2016

# State of the South African Civil Engineering Contracting Industry

SAFCEC

1st Quarter 2016

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# ECONOMIC BACKGROUND

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

Global economic growth is currently estimated at 3.1 percent in 2015, projected at 3.4 percent for 2016 and 3.6 percent in 2017. The recovery in global growth is slower than expected in the October 2015 projections, mainly due to the slow pace of recovery experienced by emerging and developing economies, accounting for 70 percent of global growth. In advanced economies a modest recovery is expected to continue, while risks to the global outlook remain on the downside and related to ongoing adjustments in the global economy, a generalized slowdown in emerging market economies, re-balancing of the Chinese economy, lower commodity prices, and the gradual exit from extraordinary accommodative monetary conditions in the United States.

*Three key factors continue to influence the global outlook:*

*Gradual slowdown and rebalancing of Chinese economy*

*Lower prices for energy and other commodities*

*Gradual tightening of US monetary policy*

- Growth in advanced economies is projected at 2.1 percent in 2016, with similar growth rates expected in 2017.
- Growth in emerging markets and developing economies is projected to increase from 4.0 percent in 2105 to 4.3 percent in 2016, and 4.7 percent in 2017.
- Growth in China is expected to slow to 6.3 percent in 2016 and 6.0 percent in 2017, reflecting the impact of weaker investment growth.
- The IMF expects most countries in the sub-Saharan Africa will experience a gradual pickup in growth, but with lower commodity prices these growth rates will be lower than seen over the past decade. This follows through on the continued adjustment to lower commodity prices and higher borrowing costs, which is weighing heavily on countries such as Angola, Nigeria and South Africa.
- World commodity prices peaked in 2011, and have since declined largely due to the slowdown in the Chinese economy. Given the high levels of capacity it is unlikely that commodity price weakness will be revised. On the African continent, falling commodity prices, rising borrowing costs and declining revenues, is increasing fiscal stress.

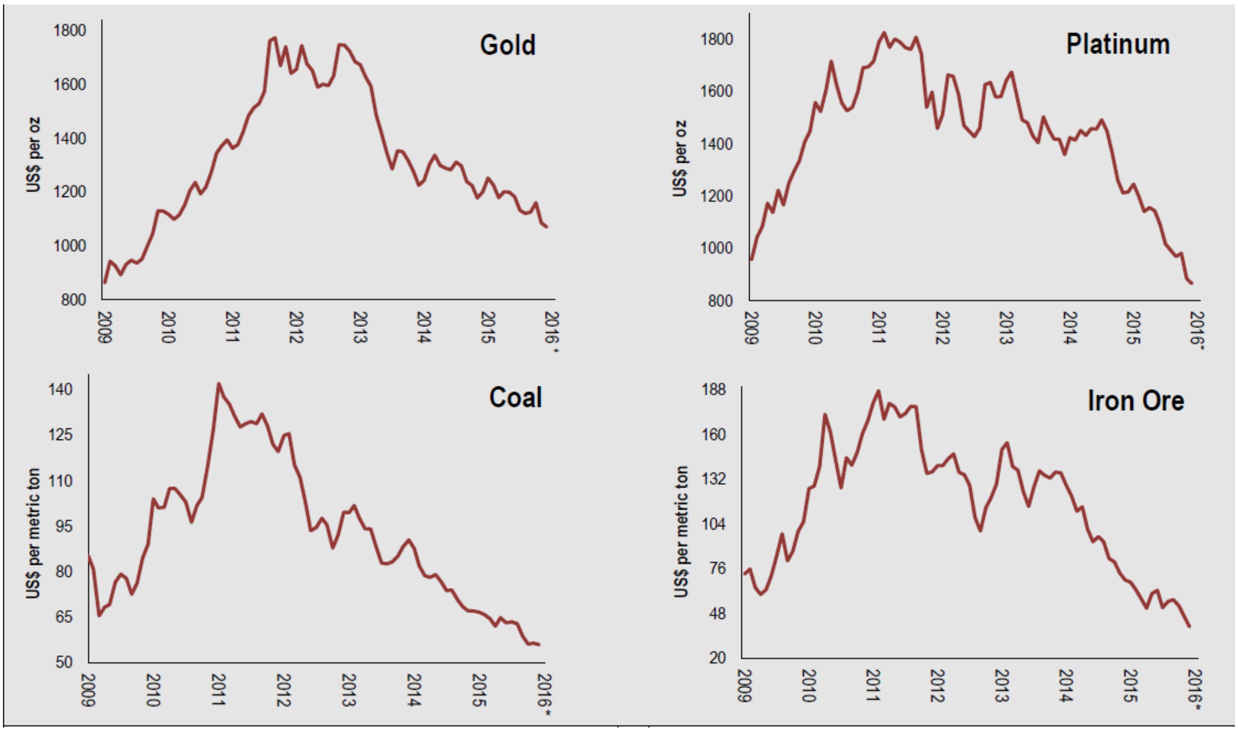



*Figure 1: Prices of SA's major commodity exports: 2009 – 2016 (Source Budget 2016 Review)*

The IMF's World economic outlook report lists the following key risks to the global growth outlook:

- A sharper-than-expected slowdown along China's needed transition to more balanced growth, with more international spillovers through trade, commodity prices, and confidence, with attendant effects on global financial markets and currency valuations.
- Adverse corporate balance sheet effects and funding challenges related to potential further dollar appreciation and tighter global financing conditions as the United States exits from extraordinarily accommodative monetary policy.
- A sudden rise in global risk aversion, regardless of the trigger, leading to sharp further depreciations and possible financial strains in vulnerable emerging market economies. Indeed, in an environment of higher risk aversion and market volatility, even idiosyncratic shocks in a relatively large emerging market or developing economy could generate broader contagion effects.
- An escalation of ongoing geopolitical tensions in a number of regions affecting confidence and disrupting global trade, financial, and tourism flows.

