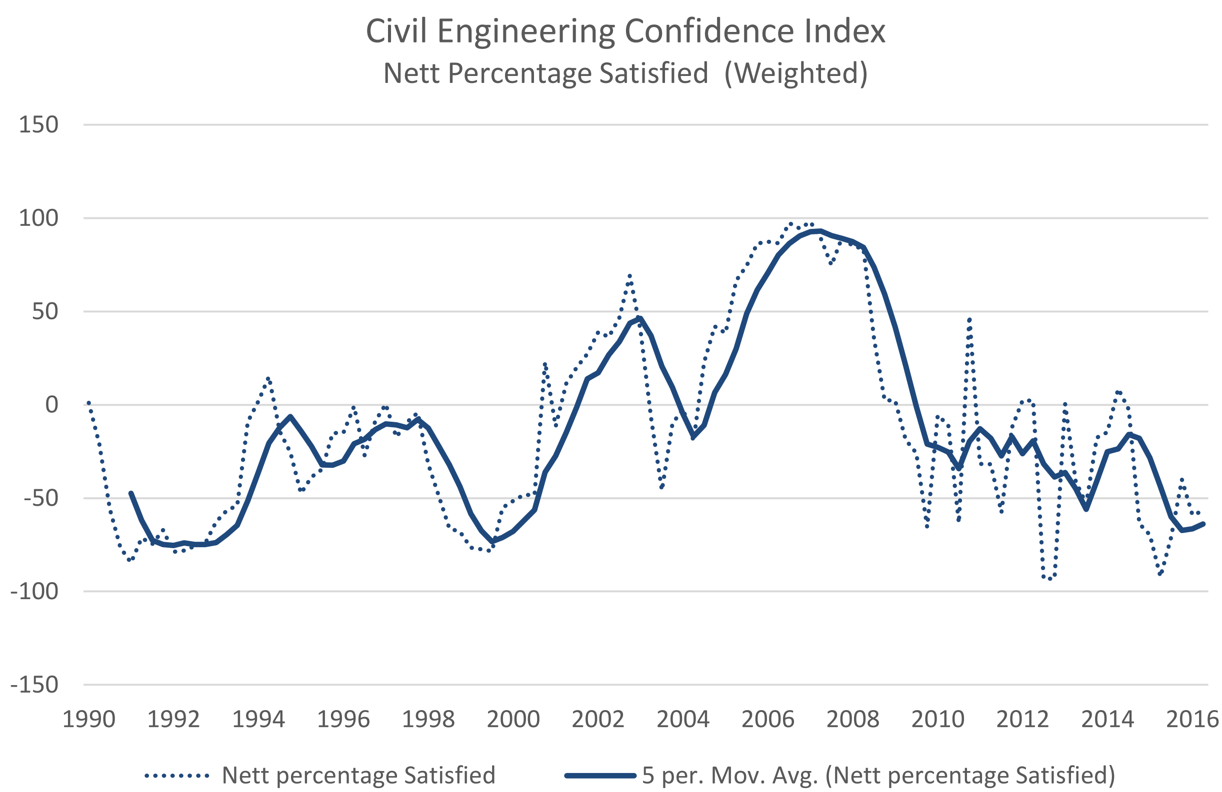
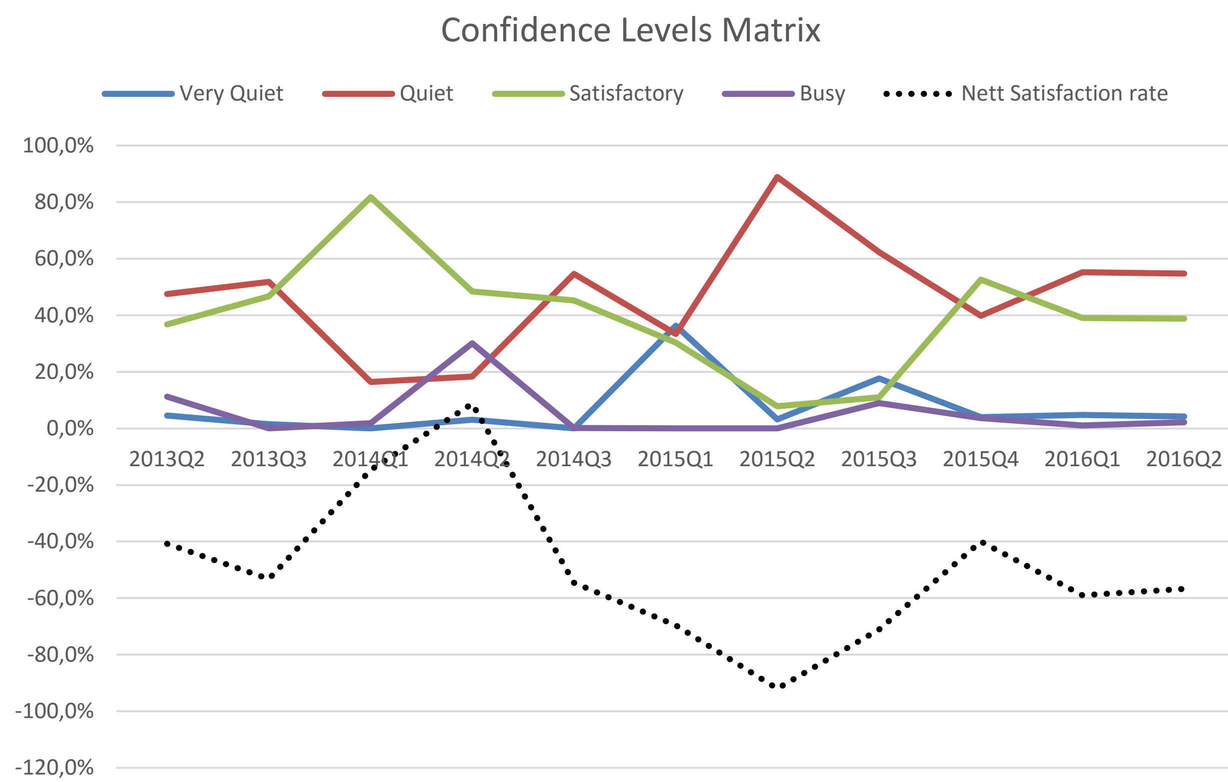


