

## State of the South African Civil Industry

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SOUTH AFRICAN FORUM OF CIVIL ENGINEERING CONTRACTORS

# State of the South African Civil Industry

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1st Quarter 2015

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## ECONOMIC BACKGROUND

Globally, monetary policies are being re-aligned to cater for the, perhaps short term, inflationary impact caused by the lower international oil price.

A few important issues are highlighted in terms of developments in the global economy that will impact on the domestic economy.

Global growth is expected to accelerate in 2015, from an estimated 3,3 percent in 2014 to 3,5 percent in 2015 and 3,7 percent in 2016. However these forecasts are still below the 4,0 percent projected in mid-2014. While growth in emerging markets are expected to slow somewhat in 2015 (from 4,4 percent in 2014 to 4,3 percent), growth in advanced economies is expected to accelerate from 1,8 percent to 2,4 percent in 2014. According to the most recent world economic outlook by the IMF (January 2015), there are four key developments in 2014 that influence the growth projections for 2015. Among these are surplus oil production, spurred by shale gas exploration in the US, accelerated growth in mainly the US, currency shifts, including a stronger US dollar and a weaker Euro, while risks associated with lower commodity prices and the lower oil price have increased in emerging markets. The IMF acknowledges that while lower oil prices could boost global growth, there are many downside risks. Lower oil prices could slow investment, increase market volatility, promote stagnation in Euro area and Japan, while geopolitical events still weigh heavy on the global growth outlook.

These factors will have divergent implications for growth forecasts of different emerging economies, which is why the IMF has revised forecasts downward for Brazil, China, Mexico, Nigeria and Russia.

Table 1: World Economic Outlook (Source: IMF)

	<i>2012</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>	<i>2016</i>
World	3.1	3.0	3.3	3.5	3.7
US	2.2	1.9	2.4	3.6	3.3
Eurozone	-0.6	-0.4	0.8	1.2	1.4
UK	0.3	1.7	2.6	2.7	2.4
Emerging Markets		4.7	4.4	4.3	4.7
Brazil	0.9	2.3	0.1	0.3	1.5
Russia	3.60	1.5	0.6	-3.0	-1.0
India	3.2	4.4	5.8	6.3	6.5
China	7.8	7.7	7.4	6.8	6.3

Sub-Saharan Africa	4.9	5.1	4.8	4.9	5.2
SA	2.5	1.8	1.4	2.1	2.5

## Domestic Economy

The domestic economy grew by an estimated 1,4 percent in 2014, from 1,8 percent in 2013, and according to the Reserve Bank, at least one percentage point was lost in 2014 due to work stoppages (strike action) during 2014. Taking into account electricity supply disruptions, the Bank lowered GDP growth forecast to 2,2 percent (in line with latest IMF forecasts) for 2015 and to 2,5 percent for 2016 (from a previous forecast of 2,9 percent).

The South African economy faces several risks as we move into 2015:

- Tightening of monetary policy by the US Federal Reserve that could tighten the interest rate differential between SA and the US, leading to capital outflows and a weaker currency. This in turn will have a negative impact on imported inflation.
- Further downgrades by the credit rating agencies will put South Africa outside of the investment grade, similar to the “junk status” just recently received by Russia. This will also lead to significant capital outflows.
- Currency volatility associated in general with emerging market risks and capital flows
- Weak private sector sentiment and confidence will continue to impact negatively on consumption expenditure and investment.
- Policy uncertainty especially in the formulation of the new land ownership bill. Cabinet is yet to decide on the exact scope of the ban on foreign land ownership and to which categories of land it will apply. There has been an outcry following this announcement, which further proposes a limit of 10,000 hectares on commercial farm owners. However, Tourism Minister Derek Hanekom does not see this as a threat to foreign investment, but major investors from countries such as Germany has already voiced their concerns.
- Labour market instability and violent strike action has become the norm for South Africa, and is a major impediment for investment as well as a significant contributor to lower economic growth.
- Electricity constraints and load shedding has again reached critical levels in South Africa slowing investment as well as economic growth

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

	2012	2013	2014	2015	2016	2017
GDP	2.5	1.9	1.4	2.2	2.3	3.1
Household consumption	3.5	2.6	1.5	3.9	2.6	3.1
Government consumption	4.0	2.4	1.4	2.0	2.5	3.0
Gross Fixed capital formation	4.4	4.7	1.3	1.3	3.4	4.2
US/ZAR	8.2	9.7	11.0	12.1	12.7	11.4

CPI Inflation	5.7	5.8	6.2	3.8	5.5	5.6
Prime Lending rate	8.7	8.5	9.3	9.3	9.8	10.3
Current account % of GDP	(5.2)	(5.8)	(6.0)	(5.8)	(5.5)	(5.3)

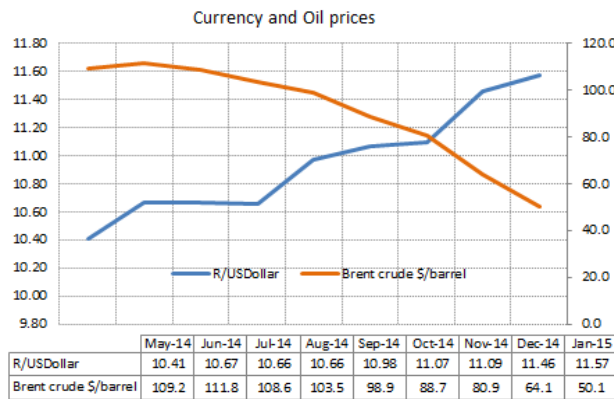


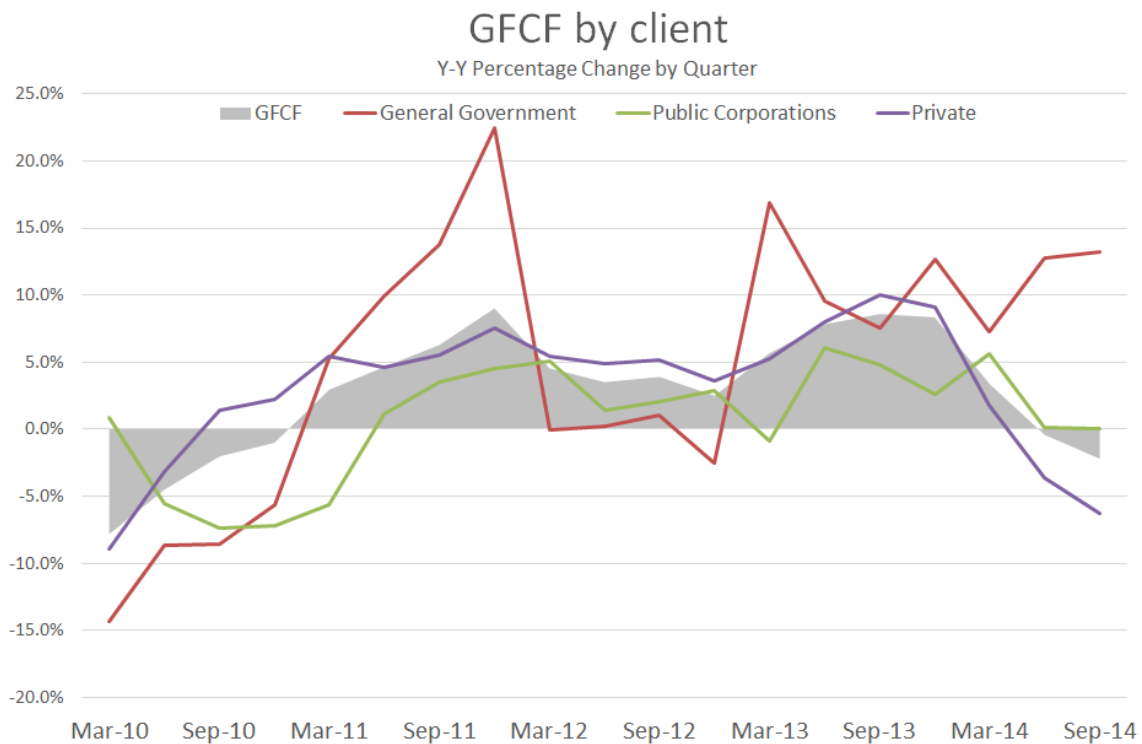
Figure 1: Currency and Oil prices

The current inflationary environment has improved following lower oil prices, postponing decisions by policy makers to adjust lending rates, including the US Federal Reserve. Inflation eased to 4,4 percent by January 2015 and is expected to average 3,8 percent for 2015, before returning to levels of between 5,0 and 6,0 percent in 2016. The lower oil price however comes with its own set of risks, including lower growth in South Africa's trading partners, which lowers South Africa's export growth potential.

Analysts however still expect the Reserve Bank to tighten monetary policy, which could be towards the end of the year (2015) or as expected by majority, by mid 2016.

The inflationary impact of the lower oil price, was mitigated by a weaker currency, which averaged R11,6/US Dollar in January 2015, from R10,4/USDollar in May 2014. The price of Brent crude oil softened to an average of \$50/barrel in January 2015 but prices started to rebound somewhat in February, expected to average \$60/barrel. There is a broad consensus view that prices will stabilise at around \$80/barrel towards the end of the year, but this will all depend on the economic recovery in the US, and further exploration of shale gas.

## Gross fixed capital formation



*Figure 2: GFCF By Client*

Investment growth in gross fixed capital formation moderated significantly since our last report, -0,4 percent and -2,2 percent y-y in the 2<sup>nd</sup> and 3<sup>rd</sup> quarters of 2014 (2010 prices, annualised rates). Growth was negatively affected by a significant contraction in private sector fixed investment (down 3,6 percent and 6,6 percent y-y in the last two quarters), while no growth was reported in investment by public corporations over the same period.

Although, investment by government continued to increase by double digit rates, up an average of 13,0 percent over the last two quarters, it wasn't enough to support growth in overall fixed investment. Investment by government contributed less than 20 percent in the 3<sup>rd</sup> quarter of 2014, to total GFCF. Private sector investment is critical to support GFCF as it represents more than 60 percent of total investment in the country. Business confidence, a prerequisite to encourage stronger levels of investment, has shown no real improvement since 2007, and remains at a relatively neutral level of close to 50. A level above 50, suggest more people are positive, while below 50 suggests there are more people feeling pessimistic regarding business conditions in the country. The outlook for private sector investment growth therefore remains fairly muted.

### Market Segment Analysis

- Investment in residential buildings fell by 6,9 percent y-y (constant prices, annualised), in the 3<sup>rd</sup> quarter of 2014, with only marginal growth of 2,5 percent reported in non-residential investment. The nett effect is total investment growth in building that has been in decline since 2009, which means investment (in real terms) has shrunk by more than 25 percent since 2008. In real prices that equates to about R32 billion.
- The private sector however did throw their weight behind the renewable energy sector, and was a significant contributor to higher levels of investment in construction works during 2013 and the first two quarters of

2014. Investment in renewable energy is likely to support some growth in 2015, but may be negatively affected by financial constraints slowing Eskom's ability to connect the newly developed renewable energy resources to the national grid.

- Overall investment growth in construction works, slowed to 8,4 percent y-y in the 3<sup>rd</sup> quarter of 2014, from 17,4 percent and 30,0 percent y-y in the two previous quarters, supported largely by higher levels of private sector investment in renewable energy projects.
- Investment in construction (including building and civil) moderated during the last two quarters from 15,8 percent and 9,2 percent in the 1<sup>st</sup> and 2<sup>nd</sup> quarters to 4,7 percent y-y in the 3<sup>rd</sup> quarter.
- Based on the first three quarters we expect a further contraction in investment in buildings for 2014 (down 2,0 percent in real terms, and a 17,5 percent overall increase in investment in construction works. It is important however to note that investment in construction works include investment associated with importing machinery and equipment used on construction projects, for example turbines.
- The outlook for investment in buildings is slightly more positive for 2015 as several large residential developments have started construction during 2015. Large projects are currently under development, including Waterfall Estate in Midrand, The Mall of the South as well as various projects in and around the V&A Waterfront in the Western Cape, supporting some growth in 2015. The outlook for further investment in non-residential building is however more negative following a contraction in pipeline activity as fewer projects are being approved for construction by the local authorities.

Please note that the Reserve Bank revised quarterly figures in the September 2014 Quarterly Bulletin, adjusting historical gross fixed capital formation numbers, largely downwards. Data in the tables below have been adjusted to 2010 constant prices (from 2005 prices).