Domestic Economy

GDP growth slowed to 0.6 percent q-q, seasonally adjusted annualised in the 4$^{th}$ quarter of 2015, from 0.7 percent q-q in the previous quarter. South African economic growth thereby slowed from 1.5 percent y-y in 2014 to 1.3 percent in 2015. Growth was largely dragged down by a further contraction in the agriculture sector, down 14 percent q-q, while construction recorded marginal growth of 1.1 percent in the 4$^{th}$ quarter (from 0.5 percent in the previous quarter). According to the South African Reserve Bank's latest quarterly figures (4$^{th}$ quarter 2015), growth in gross fixed capital formation remained muted, at 1,6 percent y-y, on par with the 3$^{rd}$ quarter of 2015. On average for the year total investment in fixed investment increased by 1,4 percent in 2015 following the 1,1 percent contraction reported in 2014. Investment in buildings continued to contract, down 2,8 percent in 2015 from a decrease of 3,7 percent in 2014. Construction works still managed positive growth of 4,6 percent, albeit slowed from an increase of

8,4 percent in 2014. Construction works is largely supported by higher levels of investment by the private sector in renewable energy.

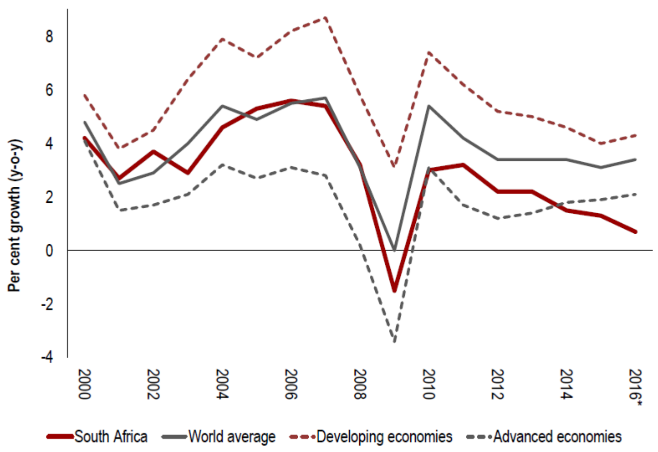



*Figure 2: SA and global economic growth: 2000 - 2016 (Source: Budget 2016 Review)*

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 word, 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.

Headline inflation averaged 4.5 percent in 2015, comfortably within the target range of 3 – 6 percent, and below 2014 level of 6.1 percent. However inflationary expectations have trended higher for the next two years, despite the weaker economy. Headline inflation is expected to average between 6.8 and 7.0 percent in 2016, with only a marginally lower inflation (at around 6.3 percent) expected for 2017. Inflation is currently fuelled by the nationwide draught, 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 have been diluted due to the increase in fuel levies imposed in April 2015 and again in April 2016, as well as currency weakness.

The exchange rate experienced several beatings during the last few months. Zuma's decision to fire respected Finance Minister Nhlanhla Nene and replace him with unknown David (Des) Van Rooyen, sent shockwaves through the economy as well as the financial markets, and although the re-appointment of Pravin Gordhan restored some confidence, the damage to investor sentiment was already done. The strong reaction to the rand, shortly after Gordhan delivered his somewhat disappointing budget speech (disappointing in that we expected plans to ensure more robust cut to government expenditure and more effective tax increases to support revenue growth), says the markets are not convinced that the South African government has done enough to prevent a junk status, depreciating the currency to close to R16.00/US$. The rand suffered another blow when it fell to R16.23/US$ following fears that the fallout between Gordhan and SARS would worsen, which could result in yet another Minister of Finance being sacked, or either resign. David Van Rooyen was subsequently appointed as Minister of COGTA, responsible for the expenditure of the Municipal Infrastructure Grant (MIG), projected to total R50bn over the next three years.

Probably the most critical concern, and most significant downside risk to inflation and economic growth, for the domestic economy is the fear of a further sovereign credit rating downgrade. So the question is what would a junk status mean to the South African economy and construction?

Moody's cut Brazil's rating to junk status on the same day South Africa's budget speech, 24 February 2016. Moody's put Brazil two notches into junk territory reducing its rating to Ba2 from Baa3 with a negative outlook highlighting the possibility of further downgrades. S&P stripped Brazil of their investment rating in September 2015, followed shortly with a second downgrade, and Fitch Ratings reduced Brazil to junk in mid-December.

This is likely the South African scenario that is awaiting us. A credit rating below investment grade, or so-called "junk status" eliminates the South African portfolio market for large international portfolio investors. This could lead to capital outflows, which will widen the current account deficit, one of the key indicators closely monitored by the credit rating agencies. Capital outflows will result in currency depreciation, which will increase import costs, amongst others oil. Even a stable oil price therefore , will still result in higher oil prices being paid in rand terms, and this in turn will lead to an increase production costs as well as consumer inflation. The current inflationary outlook is negative, expecting to surpass the 6 percent upper target this year, which means a rating downgrade could substantially increase the inflationary outlook, accelerating monetary policy tightening, further slowing and already dismal economic growth outlook. A lower credit rating also means the cost of borrowing for the South African government will escalate, which means more tax payers money will be used to finance debt, with less available to spend on critical economic and social infrastructure. Currently government expects that 3.6 percent of GDP per annum will be used on interest expenditure, estimated at around R260 bn per year, equal to total public sector infrastructure allocations per annum.

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.