Figure 24: Civil Engineering Contractors Confidence Index

Culminating all the other indicators already discussed, the nett satisfaction rate remained at very low levels, with a slight improvement to -57.0 from -59.0 in the previous survey. 55 percent of contractors surveyed reported current working conditions as being quiet (on par with respondents from the previous survey), while 39 percent reported satisfactory conditions. In this survey, all firm size categories reported negative nett satisfaction rates, although larger firms were the most "negative", with a -63 nett satisfaction rate, followed by smaller firms at -50.0 and medium size firms at a level of -40.0.



The main difference between the SAFCEC confidence index and the FNB/BER is the fact that the SAFCEC responses are weighted according to firm size. Thus while the indices may be at a different level, the trends are very similar and clearly shows the depressed conditions currently being experienced in the civil industry. The SAFCEC confidence index is recalculated here to show the percentage satisfied as opposed to the nett percentage satisfaction rate, as shown in the chart above. According to the FNB/BER, the civil contractor confidence index declined sharply to 28 percent in the 1st quarter of 2016, from 42 percent the previous quarter (4th quarter 2015), and has been below the 50 percent neutral level since 2008. The chart below clearly reflects the structural shift that has taken place, as it the current trends depicted in the industry are no longer subject to normal cyclical patterns. Serious structural reforms are required to restore growth in the industry, highlighting constraints in both government and SOE's.