Table 3: GFCF by client type, 2010 prices

	<i>Rm, 2010 prices, seasonally adj annualised</i>				<i>Annual Percentage Change</i>				<i>GFCF % of GDP</i>
	General Government	Public Corporations	Private Business enterprises	Total	General Government	Public Corporations	Private Business enterprises	Total	
2007	84800	70900	367606	523306	16.4%	19.5%	10.2%	12.1%	19.9%
2008	91122	98074	401211	590407	22.9%	35.3%	8.6%	13.8%	21.8%
2009	84155	117410	349422	550987	7.5%	38.3%	9.1%	12.8%	20.7%
2010	76204	111709	341518	529431	-7.6%	19.7%	-12.9%	-6.7%	19.3%
2011	85918	112575	361245	559738	-9.4%	-4.9%	-2.3%	-3.9%	19.7%
2012	85599	115799	378518	579916	12.7%	0.8%	5.8%	5.7%	20.0%
2013	95537	119428	409162	624127	-0.4%	2.9%	4.8%	3.6%	21.1%
1 <sup>st</sup> QTR 2014	102,251	121,560	400,867	624,678	7.3%	5.7%	1.8%	3.4%	20.9%
2 <sup>nd</sup> QTR 2014	104,632	120,150	391,255	616,037	12.7%	0.2%	-3.6%	-0.4%	20.6%
3 <sup>rd</sup> QTR 2014	106,270	121,000	391,926	619,196	13.2%	0.0%	-6.3%	-2.2%	20.6%

Source: South African Reserve Bank, Quarterly Bulletin

Table 4: GFCF Building and Construction (Rm)

	<i>GFCF Residential</i>		<i>GFCF Non-residential</i>		<i>Total Residential + Non-residential</i>		<i>GFCF Construction works</i>		<i>Total (Residential, Non-residential &amp; Construction works)</i>	
	Current prices	2010 prices, SEA Adj annualised	Current prices	2010 prices, SEA Adj annualised	Current prices	2010 prices, SEA Adj annualised	Current prices	2010 prices, SEA Adj annualised	Current prices	2010 prices, SEA Adj annualised
2007	56,244	71,431	41,748	52,320	97,992	123,751	74,880	92,834	172,872	216,585
2008	60,678	65,601	57,681	61,473	118,359	127,074	128,376	134,572	246,735	261,646
2009	59,853	61,995	60,958	63,215	120,811	125,210	155,988	159,850	276,799	285,060
2010	50,645	50,645	60,810	60,811	111,455	111,456	147,831	147,831	259,286	259,287
2011	53,978	51,244	55,763	52,682	109,741	103,926	160,546	152,275	270,287	256,201
2012	55,955	50,219	56,048	49,541	112,003	99,760	164,814	148,329	276,817	248,089
2013	55,320	46,676	59,921	49,728	115,241	96,404	194,263	165,813	309,504	262,217
1 <sup>st</sup> QTR 2014	14,641	49,090	16,131	50,059	30,772	99,149	57,564	187,871	88,336	287,020
2 <sup>nd</sup> QTR 2014	13,391	42,523	15,412	48,766	28,803	91,289	57,499	189,459	86,302	280,748
3 <sup>rd</sup> QTR 2014	13,714	42,309	15,591	49,485	29,305	91,794	57,743	188,205	87,048	279,999

Source: South African Reserve Bank Quarterly Bulletin

Table 5: GFCF: Y-Y percentage change (real prices seasonally adjusted)

	<i>Residential</i>	<i>Non-Residential</i>	<i>Total Buildings</i>	<i>Construction Works</i>	<i>Total Construction</i>	<i>Total GFCF</i>
2007	-6.3%	9.0%	0.8%	44.5%	19.5%	14.0%
2008	-8.2%	17.5%	2.7%	45.0%	20.8%	12.8%
2009	-5.5%	2.8%	-1.5%	18.8%	8.9%	-6.7%
2010	-18.3%	-3.8%	-11.0%	-7.5%	-9.0%	-3.9%
2011	1.2%	-13.4%	-6.8%	3.0%	-1.2%	5.7%
2012	-2.0%	-6.0%	-4.0%	-2.6%	-3.2%	3.6%
2013	-7.1%	0.4%	-3.4%	11.8%	5.7%	7.6%
1 <sup>st</sup> QTR 2014	-6.2%	-1.8%	-4.0%	30.0%	15.8%	3.4%
2 <sup>nd</sup> QTR 2014	-1.6%	-6.9%	-4.5%	17.4%	9.2%	-0.4%
3 <sup>rd</sup> QTR 2014	-6.9%	2.5%	-2.1%	8.4%	4.7%	-2.2%

Source: South African Reserve Bank Quarterly Bulletin



## Budget 2015/16

The 2015/16 budget held very few surprises. In the interim review it was already mentioned that a considerable amount of revenue was needed to be raised in order to start paying back borrowed money and recover revenue that was lower (R14 billion) last year. This was done so in the form of an increase in the **personal tax rate of 1 percent**. More importantly, the **fuel levy** was increased by **30.5c/litre** and the **road accident levy** by **50c/litre**. This pushes up the general fuel levy to R2.55/litre and the diesel levy to R2.40/litre. The National Treasury also downgraded their estimates of South Africa's growth in 2015 from 2.5 percent to 2 percent and some key problems identified were of course the security and reliability of the electricity supply, as well as the slowing of the Chinese economy and threats in the Eurozone.

While we recognise the need to raise revenue an absolute necessity for the long term sustainability of government debt (and subsequently our governments credit rating) as well as foreign investor sentiment, our economy is to bear the brunt in the short run. The developments mentioned in the paragraph above are to have a negative effect on consumer spending amidst the oil price set to bounce back meaning that the petrol price will return to previously high levels, as well as interest rate hikes in the US and domestically on the cards this year, which will too suppress the consumer spending which is currently driving our economy.

Nene did go on to mention that non-electricity based sectors were to be heavily relied on, such as the tourism sector which would be supported. We believe that it will therefore come down to the government's ability to deal with the electricity crisis in order to make the best of an already bad situation that is crippling our economy.

Below are a few important points that were highlighted by the Minister of Finance that effects the construction sector in some way or another.

- To support home ownership in the middle-income households, transfer duties on properties below R750k have been eliminated.
- Government has eluded to the development of a **supplier database** for some time, and aims to introduce a central supplier database from April 2015. Once on the system, it will electronically verify a supplier's tax and BEE status, and enable public sector officials doing business with the state to be identified. In close collaboration with the State Information Technology Agency, a **central e-tender portal** will also be implemented from April this year. It will be compulsory that all tenders be advertised on this portal, and all tender documents will be freely available there. Tender advertisements in newspapers and the government gazette will be phased out.
- It is encouraging that the issue of non-payment was specifically highlighted by the Minister, as non-payment is a serious issue affecting the construction industry. Quoted by the Minister: "**The non-payment of suppliers** on time is a perennial problem that needs serious attention. This practice works against government's efforts to grow the economy and develop the SMME sector. Payment of suppliers within 30 days will now be included among other SCM requirements in the performance agreements of accounting officers."
- The following infrastructure allocations were highlighted by the Minister:
  - R1.1 billion is allocated for the upgrade of the Moloto Road to improve safety and mobility on this road.
  - The Passenger Rail Agency's R53 billion ten-year renewal programme is now in progress. The first 44 new train sets, or 528 coaches, will be delivered over the next three years.
  - Over R80 billion is allocated to over 220 water and sanitation projects and for local roads.
  - R105 billion will be spent on housing and associated bulk infrastructure requirements.
  - Over R18 billion in electrification funding will provide for 875 000 households to be connected to the grid or to receive off-grid electricity.
  - R1.1 billion is allocated for broadband connectivity in government institutions and schools.

- **Health and education infrastructure:** A new approach to funding health and education infrastructure in provinces was introduced in 2013. This means that provinces that meet the minimum planning standards have been rewarded with additional allocations. As an example, the Eastern Cape receives an additional R233 million due to the quality of its plans for health and education infrastructure investment. Provinces that failed to meet the minimum standards will be prioritised for assistance through the on-going Infrastructure Delivery Improvement Programme. This allocation methodology will be expanded over the MTEF period so that all provincial departments continuously improve their planning to be eligible to receive incentive allocations. From May 2015 all school building plans will be standardised and the cost of construction will be controlled by the Office of the Chief Procurement Officer. We also hope that the Department of Education will take serious measures to improve payment procedures, following numerous complaints from contractors, surveyed through our Preferred Supplier Survey, involved in school building projects across the country of poor, late or even no-payment.
- Investing in the maintenance of **urban infrastructure** also received attention, as the Minister reported that local government infrastructure grants will receive special attention towards the **maintenance of infrastructure**.
- On the issue of **Eskom**, it will apply to the regulator again this year for adjustments towards cost-reflective tariffs, in order to stabilise its financial position. In October 2014 government announced a broad package for Eskom, including a capital injection of R23 billion, governance improvements, operational cost containment and additional borrowing and support for required tariff increases. The fiscal allocation of R23 billion will be paid in three instalments. Treasury has increased the electricity levy by 2c/kWh to 5,5c/kWh until such time the shortage is over (which could be a two to three year period). Other measure to deal with energy development include enhancing the accelerated depreciation for solar photovoltaic renewable energy. The carbon tax will be introduced in 2016 to deal with electricity shortage, while lowering the electricity levy.
- **State owned entities will invest about R360bn** over the next three years. Government is taking measures to deal with SAA and the South African Post Office.
- The **IDC** will promote faster development through industrial development, mineral beneficiation and agro-processing by investing R100 billion over the next five years. The **DBSA** will continue to manage the Infrastructure and Investment Programme for South Africa and will continue to play a key role in the development of new generation electricity capacity from hydro, coal and gas.
- And finally, SA last year finally signed a treaty for the establishment of a new **multilateral development bank** to be based in Shanghai, **China**. Previous reports referred to this as the BRICS Development Bank, but this was not mentioned today by the Minister. The first regional office of the Bank will be located in South Africa. It is hoped that SA will have some leverage on the \$100 billion resources that will support future infrastructure investment locally as well as Sub-Saharan African countries. Each member of the bank (BRICS – and including South Africa) will each initially contribute \$10 billion, according to media reports. The question is therefore asked where does the SA government get R100 billion to invest in the establishment of a new bank, when funding for our own infrastructure is dwindling?

Infrastructure expenditure by the public sector is projected to increase by 4,3 percent in 2015/16 to R273bn, -0,2 percent in 2016/17 (R273bn) and -2,7 percent in 2017/18 (R266bn), averaging an increase of just 0,5 percent over the next three years. In real terms, expenditure is therefore projected to contract on a year on year basis for the next three years. Expenditure by SOE's (currently regarded as the largest client to the civil industry) is projected to fall by 10 percent this year before contracting by between 6,0 percent and 8,0 percent in the next two years. Expenditure by government is projected to fall by 0,3 percent in 2015/16 and increase by below inflationary levels in the next two years.

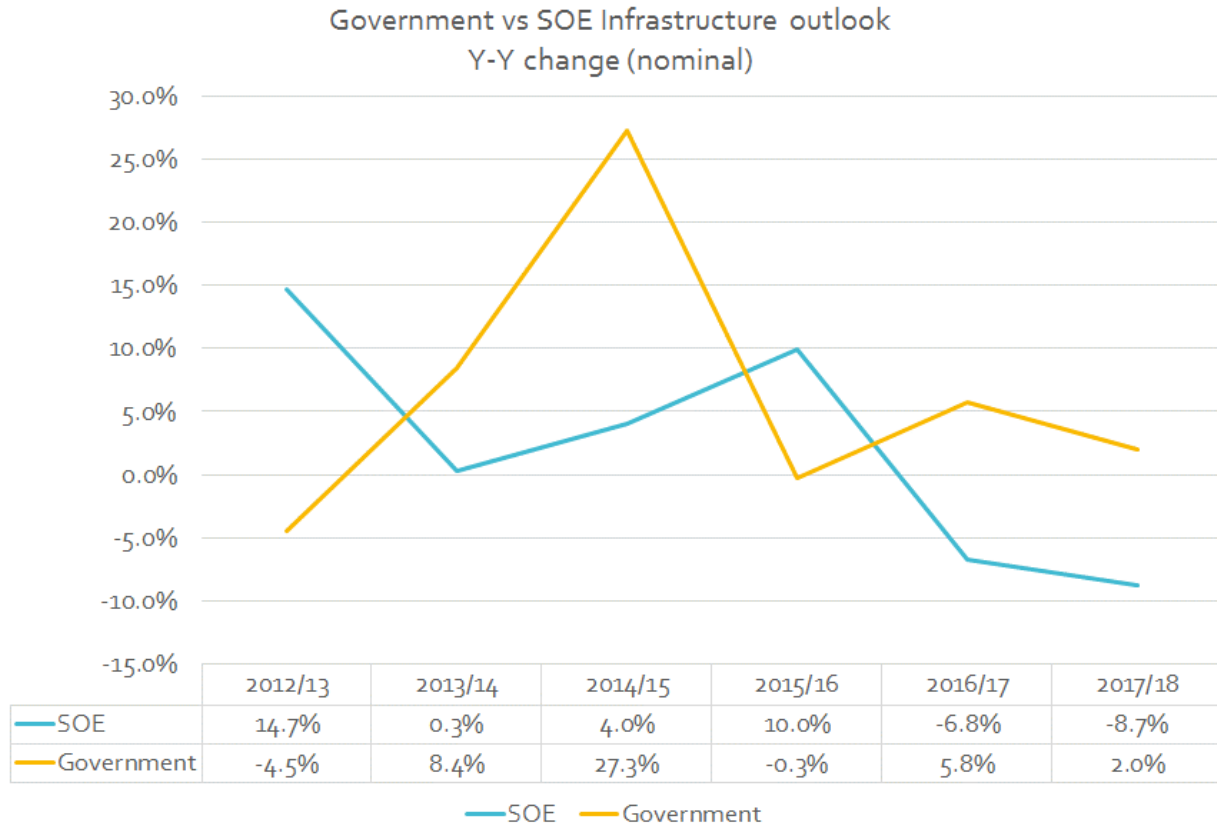


Figure 3: Infrastructure Expenditure Growth outlook, SOE's vs Government

Table 6: Public Sector Infrastructure Expenditure: Rm, current prices

	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	MTEF Total
Economic services	176100	183900	215200	228100	224800	215500	668400
Energy	75100	69500	69200	71100	56000	39200	166300
Water and Sanitation	22600	26200	34800	37300	39800	40300	117400
Transport and logistics	69500	76400	93700	104300	113500	121300	339100
Other economic services	8900	11800	17500	15400	15500	14700	45600
Social services	30200	33200	34700	34400	35700	36700	106800
Health	9700	10600	9700	9300	9900	10300	29500
Education	9800	12300	13500	14500	14500	14800	43800
Other social services	10700	10300	11500	10600	11300	11600	33500
Justice and protection services	4400	4000	3900	4500	5200	5500	15200
Central government, administrative and financial services	6900	5800	8600	6900	7700	8200	22800
<b>Total</b>	<b>217,600</b>	<b>226,900</b>	<b>262,400</b>	<b>273,900</b>	<b>273,400</b>	<b>265,900</b>	<b>813,200</b>