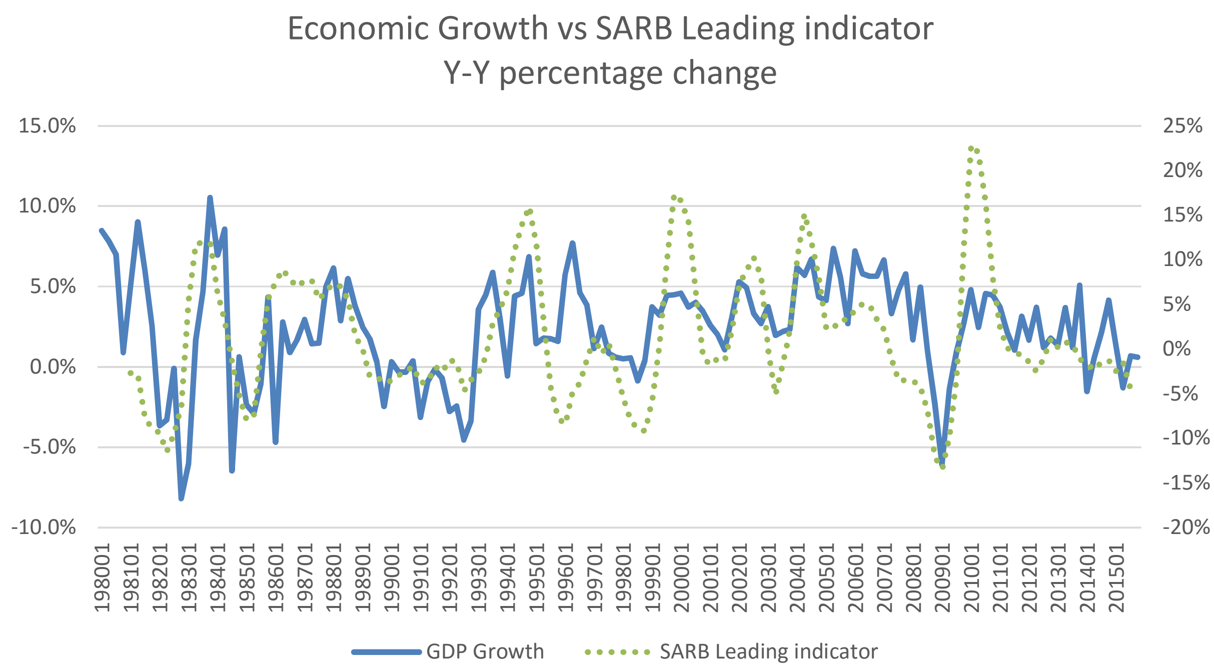



*Figure 3: Economic growth vs SARB Leading indicator*

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.

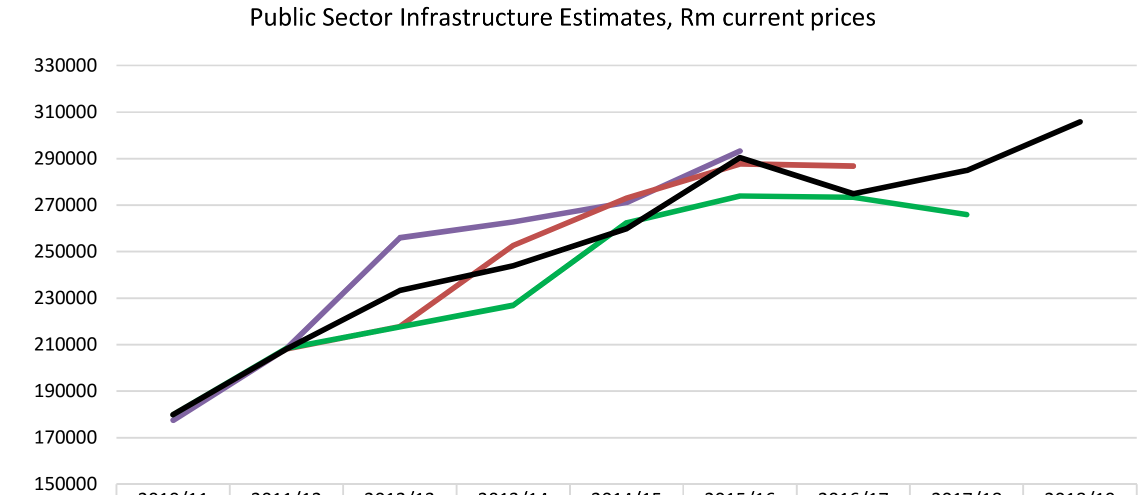
Table 1: Macroeconomic performance and projections (Source Industry Insight estimates)

| *Macro Economic Forecasts* | *2013* | *2014* | *2015* | *2016* | *2017* | *2018* |
|---|---|---|---|---|---|---|
| GDP | 2.2% | 1.5% | 1.4% | 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% | 3.4% | -0.5% | 0.2% | 2.1% |
| Imports | 1.8% | -0.5% | 6.4% | 2.5% | 3.8% | 5.0% |
| Exports | 4.6% | 2.6% | 3.0% | 3.5% | 4.0% | 4.7% |
| Prime Rate | 8.50% | 9.25% | 9.75% | 10.75% | 11.50% | 11.50% |
| Rand/Dollar | 9.70% | 10.80% | 12.10% | 16.80% | 15.60% | 15.00% |
| CPI Inflation | 5.80% | 6.20% | 3.80% | 6.20% | 6.00% | 5.80% |
| Current Account Deficit | -5.9% | -5.4% | -4.1% | -4.0% | -3.9% | -3.9% |

## Budget 2016

According to the 2016 Budget, estimates for public sector infrastructure investment were increased to R865 billion over the Medium Term Expenditure Framework (2016/17 – 2018/19), compared to estimates of R813 bn in the 2015 Budget. The increased allocations towards public infrastructure came as a surprise, given the demands on the fiscus for government to cut expenditure. Tax increases announced are not expected to be as effective as an increase in income tax would have been, which means revenue will remain under pressure. This in itself questions the ability of government to reduce the current account deficit to below 4 percent by 2018/19, and by implications questions the realism of the projected public sector infrastructure estimates.