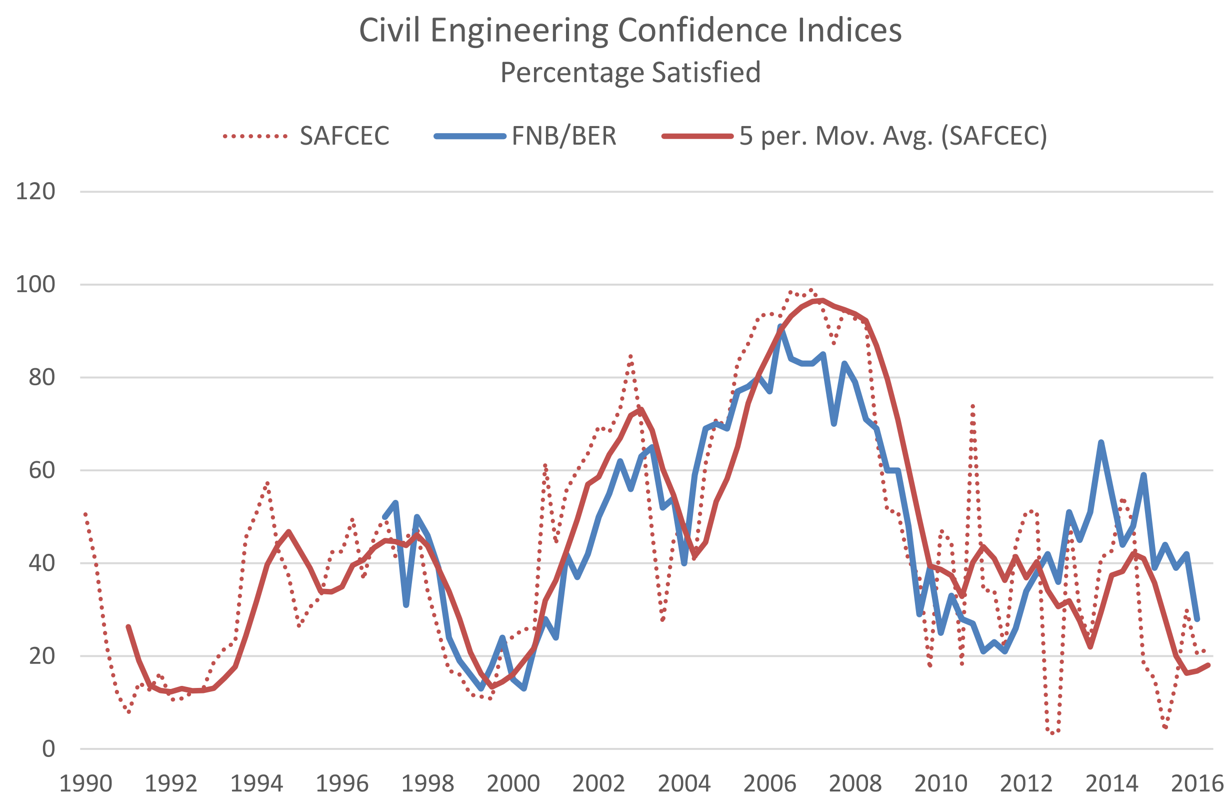


Figure 25: FNB/BER Confidence index vs SAFCEC Confidence Index

Survey results EX-RSA

Table 6: Business conditions during the past two quarters

	Previous quarter	*Current Quarter*
Very poor	20%	10%
Poor	40%	50%
Satisfactory	30%	30%
Good	10%	10%
Very Good	0%	0%
Nett Satisfaction	-50%	-50%

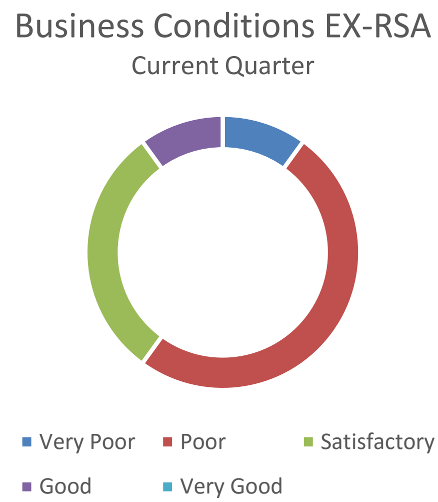
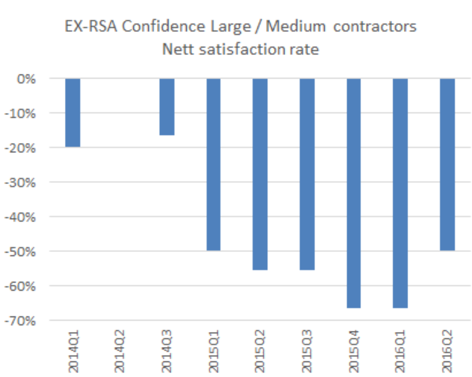
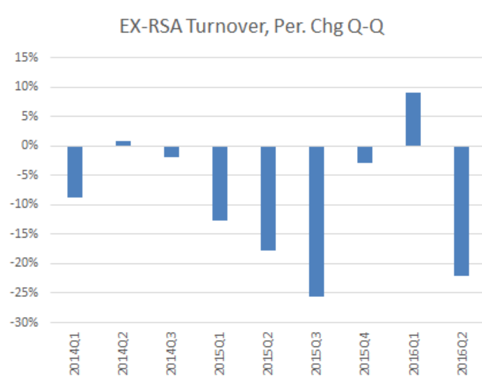
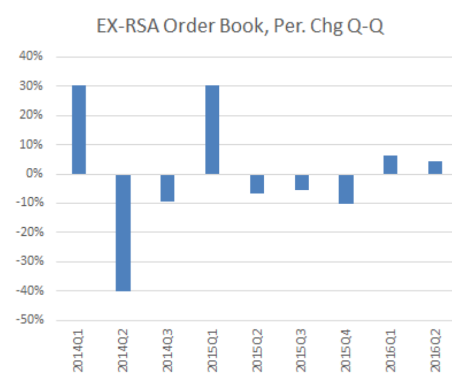