Table 7: Public Sector Infrastructure Expenditure: Y-Y Percentage Change (Current prices)

	2012/13	2013/14	2014/15	2015/16	2016/17	2017/18	MTEF Total
Economic services	4.9%	4.4%	17.0%	6.0%	-1.4%	-4.1%	0.1%
Energy	11.9%	-7.5%	-0.4%	2.7%	-21.2%	-30.0%	-16.2%
Water and Sanitation	17.7%	15.9%	32.8%	7.2%	6.7%	1.3%	5.0%
Transport and logistics	-0.9%	9.9%	22.6%	11.3%	8.8%	6.9%	9.0%
Other economic services	-22.6%	32.6%	48.3%	-12.0%	0.6%	-5.2%	-5.5%
Social services	-3.2%	9.9%	4.5%	-0.9%	3.8%	2.8%	1.9%
Health	26.0%	9.3%	-8.5%	-4.1%	6.5%	4.0%	2.1%
Education	25.6%	25.5%	9.8%	7.4%	0.0%	2.1%	3.2%
Other social services	-31.8%	-3.7%	11.7%	-7.8%	6.6%	2.7%	0.5%
Justice and protection services	57.1%	-9.1%	-2.5%	15.4%	15.6%	5.8%	12.2%
Central government, administrative and financial services	6.2%	-15.9%	48.3%	-19.8%	11.6%	6.5%	-0.6%
Total	4.4%	4.3%	15.6%	4.4%	-0.2%	-2.7%	0.5%

In other news Gauteng has set aside R10bn for five development corridors across the province. These include:

- The central development corridor (focussing on the financial sector, information and communications technology) is allocated R3,1 billion for infrastructure funding including R979m for human settlement R789m for new schools and refurbishment of existing classrooms, R543m and R263m for rehabilitating and building new roads and construction of new health care facilities
- The Eastern Development Corridor (focussing on manufacturing, logistics and transport), is allocated R2 billion, including R983m for human settlement
- Northern Corridor (focussing on the automotive sector and the knowledge based economy) is allocated R2bn, including R964m for human settlement
- The Western Corridor (focussing on new blue and green economic initiatives, as well as tourism, agro-processing and logistics) was allocated R1,4 bn
- The Southern Corridor (focussing on river tourism and agro-processing), is allocated R1,5bn including R892m for human settlement.

In the Western Cape, land is being cleared and progress is made at SA's first IDZ to be developed exclusively for oil and gas services. The IDZ will be an oil and gas services complex in the Port of Saldanha Bay and is expected to be up and running within four years. We are still however waiting for Minister of Trade and Industry to sign the SEZ act into law.

A total of 77 bids were received in the 4<sup>th</sup> window under government's Renewable Energy Independent Power Producer Procurement Programme. Investment by the private sector nearly doubled during 2013 in renewable energy projects but this growth is likely to slow substantially over the next few years as Eskom is financially unable to connect completed projects to the grid. This will inevitably delay implementation of future projects.

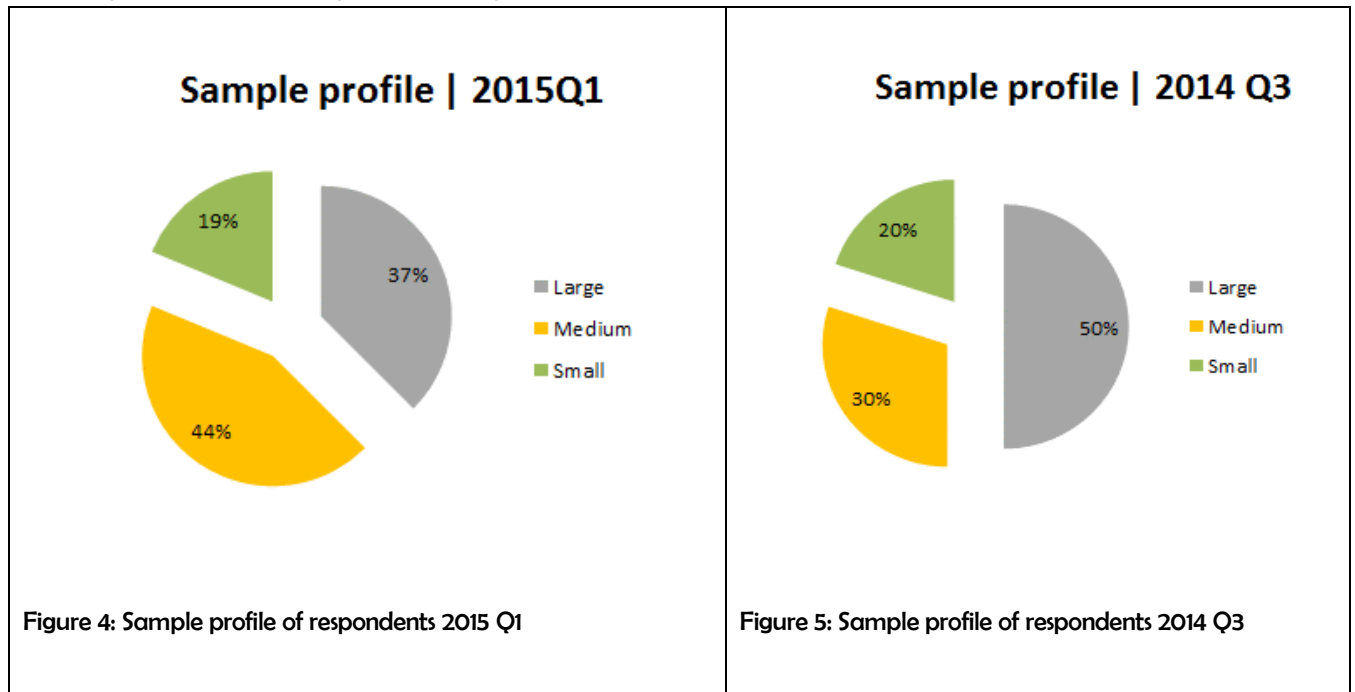
# THE POSITION OF THE CIVIL ENGINEERING INDUSTRY

## Background

- SAFCEC reviewed and redesigned the questionnaire which was distributed to all SAFCEC members during February 2015.
- 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.
- No survey was compiled for the 4<sup>th</sup> quarter of 2014. Where possible data from the 1<sup>st</sup> quarter 2015 survey results were used to determine conditions in the 4<sup>th</sup> quarter of 2014.

## Sample profile

In the 3<sup>rd</sup> quarter 2014 survey, large firms represented 50% of the sample, compared to 40% in the previous survey. This will impact the analysis of the data due to the fact that responses are weighted. Medium size firms represented 30% compared to 40% in the previous survey.



## Financial Statistics

Following a 1,8 percent q-q decline in nominal **turnover** during the last quarter of 2014 (compared with the 3<sup>rd</sup> quarter), real turnover ended 10,0 percent y-y lower when compared to the same quarter in 2013. Turnover fell for the second consecutive year, down 2,5 percent in 2014 and -10,0 percent in 2013.

More than half of the large contractors reported an increase in quarter on quarter employment. **Employment** increased by 2,3 percent q-q, supported by a 3,3 percent q-q increase in employment by large contractors, but was counteracted by a 7,5 percent q-q decline in employment by medium size contractors. Close to 60 percent of medium size firms reported a decline in employment between the 3<sup>rd</sup> and 4<sup>th</sup> quarters of 2014. A split in the quarter on quarter change between limited duration and permanent employees is provided in the table below.

*Table 8: Employment change q-q, by firm size*

	<i>Limited Duration</i>	<i>Permanent Employees</i>	<i>Total</i>	<i>% Limited Duration of total workforce</i>
Large	-9%	16%	3.3%	45.3%
Medium	-11%	-3%	-7.5%	55.2%
Small	0%	0%	0.0%	49.3%
Total	-9%	14%	2.3%	46.1%

The nominal value of **salary and wages** was unchanged in the 4<sup>th</sup> quarter, following a 10 percent q-q increase in the 2<sup>nd</sup> quarter. The contribution of the salary and wage bill to turnover averaged 24,0 percent, slightly higher than the average of between 22,0 percent and 23,0 percent, reported in previous surveys.

Late payments had a greater impact on medium size firms during the period under review. Although there was a 7,0 percent q-q overall decrease in the **nominal value of late payments**, for civil works completed and already invoiced in 2014Q4 compared to Q3, medium size firms reported an increase of 8 percent during the same period. Majority of the large contractors reported a drop in the value of late payments, averaging -10,0 percent q-q. However as a percentage of turnover, late payments (including all time frames from 30 days to more than 90 days) accelerated to an average of 14,8 percent (from 12,4 percent and 17,5 percent in the two previous surveys). To remove some of the volatility in the data, a two quarter moving average (Measured over a "two survey" period), moderated to 13,6 percent (from 14,9 percent). The current average rate was still higher, when compared to an average of 11,0 percent in 2011.

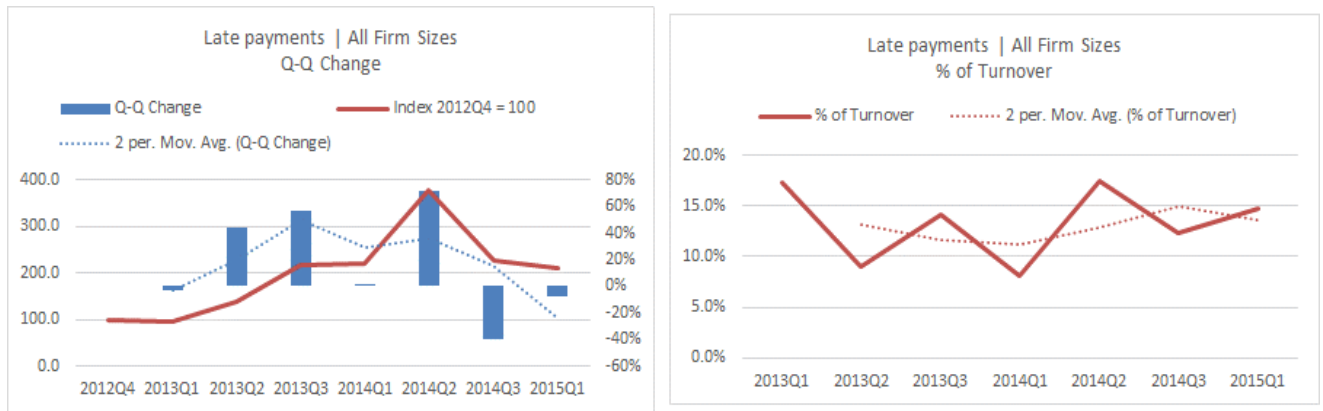


Figure 6: Late payments

The nominal value of the "two year forward order book" for South Africa surprised on the upside, and increased by an average of 6,6 percent q-q in the 4<sup>th</sup> quarter, compared with a 9 percent q-q decrease during the 3<sup>rd</sup> quarter. The nominal value of order books for large contractors increased by 7,5 percent q-q, but in spite of this large contractors nonetheless remained negative in terms of their outlook on domestic order books, with 66 percent of the contractors of the opinion their order books are low (from 60 percent in the previous survey). By contrast, 66 percent of the medium size firms were satisfied with the level of their order books, during the current survey, but there has been a shift away from those feeling the levels were deemed as "good" in the Q3 survey.