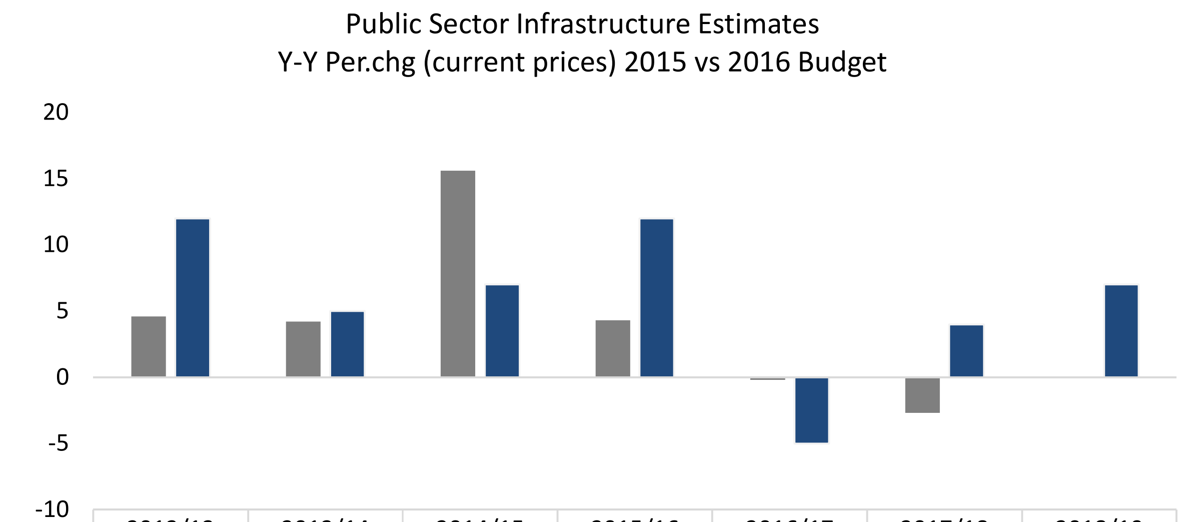
As seen in many budgets before the bulk of the increased infrastructure allocations are in 2018/19, as spending for 2016/17 is projected to fall by 5 percent compared to estimates for 2015/16. Expenditure in 2014/15 is reported to have increased by 7 percent, against an estimated increase of 15.6 percent in the 2015 Budget. Growth was therefore much weaker than expected, with a similar (downward) adjustment expected with regards to the 2015/16 estimates in next years (2017) budget.




| | 2010/11 | 2011/12 | 2012/13 | 2013/14 | 2014/15 | 2015/16 | 2016/17 | 2017/18 | 2018/19 |
|---|---|---|---|---|---|---|---|---|---|
| 2013 | 177500 | 208286 | 255905 | 262811 | 271080 | 293187 | | | |
| 2014 | 179900 | 208200 | 217800 | 252600 | 273000 | 287700 | 286700 | | |
| 2015 | 179,900 | 208,400 | 217,600 | 226,900 | 262,400 | 273,900 | 273,400 | 265,900 | |
| 2016 | 179900 | 208200 | 233300 | 243900 | 259900 | 290400 | 274800 | 284900 | 305800 |

2013 2014 2015 2016

*Figure 4: Public Sector Infrastructure Estimates (Budget 2016)*




| | 2012/13 | 2013/14 | 2014/15 | 2015/16 | 2016/17 | 2017/18 | 2018/19 |
|---|---|---|---|---|---|---|---|
| 2015 | 4.6 | 4.2 | 15.6 | 4.3 | -0.2 | -2.7 | |
| 2016 | 12 | 5 | 7 | 12 | -5 | 4 | 7 |

*Figure 5: Public Sector Infrastructure Estimates, Year on Year percentage change (nominal)*

*Table 2: Public Sector Infrastructure Estimates, Rm, current prices (Budget 2016)*

| Public Sector Infrastructure estimated: Y-Y Per. Change (nominal) | 2014/15 | 2015/16 | 2016/17 | 2017/18 | 2018/19 | MTEF Total |
|---|---|---|---|---|---|---|
| Economic services | **201200** | **221000** | **207300** | **212700** | **230300** | **650300** |
| Energy | 67800 | 69700 | 50800 | 49900 | 79900 | **180600** |
| Water and Sanitation | 29500 | 35200 | 43100 | 43100 | 45900 | **132100** |
| Transport and logistics | 90900 | 99500 | 96200 | 105300 | 90000 | **291500** |
| Other economic services | 13000 | 16600 | 17200 | 14400 | 14500 | **46100** |
| Social services | **53400** | **61500** | **60800** | **64500** | **67500** | **192800** |
| Health | 7800 | 9200 | 8800 | 9400 | 9800 | **28000** |
| Education | 15400 | 17400 | 17700 | 17800 | 18400 | **53900** |
| Human Settlements | 17100 | 18300 | 18300 | 21100 | 22300 | **61700** |
| Other social services | **13100** | **16600** | **16000** | **16200** | **17000** | **49200** |
| Admin Services | **5200** | **8000** | **6600** | **7600** | **7800** | **22000** |
| **Total** | **259800** | **290500** | **274700** | **284800** | **305600** | **865100** |