Table 7: Late payments, order books and turnover, EX-RSA

Survey period	*% late payments of turnover*	*% Change in* turnover	*% Change in order book*
2014Q2	46%	1%	-40%
2014Q3	47%	-2%	-10%
2014Q4	59%	-13%	30%
2015Q1	106%	-18%	-7%
2015Q2	133%	-26%	-6%
2015Q3	54%	-3%	-10%
2015Q4	59%	9%	6%
2016Q1	94%	-22%	4%







PROSPECTS FOR 2016 and 2017

Key issues affecting current confidence levels in the industry:

- Global economic turmoil, affecting particularly emerging and developing economies.
- Domestic economic woes intensified in 2016 with elevated political instability, violent and disruptive protest action, while credit rating agencies remain largely supportive of a further downgrade. A looming recession will have a more profound impact on an already ailing construction sector.
- Skills related to engineering is becoming a more serious constraint largely aggravated through continued client interference which creates an environment whereby agents are being disempowered. This leads to project implementation delays and is a contributing factor to the increase in payment delays, through delays in certification.

- Slow roll out of public sector infrastructure projects, including the delays to implement the targets as set out in the National Development Plan, aggravated by cuts in projected infrastructure expenditure allocations which were announced in the 2015/16 Budget, has resulted in negative growth projected over the medium term expenditure framework period (2016/17 – 2018/19).
- Award delays are also becoming more significant. Contractors have a quarter of the time to prepare and submit tender document, compared to the time taken by clients to adjudicate.
- Currency volatility and depreciation of the rand (down close to 40 percent in 2015) means any gains from the lower oil price are eroded.
- Skills shortages in procurement which also include government's ability to implement proper project planning and implementation. It is also critical to shorten the delay between tender and awards which could take as long as one year.
- The inability of certain local and district municipalities to spend allocated budgetary allocations, which also suggest inadequate skills in planning and budgetary management.
- Low confidence in the mining sector and policy uncertainty is delaying private capital expenditure.
- Continued labour unrest affecting economic performance as well as critical project execution. Unrest is expected to escalate in 2016 because of the municipal elections. This could lead to even further delays in project implementation.
- The tendency by government to break what should be larger Grade 9 projects, into smaller grade projects, referred to as project fragmentation.
- Pricing by contractors remains a concern, as some contractors would tender on projects that fall outside the scope of the prescribed CIDB grade, leading to uncessary delays in the procurement process. Prices can also vary to the extent that it can almost be deemed as irresponsible, or below cost with little or no regard to operational efficiency or the impact of (negative) escelation on contracts.
- As the industry continues to shed employment, these and other challenges will impact on the industry's future capacity to respond effectively to increased demand when the industry starts to recover.

CIVIL ENGINEERING PRICE MOVEMENTS

The Baxter contract price adjustment formula (or CPAF), is widely recognised by the industry as an accepted set of indices to adjust contracts for payment escalation. However, it is important to clarify that these set of indices are freely available and published by Statistics South Africa and is not owned or manipulated by SAFCEC in any way