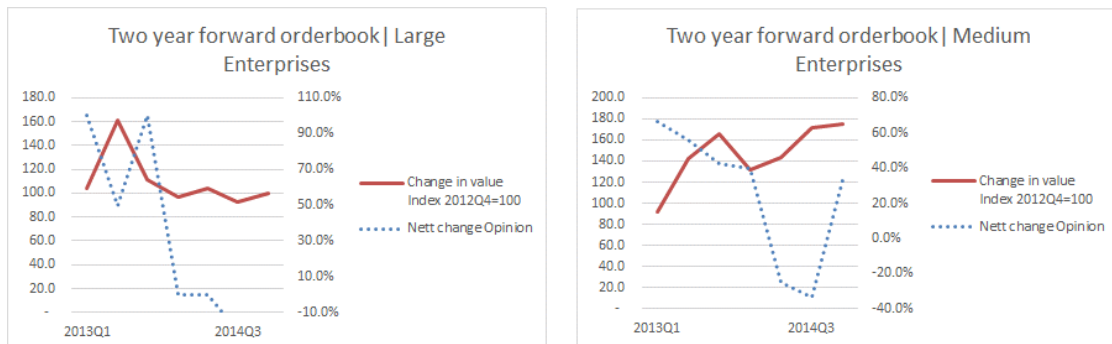


Figure 7: Two year forward order book

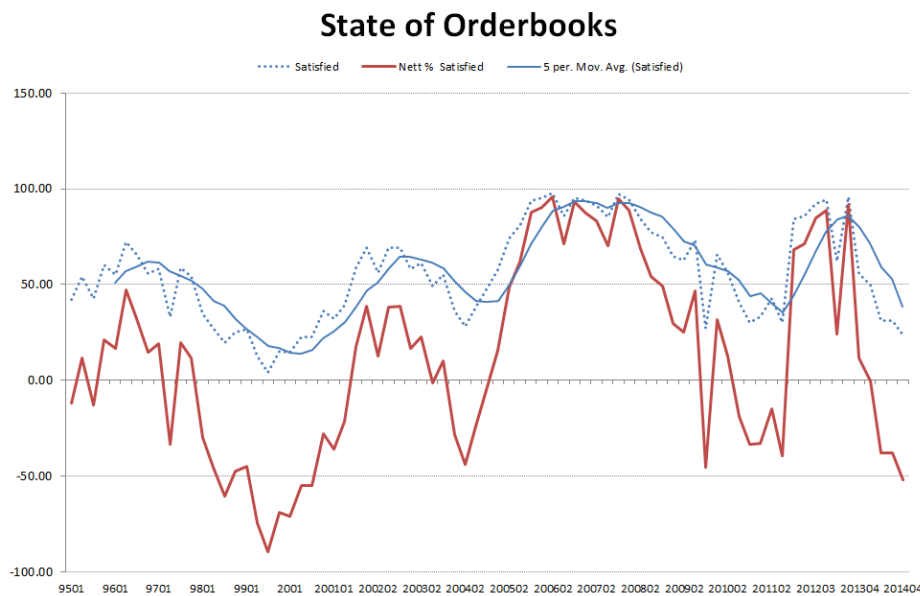


Figure 8: Opinions related to Order books

Opinions related to the order book are more erratic, but the trend line (solid blue line on the chart above) has, as expected, reached an upper turning point by mid 2013, suggesting opinions are becoming increasingly pessimistic. The nett % satisfaction rate deteriorated from a positive 11 percent in the 4<sup>th</sup> quarter of 2013, to -52,0 percent in the 4<sup>th</sup> quarter of 2014. This is the weakest level since 1999/2000 and the third consecutive quarter that it is in negative territory.

## Financial performance of listed companies

Table 9: Unaudited 6-months ended December 2014

Summary of financial results			
	2014 (Full year)	December 2013 6-months	December 2014 6-months
Revenue <sup>1</sup>	137,044	66,934	61,366
Revenue, Per Change	7.9%	-	-8.3%
Operating Margins, Avg	1.0	3.0	2.4
Order Book	147,451	130,651	126,431
Order Book, Per Change	11.6%	-	-3.2%
Ratio	1.1	2.0	2.1

Source: Company Financial Reports, Industry Insight analysis

An analysis of company results, for the 6 months ended December 2014, shows that cumulative revenue growth contracted from an average growth of 7,9 percent in 2014 to -8,3 percent in the six month period under review.

<sup>1</sup> Aveng, Group Five, WBHO



Revenue was largely adversely affected by a slowdown in the civil engineering divisions. Operating margins are still under pressure and averaged 2,1 percent for the period under review, compared with an average of 2,0 percent in the 6 months to December 2013. All of the companies included (Aveng, Group Five, WBHO and Murray & Roberts) reported either stable or weaker margins. The aggregated order book of the before mentioned companies fell by 3,2 percent (or by R4,2bn) to R126,4 billion (R130,6 billion December 13). WBHO and Group Five reported an average increase of 5,5 percent in the value of their order books (in the six month period to December 2014), while Aveng reported no change during the same period in the value of their order books. Murray & Roberts, negatively affected by a slowdown in the oil and gas sector alongside a weaker outlook in civil engineering infrastructure, reported a 15,8 percent drop in the value of their order book up to December 2014.

Revenue was supported by involvement in renewable energy projects, retail developments in and around the Gautrain Precinct and the new King Shaka Airport in KZN, while there have also been reports of increased momentum in the development of affordable as well as luxury housing (although not expected to be sustained). Revenue is also influenced by cross border activities which is expected to intensify contributing a larger portion of the order book which will impact on future revenue growth and profitability.

Two companies reported a change in leadership, including Group Five, who appointed Eric Vemer as new CEO, with effect 1 December 2014 and Neville Nicolau, appointed as new CEO for Basil Read, effective 1 September 2014.

## Industry Profile

The following section provides a snapshot view of responding firms' turnover earned by project type, client and province during the 4<sup>th</sup> Quarter of 2014, surveyed in February 2015. This is not necessarily representative of the entire industry, but shows the significant contribution by the roads segment to large, medium and small contractors.

Table 10: Turnover distribution by sub-discipline

Discipline	Large	Medium	Small	Total 2014Q1	Total 2014Q2	Total 2014Q4
Roads	38.1%	78.3%	42.3%	53.8%	27.5%	74.4%
Earthworks	9.3%	0.0%	29.0%	4.5%	4.8%	0.9%
Water Bulk Infrastructure	5.7%	0.0%	0.0%	5.9%	10.2%	0.6%
Water and Sanitation	2.9%	0.2%	0.0%	3.9%	0.0%	0.4%
Rail	4.1%	0.0%	0.0%	0.7%	1.8%	0.4%
Harbours	0.5%	21.5%	0.0%	0.1%	0.7%	19.5%
Power (bulk)	19.8%	0.0%	0.0%	11.4%	24.4%	1.9%
Power (services)	0.0%	0.0%	0.0%	2.4%	1.4%	0.0%
Airports	0.0%	0.0%	0.0%	1.9%	0.0%	0.0%
Mining Infrastructure	7.1%	0.0%	0.0%	5.8%	8.5%	0.7%
Mining (Surface earthworks)	0.4%	0.0%	0.8%	3.0%	1.4%	0.0%
Other	12.0%	0.0%	27.9%	6.6%	19.2%	1.2%

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Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%
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Table 11: Turnover distribution by client

	Large	Medium	Small	Total 2014Q1	Total 2014Q2	Total 2014Q4
Central	6.3%	23.9%	0.0%	16.4%	15.1%	8.1%
Provincial	9.2%	36.5%	3.6%	9.2%	3.0%	12.1%
Local	6.8%	32.1%	0.0%	5.6%	6.5%	9.4%
Corporations	34.0%	6.0%	0.0%	27.1%	36.4%	30.5%
Private	43.8%	1.5%	96.4%	41.8%	39.0%	39.9%
Total	100.0%	100.0%	100.0%	100.0%	100.0%	100.0%

Data for the third quarter not available

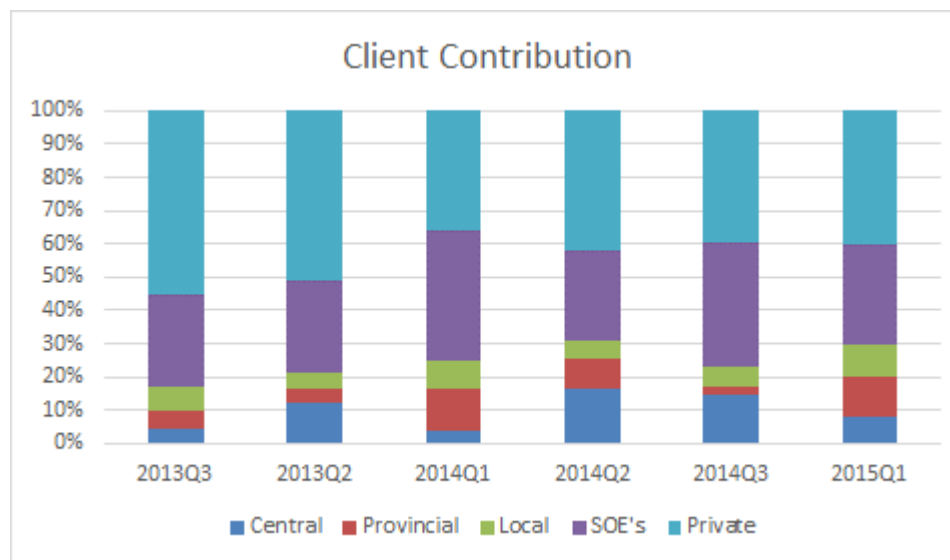


Figure 9: Client contribution to turnover

The contribution by the private sector in this survey was relatively unchanged at 39,9 percent, but the contribution by central government moderated to 8,1 percent (Q3: 15%), while provincial government escalated to 12 percent (Q3 3%). Turnover by state owned corporations dropped to 30,0 percent from 36,0 percent in the previous survey.

Table 12: Geographic Distribution of the value of civil engineering construction work (turnover)

Province	Large	Medium	Small	2014Q1	2014Q2	2014Q2
GAU	20%	68%	4%	17%	19%	58%
WC	9%	0%	0%	13%	6%	2%
EC	5%	30%	0%	6%	4%	25%
NC	1%	0%	0%	7%	6%	0%
MPU	32%	0%	0%	20%	23%	7%
FS	7%	0%	0%	8%	9%	2%
LIM	11%	0%	0%	11%	10%	2%
NW	2%	1%	88%	2%	3%	1%
KZN	12%	0%	8%	17%	18%	3%
Total	100%	100%	100%	100%	100%	100%

Gauteng had a significant impact on this quarter's survey, contributing on average 58,0 percent of total turnover, followed by the Eastern Cape, which contributed 25 percent, due to an increased presence by the medium size contractors. Larger firms were more active in Mpumalanga and Kwazulu Natal by comparison to the medium size firms.

In order to fill the void in the regional sample, a comparison between survey results and an independent database of domestic civil contracts awarded over the last four quarters, is included in the next section. Please note that the project database unfortunately excludes infrastructure related to mining developments, an important discipline to the larger construction firms. Nonetheless it provides a yardstick for comparative purposes. A breakdown by province is also provided.

Table 13: Value (nominal) of civil contracts awarded: Y-Y change (same qtr previous year)

	2013 Q2	2013 Q2	2013 Q4	2014Q1	2014 Q2	2014Q3	2014Q4	2014	2013	2012
EC	35%	41%	-49%	89%	-28%	79%	91%	51%	7%	-9%
FS	17%	-67%	16%	-42%	127%	58%	46%	25%	-5%	56%
GAU	77%	20%	34%	-64%	-81%	158%	-60%	-28%	55%	6%
KZN	-25%	30%	44%	17%	176%	25%	-57%	21%	42%	-5%
LIM	-74%	-34%	-47%	109%	5%	435%	181%	136%	-59%	-45%
MPU	-3%	-42%	-91%	-62%	-90%	-26%	1220%	-48%	-18%	-11%
NW	445%	-92%	-80%	-43%	-42%	841%	129%	2%	1%	43%
NC	-44%	-88%	-75%	-65%	-77%	87%	74%	-40%	-52%	15%
WC	21%	173%	41%	-25%	-51%	-80%	-7%	-44%	46%	-12%
TOTAL	3%	-2%	-14%	-19%	-21%	49%	4%	-1%	10%	-6%

The nominal value of civil contracts awarded fell by 1 percent y-y in 2014, (or by 7,5 percent in real terms), compared with a 10 percent y-y nominal increase (or 3,7 percent in real terms) in 2013. The value of civil awards increased during the second half of 2014 compared with the same period in 2013 (up by 49 percent and 4 percent y-y during the 3<sup>rd</sup> and 4<sup>th</sup> quarters respectively) but was not enough to counterbalance the strong decline reported during the first half of 2014. The national trend does however not reflect provincial activities. A few provinces reported strong double-digit growth during 2014, including Eastern Cape, Free State, Kwazulu Natal, and Limpopo. The value of awards in Gauteng fell by 28 percent y-y during 2014, with between 40 and 44 percent declines reported in the Northern and Western Cape.

In stark contrast to the dismal performance in the civil industry, the nominal value of building contracts awarded increased by 54,0 percent y-y during 2014. The value of building awards started showing more positive growth from the 4<sup>th</sup> quarter of 2013 and has recorded double digit growth on a year on year basis for five consecutive quarters as at the 4<sup>th</sup> quarter of 2014. Growth did however slow to an increase of 13 percent y-y in the 4<sup>th</sup> quarter compared with the same quarter in 2013, the slowest rate of increase since the uptick in 2013Q4.

A provincial summary based on the real value of civil contracts awarded are included in **Annexure C**.

## 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 (1<sup>st</sup> quarter 2015).

The mostly negative market sentiment continues to prevail since 2009, but the level of sentiment expressed by respondents have reached new lows during the 1<sup>st</sup> quarter of 2015.

**The nett % satisfied with working conditions** during the 4<sup>th</sup> quarter 2014, fell to -56,9, from -2,2 In the previous survey, as majority of contractors reported quiet conditions (56,0 percent. A positive rate implies more firms reported improved business conditions, while a negative rate implies a growing number of firms have a more pessimistic outlook on the industry.