*Table 3: Public Infrastructure Estimates, Y-Y percentage change (current prices, not adjusted for inflation)*

| Public Sector Infrastructure estimated: Y-Y Per. Change (nominal) | 2014/15 | 2015/16 | 2016/17 | 2017/18 | 2018/19 | % of Total | Avg Growth (Nominal) |
|---|---|---|---|---|---|---|---|
| Economic services | 8.6% | 9.8% | -6.2% | 2.6% | 8.3% | 75% | 1.6% |
| Energy | -2.6% | 2.8% | -27.1% | -1.8% | 60.1% | 21% | 10.4% |
| Water and Sanitation | 14.3% | 19.3% | 22.4% | 0.0% | 6.5% | 15% | 9.6% |
| Transport and logistics | 19.0% | 9.5% | -3.3% | 9.5% | -14.5% | 34% | -2.8% |
| Other economic services | -3.7% | 27.7% | 3.6% | -16.3% | 0.7% | 5% | -4.0% |
| Social services | -0.4% | 15.2% | -1.1% | 6.1% | 4.7% | 22% | 3.2% |
| Health | -22.0% | 17.9% | -4.3% | 6.8% | 4.3% | 3% | 2.2% |
| Education | 12.4% | 13.0% | 1.7% | 0.6% | 3.4% | 6% | 1.9% |
| Human Settlements | 0.6% | 7.0% | 0.0% | 15.3% | 5.7% | 7% | 7.0% |
| Other social services | 1.6% | 26.7% | -3.6% | 1.3% | 4.9% | 6% | 0.9% |
| Admin Services | 4.0% | 53.8% | -17.5% | 15.2% | 2.6% | 3% | 0.1% |
| **Total** | **6.5%** | **11.8%** | **-5.4%** | **3.7%** | **7.3%** | **100%** | **1.8%** |

Growth in economic services, related to the development of economic infrastructure is projected to average 1.6 percent over the MTEF period, with a 10 percent increase reported in both the Energy and Water sectors. In terms of energy an additional R70bn was allocated in the final three year window period but no further detail was provided to what it would relate. Majority of the larger projects in pipeline related to Renewable energy projects, although R200million was allocated to the further investigations in the nuclear power programme in 2016/17. Robust growth is projected in water and sanitation for this financial year, up 22 percent, as government re-prioritises spending on critical water resources. Spending cuts were announced in both transport and other economic services.

For the first time the 2016 Budget included an overview of actual and projected spending / allocations from the fiscus to the 18 identified Strategic Infrastructure Projects (SIPS) as outlined in the National Development Plan. This shows significant less spending on SIP1 (development of mineral belt in Waterberg) while spending on SIP18 (Water and Sanitation master plan) is projected to more than double in 2016/17 compared to last year. Targets set out in the NDP include public sector infrastructure spending to reach 10 percent of GDP by 2030, however, in terms of these targets we have taken a few steps back, while targets related to gross fixed capital formation reaching 30 percent of GDP is also highly unlikely, currently hovering at 20 percent of GDP. The current shortfall to reach the 30 percent target is estimated at R300bn, while public sector spending on infrastructure need to increase by R100bn per annum to reach 10 percent of GDP. The NDP may outline critical reforms required to more effectively mobilise South Africa's poor economic growth rate and to create a more inclusive economy, but so far it has had a limited impact. Unfortunately reforms outlined in the NDP can not materialise without private sector participation. Unless government restores private sector and business confidence the current economic downturn, that could possible turn into a recession, will simply be prolonged eventually rendering the NDP as just another policy document.

The Budget included several initiatives to improve the capacity to deliver including improving planning and delivery of quality projects, whereby government is considering a new capital budget framework, improving asset management by giving priority to maintenance and rehabilitation projects to reduce the growing maintenance backlog, while the new Standard Procurement requirements, announced through the Standard for Infrastructure Procurement and delivery management (SIPDM) is hoped will improve value for money, accelerate delivery of projects, while reducing the scope for corruption.

**Table B.4 Allocations from the fiscus to strategic infrastructure projects**

| R million | 2012/13 | 2013/14 | 2014/15 | 2015/16 | 2016/17 | 2017/18 | 2018/19 |
|---|---|---|---|---|---|---|---|
| | Audited outcome | | Preliminary outcome | | Forecast | | |
| **SIP Category** | | | | | | | |
| SIP 1: Unlocking the northern mineral belt with Waterberg as catalyst | 1 051.9 | 1 042.8 | 1 053.7 | 604.1 | 371.4 | 397.8 | 478.9 |
| SIP 2: Durban-Free State-Gauteng logistics and industrial corridor | 13.0 | 11.6 | 4.9 | 109.5 | 50.7 | 8.7 | – |
| Sip 3: South eastern node and corridor development | 6 602.6 | 7 043.5 | 8 215.5 | 8 633.5 | 9 377.9 | 11 411.2 | 12 742.6 |
| SIP 4: Unlocking the economic opportunities in the North West province | 265.3 | 265.3 | 305.5 | 632.6 | 596.9 | 536.7 | 329.5 |
| SIP 5: Saldanha-Northern Cape development corridor | 228.7 | 44.5 | 177.2 | 269.4 | 136.0 | 55.3 | 35.5 |
| SIP 6: Integrated municipal infrastructure project | 16 959.3 | 17 117.0 | 18 042.4 | 20 043.0 | 19 915.1 | 20 459.5 | 21 109.5 |
| SIP 7: Integrated urban space and public transport programme | 36 520.1 | 38 873.0 | 49 751.5 | 49 398.3 | 49 749.1 | 55 199.1 | 58 562.3 |
| SIP 10: Electricity transmission and distribution for all | 1 937.7 | 2 251.3 | 3 018.0 | 3 779.8 | 3 692.8 | 4 066.0 | 4 196.7 |
| SIP 11: Agri-logistics and rural infrastructure | 6 845.1 | 7 544.8 | 9 401.5 | 9 861.2 | 10 267.5 | 10 847.9 | 11 797.1 |
| SIP 12: Revitalisation of public hospitals and other health facilities | 6 190.6 | 5 473.5 | 5 794.3 | 6 278.5 | 6 065.8 | 6 718.9 | 7 024.8 |
| SIP 13: National school build programme | 6 860.7 | 8 319.6 | 10 070.6 | 11 695.7 | 12 218.3 | 13 165.6 | 13 919.0 |
| SIP 14: Higher education infrastructure | 1 799.9 | 2 150.0 | 2 700.0 | 3 301.2 | 3 396.7 | 3 537.6 | 3 708.0 |
| SIP 15: Expanding e-access to communication technology | – | 808.2 | – | 226.7 | 450.3 | 563.6 | 890.5 |
| SIP 16: SKA and Meerkat | 218.7 | 328.1 | 645.2 | 687.4 | 652.8 | 711.9 | 729.0 |
| SIP 18. Water and sanitation master plan | 905.4 | 1 062.9 | 855.9 | 1 629.9 | 2 053.2 | 2 076.8 | 2 722.5 |
| **Total** | **86 399.1** | **92 336.0** | **110 036.4** | **117 150.9** | **118 994.4** | **129 756.6** | **138 245.9** |