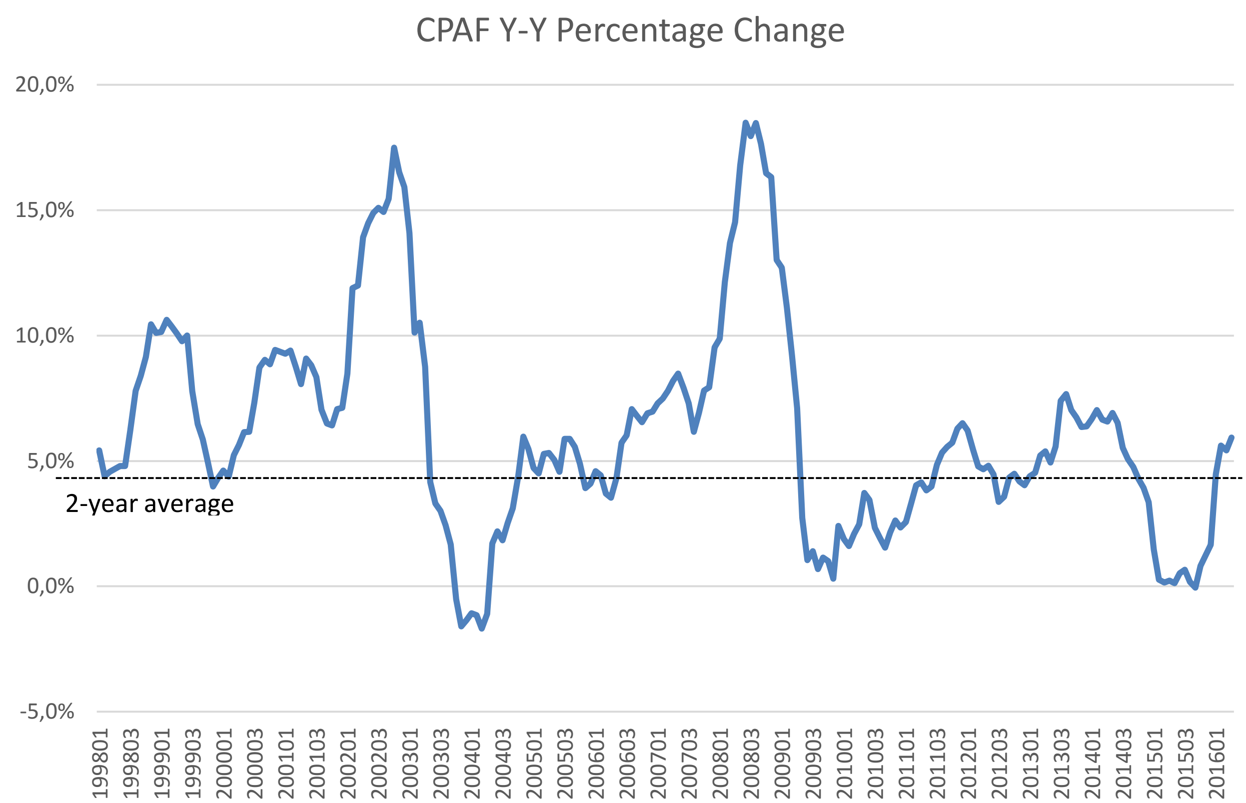
Input cost price movements based on the Baxter contract price adjustment formula (CPAF) averaged (revised) 0.6 percent in 2015, as opposed to a "negative" -0.3 as previously published. The revision is due to the termination of the PPI fuel index "Diesel Fuel: Coast and Witwatersrand" in February 2016 and replaced with "Diesel Fuel: Wholesale. Although price deflation still occurred in the fuel price index, the decline based on the new index was more moderate averaging -15.5 percent as opposed to -25.9 percent.

Input cost inflation averaged 5.9 percent y-y in the 1st quarter of 2016, following an average increase of 1.2 percent in the 4th quarter of 2015. Price deflation still occurred in the material index, down 0.6 percent y-y, but at a much slower pace compared to the -7.1 percent average drop in the previous quarter. Price deflation in the fuel index also slowed from -8.4 percent y-y to -0.6 percent, while the annual increase in the plant index accelerated to 9.5 percent from 5.2 percent in the previous quarter. Labour costs, as measured by the CPI, also accelerated from an annual increase of 4.9 percent in the 4th quarter of 2015 to an average of 6.5 percent in the 1st quarter. Pending further developments in the oil price and currency vulnerability, we expect the composite index to average an increase of 10 percent in 2016 (coming off a lower base in 2015 and assuming further currency weakening, but with more moderate oil prices), and 3.0 percent in 2017, accelerating to 5.2 percent by 2018. Our assumptions include a continuation of the low oil price, falling from an average of $48/barrel in 2015 to $40/barrel in 2016, before showing a mild recovery in 2017 and 2018, and faster than anticipated depreciation in the currency, averaging R16.0/US Dollar in 2016, pending further developments in South Africa's sovereign credit rating. The risk weighs more on the upside of a stronger recovery in the oil price, and if maintained at just below $49/barrel (as at June 2016) for the remainder of the year, will average $44/barrel for 2016. These developments and the impact on input cost construction will be closely monitored.