The nett % satisfied with working conditions in the 1<sup>st</sup> quarter of 2015 deteriorated further to -95.9 from -50.1. The outlook for the 2<sup>nd</sup> quarter of 2015 remains negative (-78,1), as only 18 percent of contractors expect (at best) satisfactory conditions. The majority expect the more depressed conditions to continue into the following quarter.

**Competition for tenders** has reportedly eased somewhat during 2014, but an increasing number of contractors (4,6 percent from 1,9 percent in the previous survey), reported higher levels of competition of between 11 and 25 bids per tender in the 1<sup>st</sup> quarter of 2015. Tender prices remain under pressure with only 1,1 percent of respondents saying tender prices were reasonable. Majority reported tender prices as keen (87,5 percent) or very low (11,5 percent).

While current business conditions are clearly more depressed affecting tender prices and profitability, the more negative outlook in terms of **order books** suggests these difficult times are likely to continue or get progressively worse. The nett % satisfaction rate fell deeper into negative territory from -37,8 percent in the 3<sup>rd</sup> quarter to -52.2 in the 1<sup>st</sup> quarter of 2015. Order books are negatively affected by the slow roll-out of public infrastructure, low confidence in mining sector which is delaying capital expenditure, while projects are broken into smaller projects, benefitting Grade 7 and 8 contractors more so than Grade 9 contractors, but even this has worsened to even lower Grade projects.

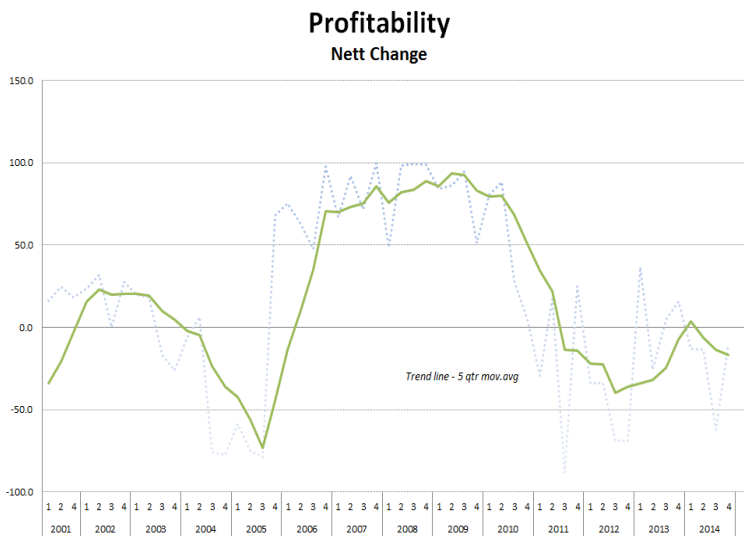


Figure 10: Opinions related to Profitability

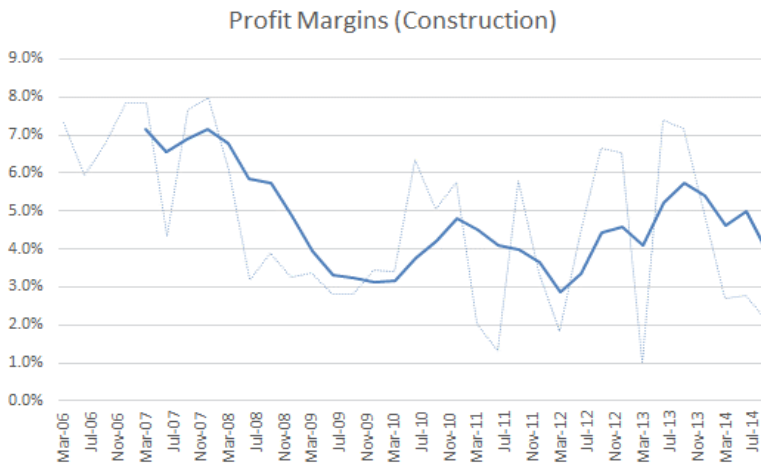


Figure 11: Profit Margin (Source Statistics South Africa, PO044)

In line with the overall negative market sentiment, majority of respondents reported low to very low **profitability** (55,3 percent), but a slightly higher percentage by comparison to the previous survey said it was at a satisfactory level (44,8 percent vs 18,8 percent in the previous survey). The nett % satisfaction rate improved, but remained in negative territory, to -10,5 from -62,3 in the previous survey. The trend line (based on a 5 qtr moving average), has been in negative territory for the past three years (since 2011).

According to Stat SA's estimates, profit margins eased to an average of 2,1 percent in the 3<sup>rd</sup> quarter of 2014 (latest available data), from 2,8 and 2,7 percent in the two previous quarters. Margins are more erratic, a trend mirrored by the confidence index depicting profitability. Thus smoothed over a four quarter period, profit in rand terms fell by 37 percent y-y by the 3<sup>rd</sup> quarter, the strongest decline since 2011 when profit fell by 40 percent. In rand terms, industry profitability contracted by R6bn to R10,2 bn from R16,3 bn (as at 3<sup>rd</sup> quarter 2013).

## Capacity Utilisation and Plant equipment

Capacity utilisation in terms of general plant and resources recovered marginally in the 4<sup>th</sup> quarter of 2014, as an increasing number of contractors (58 percent compared with 36 percent) reported utilisation levels of between 76 percent and 90 percent.

A higher percentage of plant equipment was standing idle during the period under review, with 43 percent of contractors having reported that between 26 percent and 50 percent of plant equipment was standing idle, compared with the majority saying that less than 25 percent was idle in the previous quarter.

Firms spent around 15 percent y-y less on hiring and leasing of equipment during the first three quarters of 2014 compared with the previous year, according to estimates provided by Stats SA (Publication P0044). According to Stats SA approximately 2,1 percent of turnover was spent on hiring and leasing of plant equipment during the 3<sup>rd</sup> quarter of 2014.

Medium size firms are spending a higher portion of their turnover on hire/leasing of plant equipment, but the ratio has slowed from 6, 0 percent on average in the first three quarters of 2013 to 4, and 2 percent in the 3<sup>rd</sup> quarter. Larger enterprises spent an average of 2, 3 percent of turnover on plant equipment in the first nine months of 2014. Larger companies would generally require less expenditure on plant equipment as they have the ability to own a large portion of their plant equipment, while it made better economic sense for medium and smaller companies to either hire or lease equipment as demand dictates. It does however mean that the expected increase in the cost of plant and equipment in 2014 could have a more serious impact on the profitability of medium and smaller size contractors.



## Opinions related to tenders, awards, order books and turnover

### Tender activity

*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.*

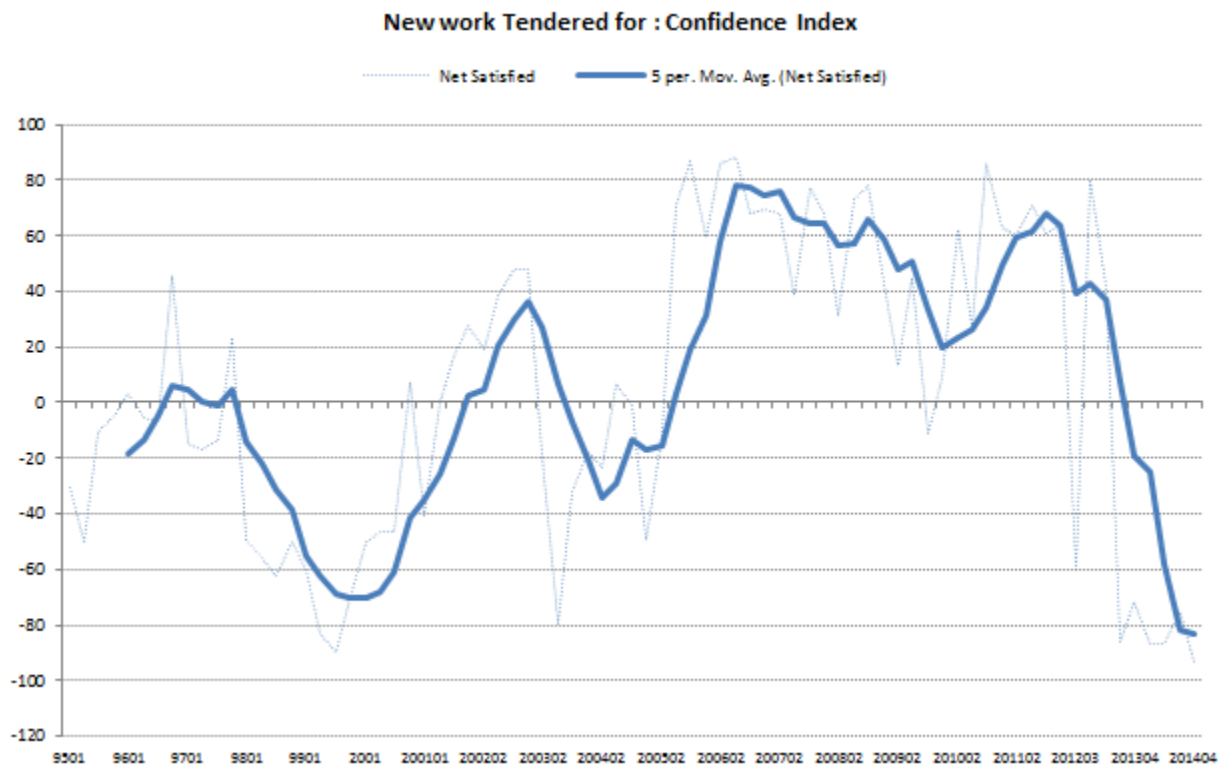


Figure 12: Opinions of new work tendered for

Majority of firms continued to express their dissatisfaction with tender volumes. The nett satisfaction rate remained at almost historical record low levels over the past five surveys, recovered marginally to -75.3 percent in Q2, before deteriorating again to -93.1. The trend line based on a 5 quarter smoothed average, is now deep in the red and still on a downward trajectory.

Growth in civil tender activity remained on the downward trajectory. Tender activity fell by 18 percent y-y in 2014, but on a more positive note, because of an increase in the number of grade 9 contracts out to tender (which increased by 38 percent from 55 to 76 in 2014) the estimated value of tenders increased by 19,8 percent y-y (nominal terms). From around mid-2013, based on a 12 month mov.avg, there has been a notable increase in the number of grade 9 contracts out to tender, while simultaneously the overall trend (including contracts from all grades) started to decline.

Bulk of tender activity in the 4<sup>th</sup> quarter related to Grade 7 local municipal tenders.

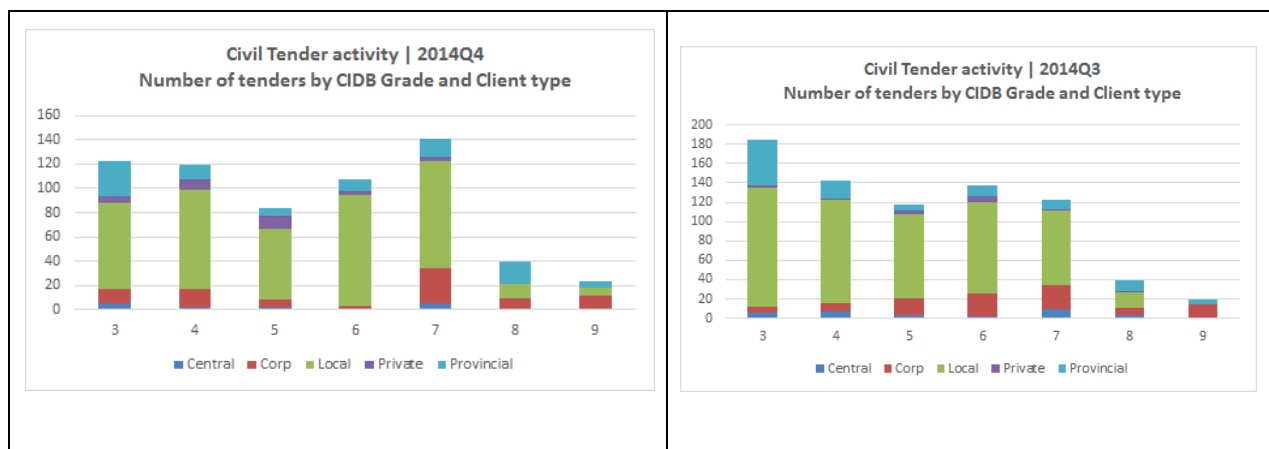


Figure 13: Civil Tender Activity

Table 13: Civil Tender activity by known CIDB grade

Year, Quarter	3	4	5	6	7	8	9	Total
201201	211	146	95	92	72	28	14	658
201202	218	112	77	91	112	39	12	661
201203	261	170	120	130	123	43	15	862
201204	198	185	134	155	76	39	10	797
201301	246	123	97	106	59	31	9	769
201302	316	153	132	120	102	31	7	671
201303	239	188	152	173	109	30	15	906
201304	175	124	101	139	111	68	24	742
201401	180	158	108	113	92	33	9	693
201402	220	136	126	124	120	49	24	799
2014Q3	190	150	123	138	123	39	19	782
2014Q4	122	121	84	108	141	41	24	641