*Source: National Treasury*

# THE POSITION OF THE CIVIL ENGINEERING INDUSTRY

## Background

- Questionnaires were distributed to all SAFCEC members during February 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 fell by 17 percent in the 4th quarter of 2015, due to a drop in participation by smaller companies. The contribution by larger firms was maintained while there was a notable increase in the participation by medium size companies. Larger firms contributed 42 percent to the 1st quarter survey (from 35 percent in the previous survey), medium size firms 32 percent and smaller firms 26 percent, compared to 52 percent in the previous survey.

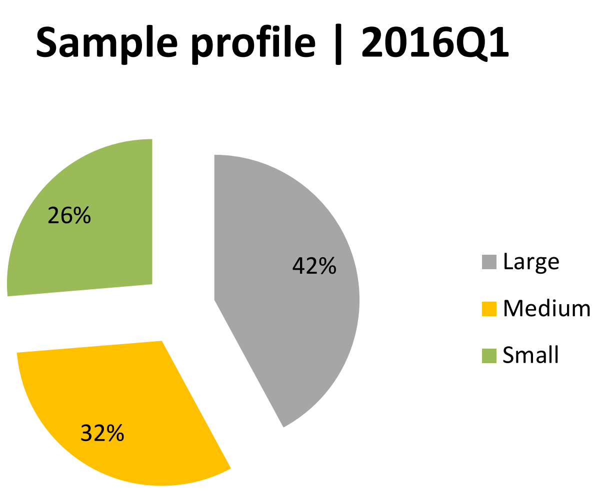



*Figure 6: Profile of respondents*

# Key observations

## Human Resources

- Employment fell by 5.9 percent q-q in the 1st quarter of 2016, following a 8,3 percent q-q contraction in the previous quarter as larger contractors reported a decline of 7.5 percent q-q, and medium size firms (again) reported an increase in employment of 12 percent q-q (largely due to an increase in the use of limited duration employees).
- Limited Duration contributed 47.6 percent of total employment, compared to 45 percent in the 4th quarter. In large firms limited duration contributed 46.3 percent, slightly higher compared to the last survey, but the most notable shift was reported by medium size firms were limited duration contribution increased to 60 percent from 35,6 percent.

| *Firm Size Category* | *Limited Duration* | *Permanent Employees* | *Total* | *% Limited Duration of total workforce* |
|---|---|---|---|---|
| *Large* | -2% | -12% | -7.52% | 46.3% |
| *Medium* | 18% | 5% | 12.13% | 60.1% |
| *Small* | 0% | 0% | 0.00% | 43.3% |
| *Total* | 0% | -11% | -5.87% | 47.6% |

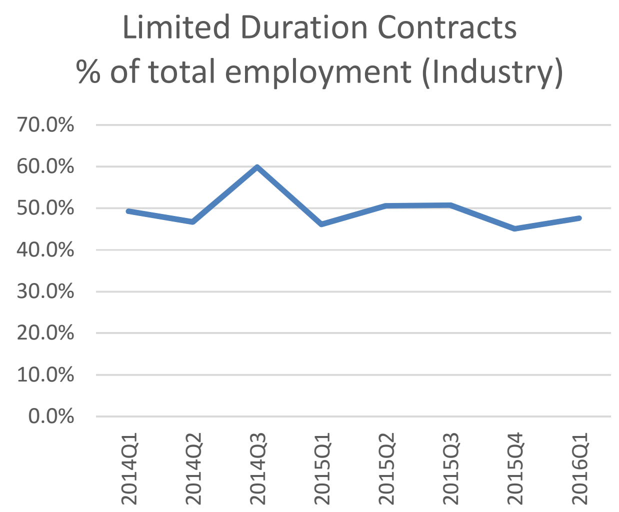



*Figure 8: Limited Duration Contracts, % of total employment*

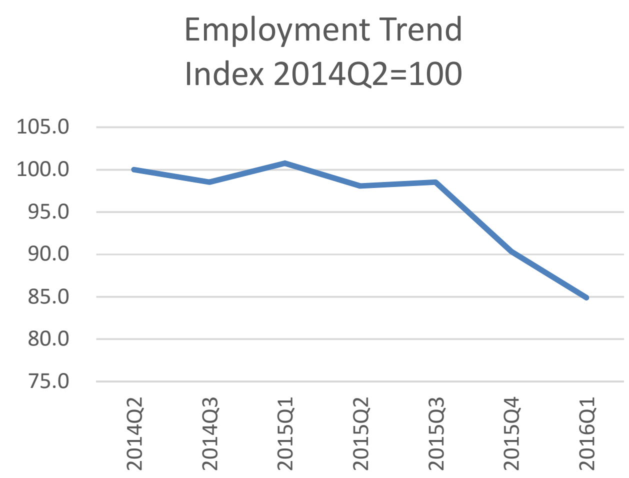



*Figure 7: Employment trend Index 2014Q2*

- Labour brokers represented 3 percent of the total workforce, well below the trend in the last few years, and well below the 7 percent reported in the 4th quarter. 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 fell by 17 percent, following an increase of 8 percent reported in the 4th quarter.