Please note the fuel index is now based on Diesel Fuel – Wholesale

Table 17: CPAF Indices Annual Percentage Change

Year	Material (SAFCEC)	Fuel (SAFCEC)	Plant (SAFCEC)	Labour (CPI)	Composite
2013	4.3%	7.2%	6.3%	5.8%	5.7%
2014	3.3%	3.1%	6.4%%	6.1%	5.6%
2015	-5.2	-15.5%	3.2%	4.6%	0.6%
2016*	2.0%	3.2%	26.0%	6.2%	10.0%
2017*	3.0%	3.0%	-1.9%	6.0%	3.0%
2018*	3.0%	14.2%	3.8%	5.8%	5.3%



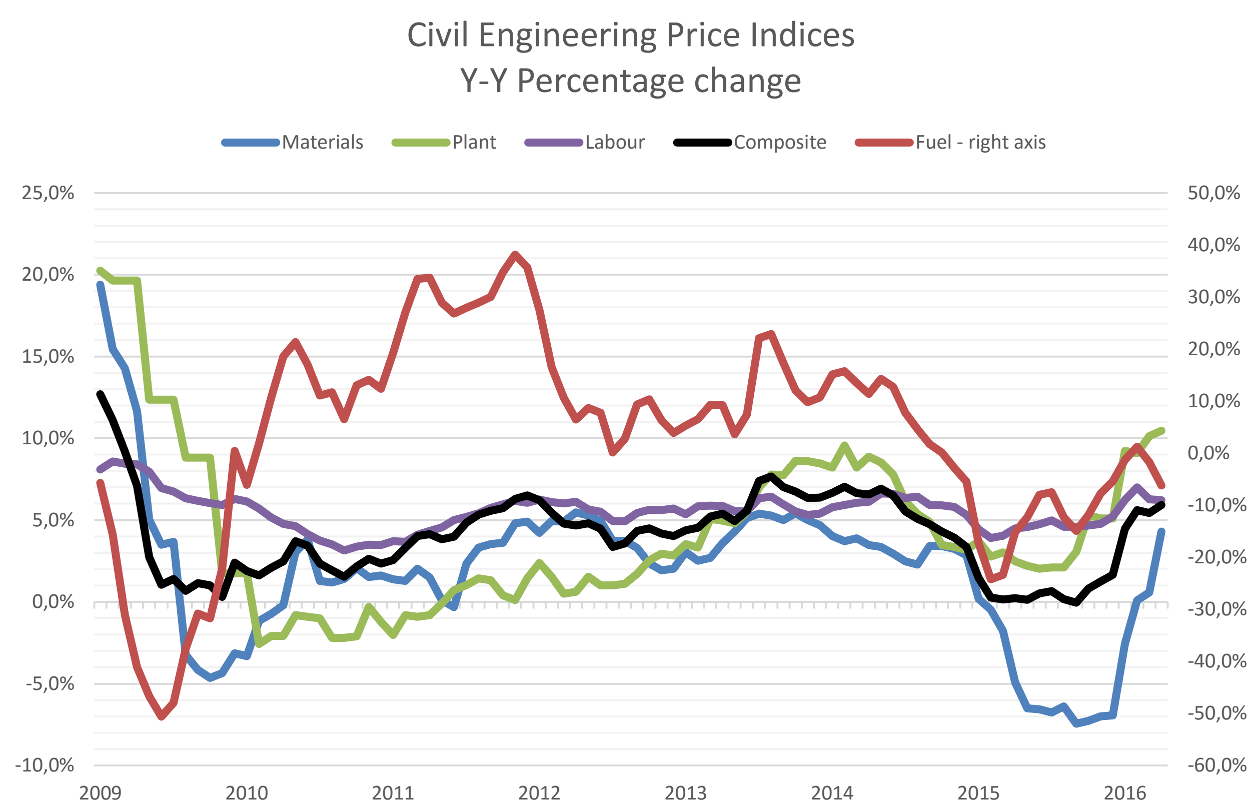


Figure 26: Civil Engineering price movements (source Stats SA)