## Est Civil Tender Values (Rm)

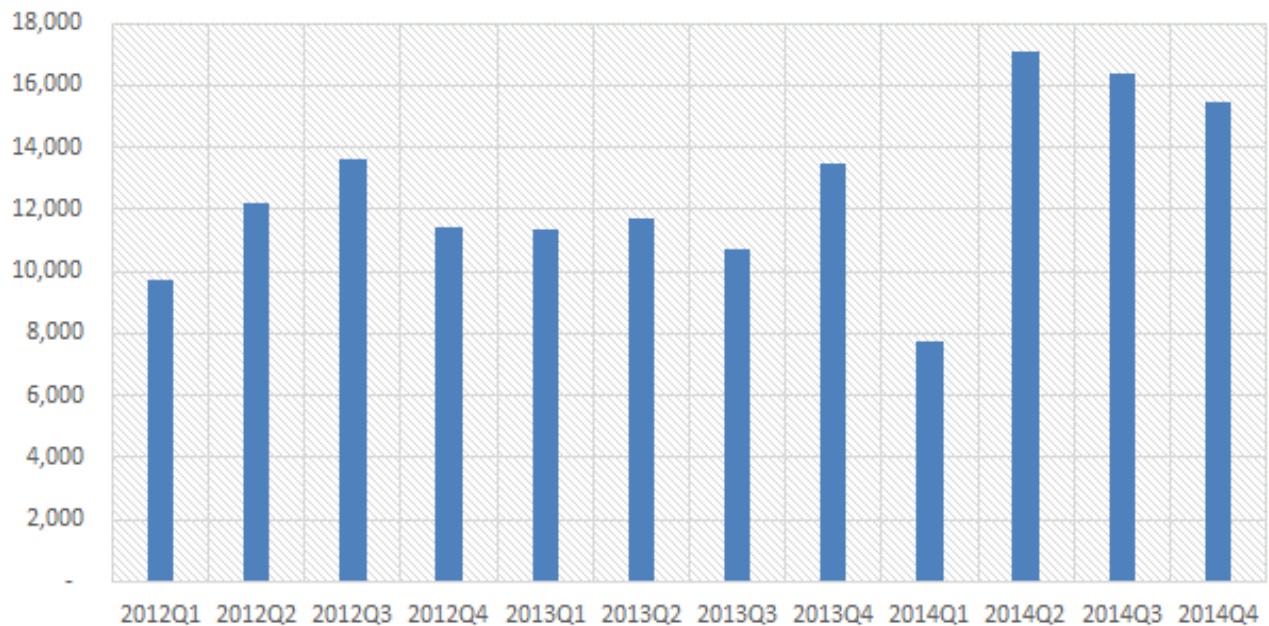


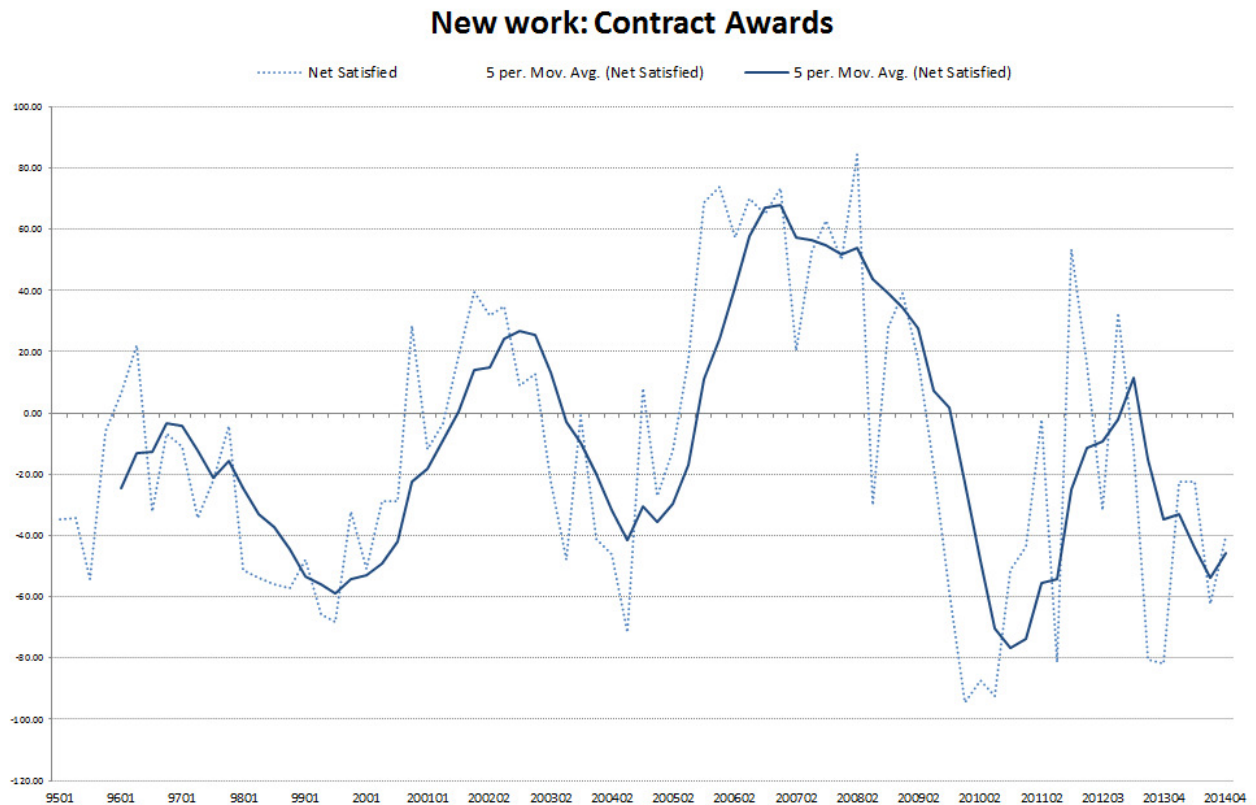
Figure 14: Estimated Tender Values (RM)

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

	Air	Bridges	Civil Other	Power	Rail	Road	Water	Grand Total	Y-Y Per. Change (Nominal)
2012Q1	12	206	244	610	-	4,289	4,399	9,759	
2012Q2	-	87	549	404	16	4,919	6,247	12,223	
2012Q3	11	194	289	765	235	6,625	5,466	13,585	
2012Q4	-	197	498	778	13	6,392	3,527	11,404	
2013Q1	-	125	668	548	-	6,378	3,614	11,333	16.1%
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%

Source: Industry Insight Project Database, Databuild

## Awards



*Figure 15: Opinions related to Awards*

Contractors remained negative in terms of the awarding of contractors, although there was a slight improvement in the nett % change from -62.4 to -40.0. This reversed the 5 quarter trend slightly upward, albeit just marginally. However even a higher percentage reported satisfactory levels (29%), 7,6 percent of contractors reported “nil” levels, the highest since the 1<sup>st</sup> quarter of 2013 (8.2%). Be that as it may, the quarter on quarter intricacies in the movement of the index does little to change the glaringly oblivious state of affairs that contractors are negative with regards to the pace by which contracts are awarded.

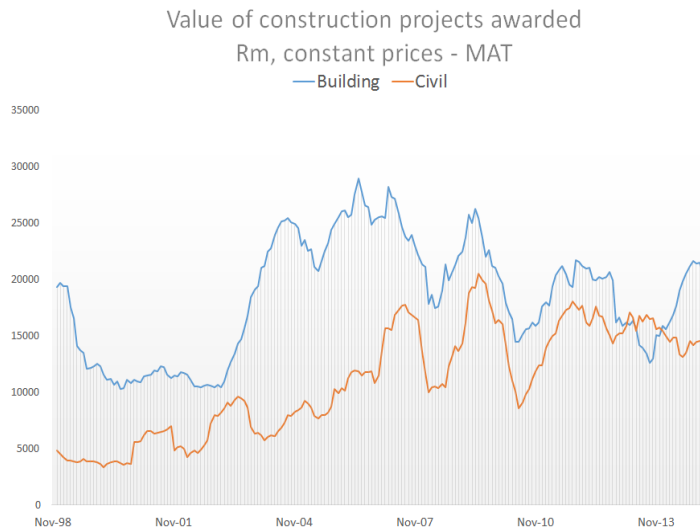


Figure 16: Real value of construction projects awarded

### Construction sector growth supported by building industry recovery

The annual growth rate in the nominal rand value of construction projects awarded increased by 17,2 percent y-y in 2014, from -3,0 percent in 2013. The outlook for construction has therefore improved on the back of stronger growth in the building industry where the value of awards increased by 43 percent y-y in 2014. It may seem however that the current growth cycle will be shortlived considering the weakening economic outlook and slowdown in pipeline projects. A few large housing projects (to be completed over many years) were also awarded during 2014 which has distorted the data somewhat considering the fact that these projects will take years to complete. By stark contrast the value of civil projects awarded during the same period contracted by 7,5 percent y-y.

### Projects postponed

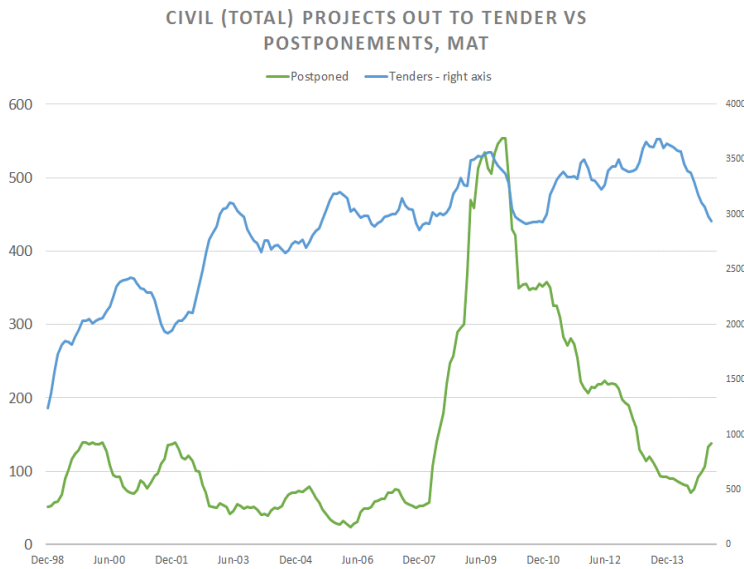


Figure 17: Projects postponed

The number of civil projects placed on hold increased by 44,6 percent in 2014 compared to 2013, with a notable acceleration from mid-2014 onwards, shortly after the finalisation of the 2014 National Elections. Although tender activity generally slowdown after an election period (as seen in 1999, 2004, 2009 and 2014), by on average between 15 percent and 20 percent, the contraction in 2014/15 is the strongest year on year decline since 1999, and is worsened by the simultaneous increase in the number of projects being held back.

## Turnover and Employment

Turnover fell by 1,8 percent y-y in the 4<sup>th</sup> quarter compared to the previous (3<sup>rd</sup>) quarter, which in real terms translated to a 10,0 percent y-y decline when compared to the same quarter in 2013. Turnover for the year is estimated to have increased by 2,6 percent y-y in nominal terms, but if construction cost is taken into consideration, real turnover fell by an estimated 2,5 percent y-y in 2014 and by 10,0 percent in 2013.

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 value of civil contracts awarded last year, 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 2015/16 Budget.

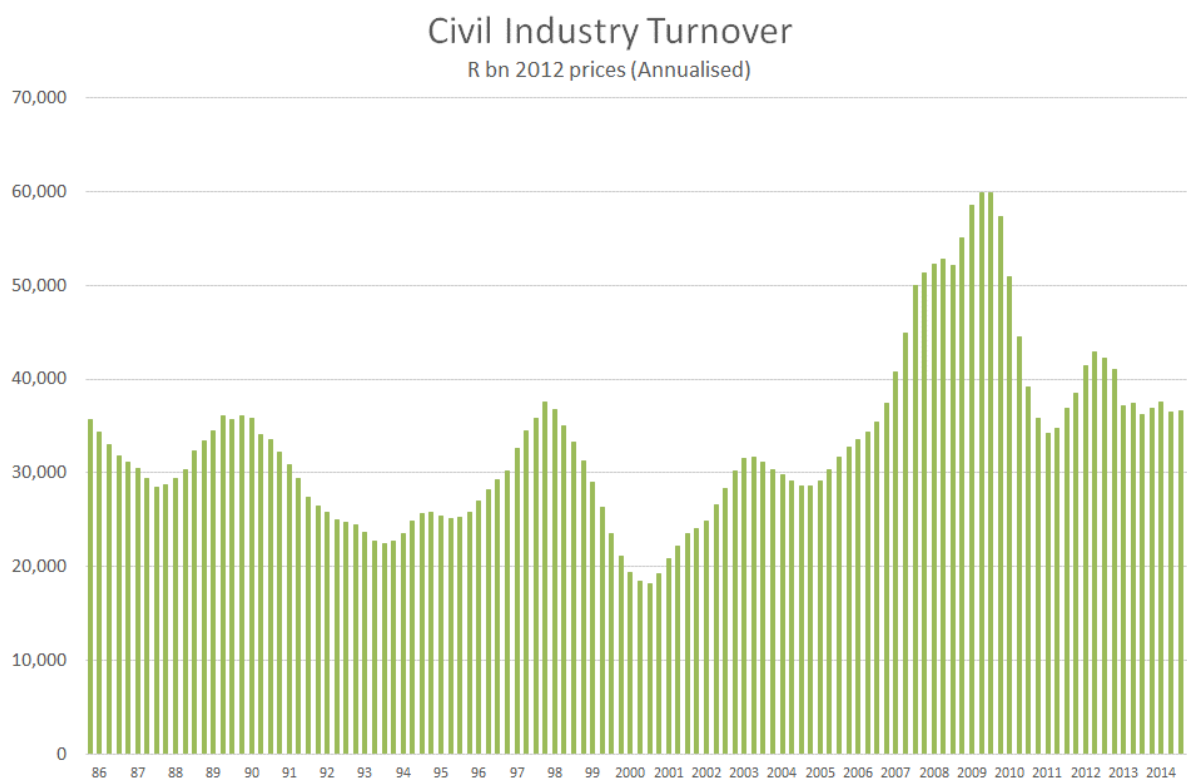


Figure 18: Civil Industry Turnover, 2012 prices

An increasing number of firms were of the opinion that turnover in the 2<sup>nd</sup> quarter was low (52 percent compared to an average of 33 percent over the previous two quarters).