# Financial Statistics

## Turnover, Wages and Order Books

- The total value of Civil engineering construction certified for payment fell 11.5 percent q-q in the 4th quarter of 2015 compared to the 3rd quarter, following a marginal increase of 0.5 percent q-q reported in the previous quarter (Q3) and a 16 percent increase in the quarter before that.
- Larger firms reported a 12.5 percent decrease, from an increase of 1,7 percent in the previous survey, medium size firms reported no change in turnover (from 6,8 percent increase) while smaller firms reported a significant increase of 32 percent (based on a relatively small sample though).

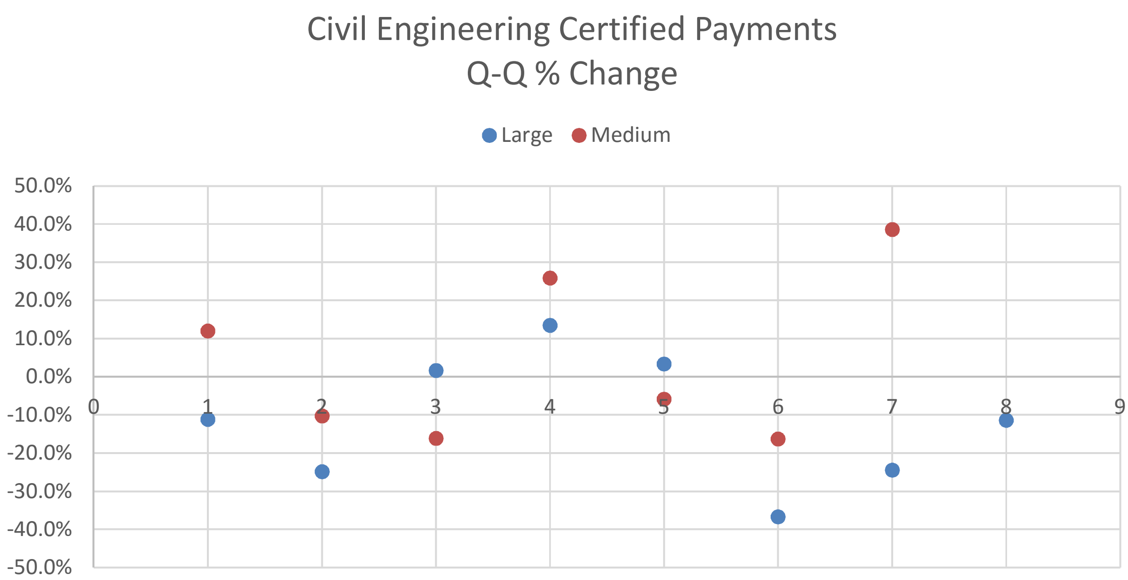



*Figure 9: Civil Engineering certified payments, q-q percentage change, matrix*

- The cumulative salary and wage bill represented 23 percent of total turnover, from 21 percent in the previous quarter, but with some dubious results reported by the smaller firms. However, due to its size it has no real impact on the overall trend.
- In line with a contraction in employment, the total salary and wage bill fell by 4.1 percent (from a decline of 8,3 percent), although medium size firms reported an increase of 30 percent q-q in their cumulative wage bill, in line with the increase in reported turnover.

- The value of the two-year forward order book fell by 14 percent q-q, following a 6,8 percent increase reported in the previous survey, as both large and medium size contractors reported a decline in order book values since the last survey.

o The order book for activities outside of RSA, continued to weaken and fell by 27 percent q-q (from a 10 percent decline in the previous survey).