Table 18: Macro Price Assumptions

	2012	*2013*	*2014*	*2015*	*2016*	*2017*	*2018*
R/US$ Exchange Rate	8.2	9.7	11.3	12.7	16.0	15.7	16.3
Oil price ($ per barrel, UK Crude oil)	111.8	108.0	96.0	48.8	40.0	42.0	46.2
Oil Price (ZAR per barrel)	917.9	1042.2	1085.1	620.2	640.0	659.4	753.1
CPI (% change)	5.7%	5.8%	6.1%	3.8%	6.2%	6.0%	5.8%

Table 19: CPAF Indices Forecast 2012-2017

Index 2012= 100	*2012*	*2013*	*2014*	*2015*	*2016*	*2017*	*2018*
Plant	100.0	106.3	113.1	116.8	147.1	144.3	149.9
Fuel	100.0	107.2	110.6	99.8	103.0	106.1	121.2
Materials	100.0	104.3	107.7	102.1	104.2	107.3	110.5
Labour	197.2	208.5	221.2	231.3	245.6	260.4	275.5
Composite	129.1	136.4	143.6	145.0	159.4	164.2	172.9
Y-Y Percentage Change							
Plant	1.6%	6.3%	6.4%	3.2%	26.0%	-1.9%	3.8%
Fuel	8.8%	7.2%	3.1%	-15.5%	3.2%	3.0%	14.2%
Materials	3.9%	4.3%	3.3%	-5.2%	2.0%	3.0%	3.0%
Labour	5.7%	5.8%	6.1%	4.6%	6.2%	6.0%	5.8%
Composite	4.5%	5.7%	5.3%	0.4%	9.9%	3.0%	5.3%

Table 20: CPAF Indices (Quarterly Average)

		CPAF Indices 2012=100					Y-Y Inflation				
Year	Quarter	Materials	Labour	Fuel	Plant	Composite	Materials	Labour	Fuel	Plant	Composite
2012	1	99.6	193.3	99.0	98.9	127.5	4.7%	6.1%	17.8%	1.5%	5.5%
	2	100.0	196.2	101.2	99.5	128.8	5.2%	5.8%	7.6%	1.0%	4.6%
	3	100.1	198.0	94.8	100.4	129.0	3.6%	5.1%	4.1%	1.3%	3.8%
	4	100.1	201.1	105.1	101.2	131.2	2.1%	5.6%	6.8%	2.8%	4.2%
2013	1	102.4	204.4	106.3	102.8	133.5	2.7%	5.7%	7.4%	4.0%	4.7%
	2	104.3	207.2	107.7	104.5	135.6	4.3%	5.7%	6.5%	5.1%	5.3%
	3	105.4	210.4	115.6	107.9	138.7	5.2%	6.2%	21.9%	7.5%	7.5%
	4	105.1	212.0	116.6	109.8	139.8	5.0%	5.4%	10.9%	8.6%	6.5%
2014	1	106.3	216.5	122.2	111.7	142.6	3.9%	5.9%	14.9%	8.7%	6.8%
	2	107.7	220.6	121.0	113.3	144.6	3.3%	6.5%	12.4%	8.4%	6.6%
	3	108.2	223.5	118.8	113.8	145.6	2.7%	6.2%	2.8%	5.5%	5.0%
	4	108.5	224.0	110.3	113.5	144.8	3.2%	5.7%	-5.4%	3.3%	3.6%
2015	1	105.6	225.4	91.2	115.2	143.0	-0.7%	4.1%	-25.4%	3.2%	0.3%
	2	101.3	230.8	105.3	115.8	144.9	-6.0%	4.6%	-13.0%	2.2%	0.2%
	3	100.8	234.1	102.1	116.6	145.7	-6.9%	4.7%	-14.0%	2.4%	0.1%
	4	100.8	235.0	100.7	119.4	146.6	-7.1%	4.9%	-8.7%	5.2%	1.2%
2016	1	104.9	240.0	100.3	126.2	151.4	-0.6%	6.5%	10.1%	9.5%	5.9%

Bibliography

1. SAFCEC Membership surveys
2. Databuild / Industry Insight project database of tenders, awards, postponements (www.industryinsight.co.za)
3. IMF World Economic Outlook
4. Statistics South Africa
    a. POO44 Financial statistics
    b. P0141 Consumer Price Index
    c. P0151 Production Price Index: PPI For Selected Materials
5. FNB/BER confidence Indices
6. Estimates of National Expenditure Reviews (Treasury)