Construction cost inflation accelerated to an average of 5,3 percent in 2014 compared to 5,7 percent in 2013, and is expected to moderate to an annual average increase of 4,1 percent in 2015, before accelerating to 7,3 in 2016. Price pressures are expected to ease somewhat in 2015 mainly due to the moderating effect of the lower oil price and lower consumer price inflation.

Table 15: Actual and Expected Turnover trends

	<i>Turnover Nominal</i>	<i>% Change (Nominal)</i>	<i>Turnover 2000=100</i>	<i>% Change (Real)</i>
1995	7 653 130 803		11,751,401,745	
1996	9 864 977 221	28.9%	13,548,444,351	15.3%
1997	13 282 356 448	34.6%	16,806,228,721	24.0%
1998	11 680 899 837	-12.1%	13,987,962,456	-16.8%
1999	8 600 472 761	-26.4%	9,455,575,722	-32.4%
2000	8 669 595 494	0.8%	8,639,968,534	-8.6%
2001	11 723 000 614	35.2%	10,762,140,678	24.6%
2002	17 138 501 083	46.2%	13,564,355,097	26.0%
2003	17 701 840 728	3.3%	13,621,980,350	0.4%
2004	17 180 281 073	-2.9%	12,844,628,262	-5.7%
2005	20 999 901 277	22.2%	14,682,985,873	14.3%
2006	25 783 535 490	22.8%	16,786,189,738	14.3%
2007	38 084 310 982	47.7%	23,146,856,716	37.9%
2008	58 063 639 993	52.5%	28,955,855,614	25.1%
2009	51 147 261 584	-11.9%	25,857,399,665	-10.7%
2010	32 744 103 366	-36.0%	16,140,361,470	-37.6%
2011	36,888,136,573	12.7%	17,366,815,461	7.6%
2012	40,952,061,358	11.0%	18,449,854,654	6.2%
2013*	38,920,982,014	-5.0%	16,505,163,586	-10.1%
2014*	39,941,145,748	2.6%	16,167,182,556	-2.5%
2015 *	41,538,791,578	4.0%	16,151,652,122	-0.1%
2016	41,331,097,620	-0.5%	14,977,533,887	-7.3%
2017	40,297,820,180	-2.5%	14,274,775,699	-4.7%

\*Provisional Figures

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

	Employment	Turnover (nominal)	Salaries and Wages (nominal)
2007	156 706	38 472 602 944	8 513 987 032
2008	196 596	58 063 639 993	12 849 483 530
2009	174 927	51 147 261 584	11 318 888 989
2010.1	121 395	9 287 099 665	2 055 235 156
2010.2	99 762	7 769 761 961	1 719 448 322
2010.3	97 237	7 687 241 740	1 701 186 597
2010.4	103 968	8 000 000 000	1 770 400 000
2010	105 591	32 744 103 366	7 246 270 075
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	105 522 *	9,237,998,741	2,044,369,121
2012	96502 *	40,952,061,358	9,062,691,178
2013.1	81651 *	7,944,678,917	1,758,157,444
2013.2	112823 *	11,122,550,484	2,461,420,422
2013.3	93894 *	9,454,167,911	2,092,207,359
2013.4	93894 *	10,399,584,702	2,301,428,095
2013	95565	38,920,9982,014	8,613,213,320
2014.1	96241	9,255,630,385	2,048,271,004
2014.02	96048	10,643,974,943	2,355,511,655
2014.03	103732	10,111,776,196	2,237,736,072
2014.04	106326	9,929,764,224	2,197,456,823



## Confidence Index

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 (solid line).

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 another weakening.

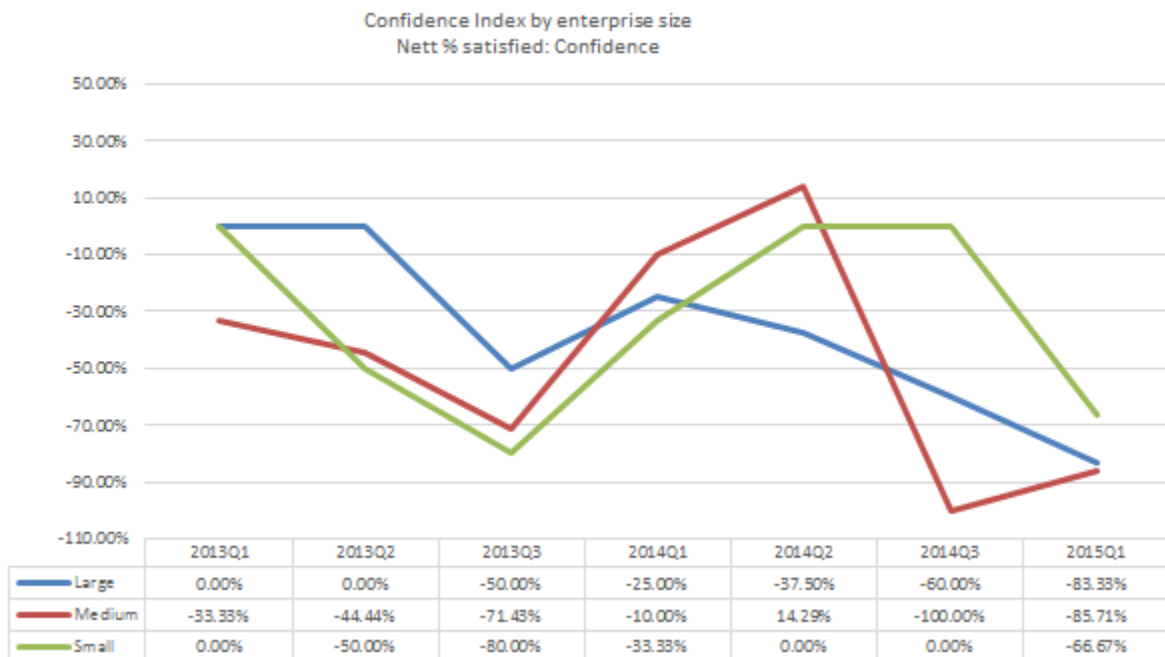


Figure 19: Confidence Index by firm size

Culminating all the other indicators already discussed, the nett satisfaction rate deteriorated to -70.0 in the 4<sup>th</sup> quarter of 2014, from -64.0 in the previous survey. The current trend surpasses even the negative sentiment expressed by contractors in the slowdown that followed in 2009. Smoothed over the last five quarters, the nett satisfaction rate deteriorated to -28 in the 1<sup>st</sup> quarter of 2015, from -18.0 and -16.0 in the previous two quarters.

The more negative sentiment was expressed by all firm sizes.

The poor state of affairs in terms of industry confidence is supported by the FNB/BER civil industry confidence index. Although the FNB/BER confidence index improved to a level of 59 in the last quarter of 2014, the index fell sharply in the 1<sup>st</sup> quarter 2015, supporting the results of this survey. 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.

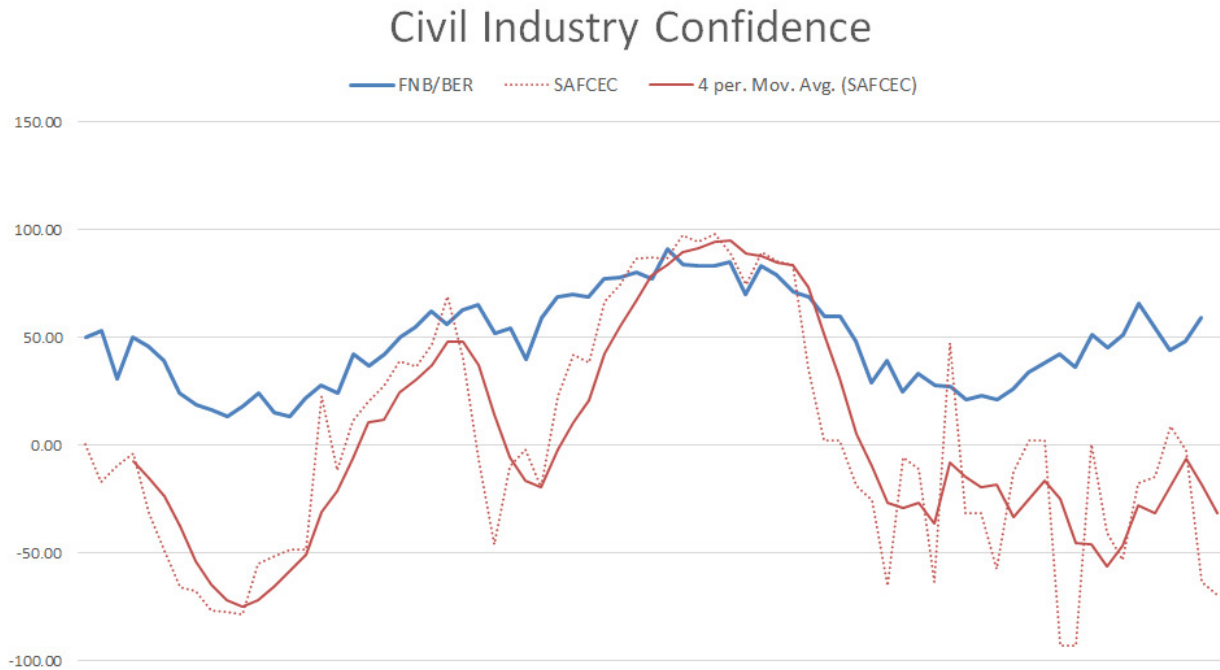


Figure 20: FNB/BER Confidence index vs SAFCEC Confidence Index

#### Key issues affecting current confidence levels in the industry:

- 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 was announced in the 2015/16 Budget, has resulted in negative growth projected over the medium term expenditure framework period (2015/16 to 2017/18)
- Delays in SANRAL's ability to roll out road contracts due to the ongoing e-toll dispute, will have a serious impact on the industry, considering the high contribution of the road segment to industry turnover.
- 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
- Another concern is where client bodies seem to be interfering with the role and responsibility of the designated engineer or principle agent.
- Low confidence in the mining sector is delaying capital expenditure
- Continued labour unrest affecting economic performance as well as critical project execution
- Payment is becoming a more serious concern as payment delays should (in theory) not exceed 30 days while there has also been an increase in the number of disputes reported. Payment delays may also be linked to certification disputes.
- The tendency by government to break what should be larger Grade 9 projects, into smaller grade projects

## PROSPECTS FOR 2015 and 2016

What can we expect in the next 12 to 24 months

- There is more muted outlook for public sector expenditure on infrastructure in the next three years, following a downward adjustment in growth estimates, announced in the 2015/16 Budget. Growth is projected to average 0,5 percent in nominal terms over the 3 year forecast period. Public Sector infrastructure as a percentage of GDP, targeted to reach 10% by 2030, is projected to fall back to 5,4 percent by 2017/18.
- Weak economic growth, and possible further downward revisions to GDP growth for this year, will further erode funds allocated for infrastructure expenditure, while likely strike action by the public sector in 2015 may result in higher than expected wage increases in the public sector wage bill. With very little reserves available to government, it may lead to further cut backs in capital (and infrastructure) spending.
- There are several risks to the economy most paramount the views expressed by credit rating agencies on South Africa's ability to manage its current account deficit and electricity crisis.
- South Africa is further faced by the conundrum that close to 40 percent of bonds are held by foreigners increasing our vulnerability to currency volatility and worsening the impact should SA face a further downgrade by credit rating agencies.
- The pending interest rate hike, expected to be announced by the US Federal Reserve in the next 6 to 12 months, will have a negative impact on the currency unless South Africa also raises interest rates. In an already ailing economy, with excessive unemployment, this will be detrimental. This raises the question whether or not interest rates are deemed as a monetary policy to control money supply and manage inflation or to protect the currency?
- SOE's infrastructure programmes are being delayed due to financial constraints as tariff increases are deemed as insufficient to finance pipeline projects. As the completion of Medupi and Kusile nears completion, there are no pipeline projects ready for roll out by Eskom to fill the void in the next three years. Implementation of renewable energy projects identified in the 3<sup>rd</sup> and 4<sup>th</sup> window, may be delayed as Eskom struggles to connect existing renewable projects to the grid.
- Private sector confidence remains elusive, not sufficient to stimulate renewed investment growth. This combined with policy uncertainty in the mining sector and labour tensions in the mining sector will continue to delay much needed infrastructure spending.

The start of 2015 posed many challenges, foremost the regular supply interruption of electricity as Eskom embarked on national load shedding, which was shortly thereafter accompanied by threats of strike action by not one, but seven labour unions. Nhlanhla Nene (Minister of Finance) may have expected a 2,2 percent increase in GDP in 2015, but electricity interruptions together with potential strike action by the Public sector, an increase in personal income tax (for the first time in 20 years), looming potential downgrade by credit rating agencies and the US Federal Reserve preparing to hike interest rates, are all deemed as aggravating conditions, that could have a serious negative impact on GDP growth this year.

### Developments that could shape the industry in 2015:

- Promulgation of the SEZ act by Minister of Trade and Industry hopefully in the first half of 2015, will add further incentive for the private sector to partake in infrastructure development earmarked by the Special Economic Zones, including the Saldanha Bay IDZ where construction has already started.
- The alignment process of the Construction Sector Charter with the revised Codes of Good Practice has already started and will come into effect in May 2015. The revised codes include fewer elements (five as opposed to seven), but with more stringent targets and the added penalty of discounting points where targets are not being complied with. Thus far no agreement has been reached between labour and business, which is why it is important that members understand the implication of adopting the generic codes. Government aims to develop a central supplier database as well as centralise procurement. If not properly implemented it could lead to large scale delays in the adjudication of tenders.
- Accessing tender information will be made more accessible through the development of the e-tender system.

## CIVIL ENGINEERING PRICE MOVEMENTS

Input cost price movements based on the Baxter contract price adjustment formula (CPAF) averaged 5,3 percent 2014, compared to 5,7 percent in 2013. Contribution to the lower input construction cost, was mainly the composite civil material price index, which slowed from an average increase of 4,3 percent in 2013 to 3,1 percent. Other indices, including fuel, plant and labour increased by a slightly higher rate in 2014, compared with 2013. Pending further developments in the oil price and currency vulnerability, we expect the composite index to moderate to an average of 4,1 percent in 2015 before accelerating to 7,3 percent in 2016. Our assumptions include a recovery in the oil price to an average of \$77/barrel in 2016 and further depreciation in the currency, averaging R13.3/US Dollar. These developments and the impact on input cost construction will be close monitored.

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

Table 17: CPAF Indices Annual Percentage Change

Year	Material (SAFCEC)	Fuel (SAFCEC)	Plant (SAFCEC)	Labour (CPI)	Composite
2013	4.3%	7.4%	6.3%	5.8%	5.7%
2014	3.1%	9.5%	7.6%	6.3%	5.3%
2015*	3.8%	-6.4%	7.0%	4.5%	4.1%
2016*	3.5%	21.0%	10.0%	5.7%	7.3%

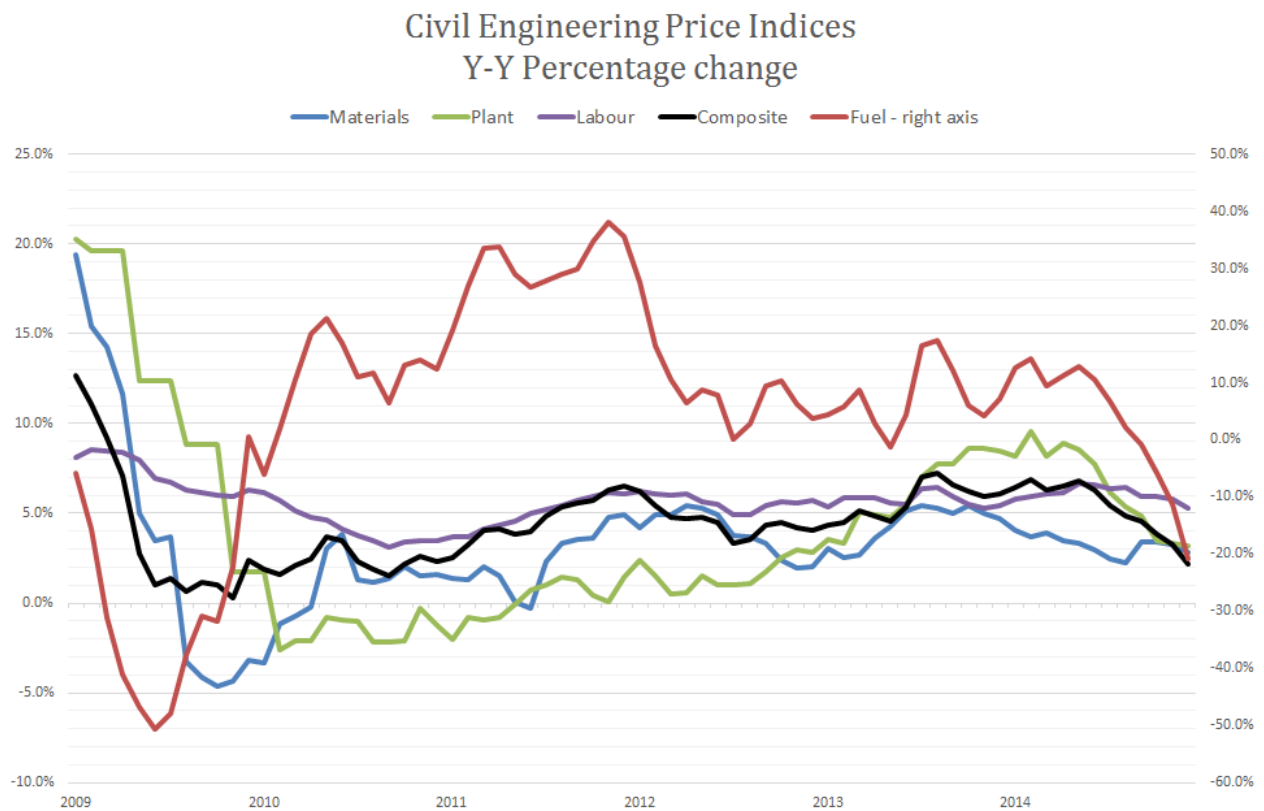


Figure 21: Civil Engineering price movements (source Stats SA)

Table 18: Macro Price Assumptions

	2012	2013	2014	2015	2016	2017
R/US\$ Exchange Rate	7.3	8.2	9.7	11.3	12.1	13.3
Oil price (\$ per barrel, UK Crude oil)	111.0	111.8	108.0	80.0	70.0	77.0
Oil Price (ZAR per barrel)	805.6	917.9	1042.2	904.0	846.4	1024.1
CPI (% change)	5.65%	5.75%	6.07%	4.5%	5.7%	5.3%

Table 19: CPAF Indices Forecast 2012-2017

<i>Index 2012= 100</i>	<i>2012</i>	<i>2013</i>	<i>2014</i>	<i>2015</i>	<i>2016</i>	<i>2017</i>
Plant	100.0	106.3	113.1	121.0	133.1	126.4
Fuel	100.0	107.2	110.6	103.5	125.2	130.9
Materials	100.0	104.3	107.7	111.8	115.7	119.9
Labour	197.2	208.5	221.2	231.1	244.3	257.2
Composite	129.1	136.4	143.6	149.5	160.5	164.2
<b>Y-Y Percentage Change</b>						
Plant	1.6%	6.3%	6.4%	7.0%	10.0%	-5.0%
Fuel	8.8%	7.2%	3.1%	-6.4%	21.0%	4.5%
Materials	3.9%	4.3%	3.3%	3.8%	3.5%	3.7%
Labour	5.7%	5.8%	6.1%	4.5%	5.7%	5.3%
Composite	4.5%	5.7%	5.3%	4.1%	7.3%	2.3%

Table 20: CPAF Indices (Quarterly Average)

Year	Quarter	CPAF Indices 2012=100					Y-Y Inflation				
		Materials	Labour	Fuel	Plant	Composite	Materials	Labour	Fuel	Plant	Composite
2011	1	95.2	182.2	84.1	97.4	120.8	1.6%	3.8%	26.7%	-1.3%	3.3%
	2	95.0	185.5	94.0	98.4	123.1	0.4%	4.6%	29.8%	-0.1%	4.0%
	3	96.7	188.4	91.1	99.1	124.4	3.1%	5.5%	28.9%	1.3%	5.2%
	4	98.0	190.4	98.5	98.4	125.9	4.4%	6.1%	36.2%	0.6%	6.2%
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	105.3	102.8	133.4	2.7%	5.7%	6.3%	4.0%	4.7%
	2	104.3	207.2	103.1	104.5	135.1	4.3%	5.7%	1.9%	5.1%	4.9%
	3	105.4	210.4	109.2	107.9	138.0	5.2%	6.2%	15.3%	7.5%	7.0%
	4	105.1	212.0	111.3	109.8	139.2	5.0%	5.4%	5.8%	8.6%	6.1%

2014	1	106.3	216.5	118.0	111.7	142.1	3.9%	5.9%	12.1%	8.7%	6.6%
	2	107.7	220.6	115.0	113.3	144.0	3.3%	6.5%	11.5%	8.4%	6.5%
	3	108.2	223.5	112.1	113.8	144.9	2.7%	6.2%	2.7%	5.5%	5.0%
	4	108.5	224.0	97.1	113.5	143.5	3.2%	5.7%	-12.7%	3.3%	3.1%
2015	1*	110.5	226.4	104.9	118.7	147.2	3.9%	4.6%	-11.1%	6.3%	3.5%
	2*	111.8	230.1	104.0	120.2	149.0	3.8%	4.3%	-9.6%	6.1%	3.5%
	3*	112.4	226.4	102.8	122.1	148.6	3.9%	1.3%	-8.3%	7.2%	2.5%
	4*	112.4	235.0	102.4	123.0	151.3	3.6%	4.9%	5.4%	8.4%	5.4%
*forecast											

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Annexure A

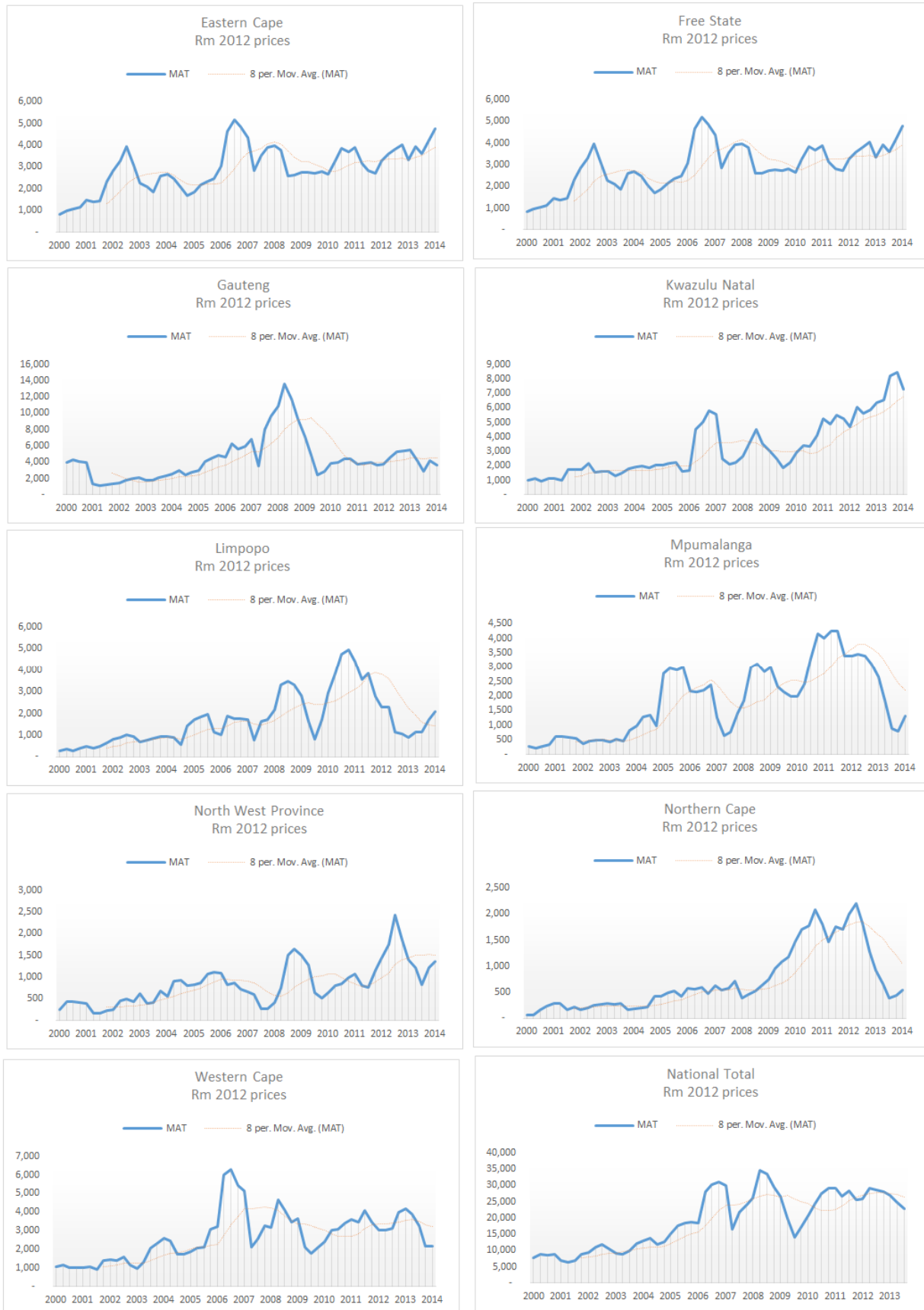


Figure 22: Provincial Trends