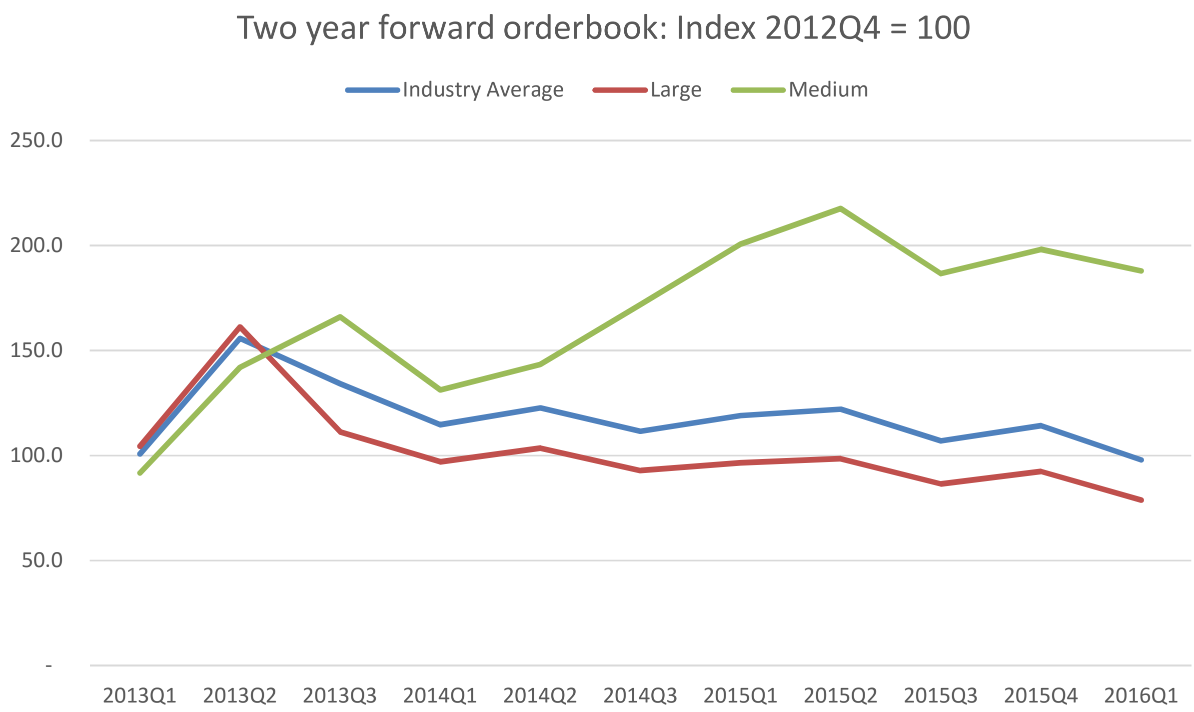



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*Figure 10: Value of two year forward order book, Index 2012Q4=100*

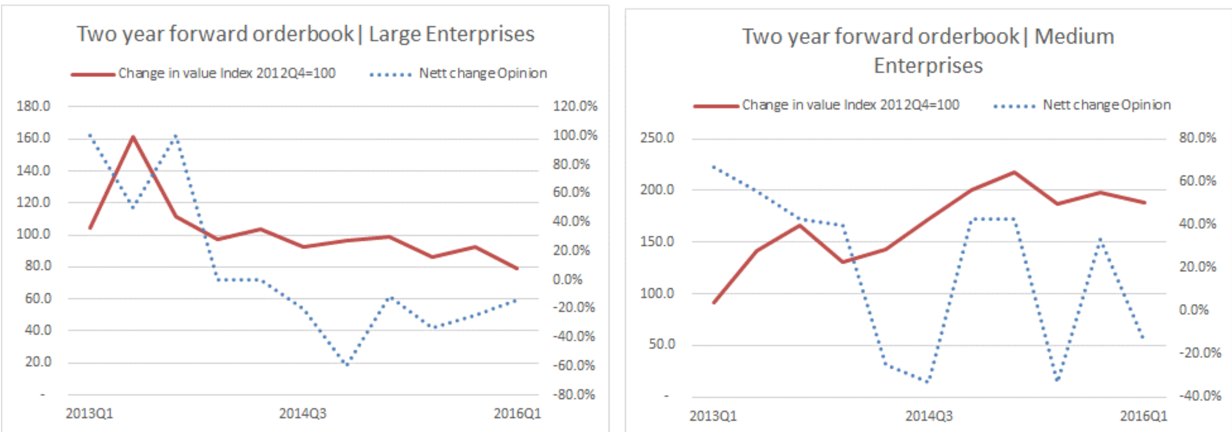



*Figure 11: Two year forward order book, Large vs Medium Enterprises*

## Late Payments

- Contractors continue to report on improved conditions related to late payments. In this survey, the total value of late payments were 23 percent q-q lower, following the 79 percent and 27 percent declines reported in the previous two quarters. Smaller firms reported a marginal increase of 4 percent, while both medium and large contractors reported an improvement in payment.
- The value of late payment as a percentage of turnover decelerated to 15 percent, from 17 percent in the previous reported period. Large firms improved from 17 percent to 15 percent, and medium size firms from 18 percent to 11 percent. 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 the provincial departments at 33 percent, SOE's at 7.3 percent and local government at 2.5 percent.

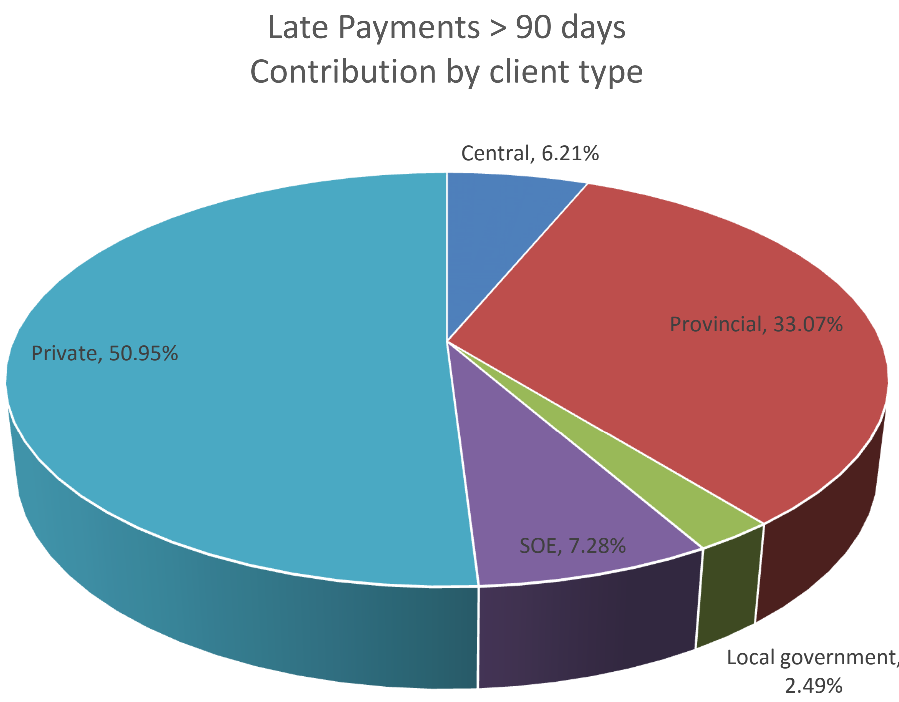



*Figure 12: Late payments > 90 days, contribution by client*

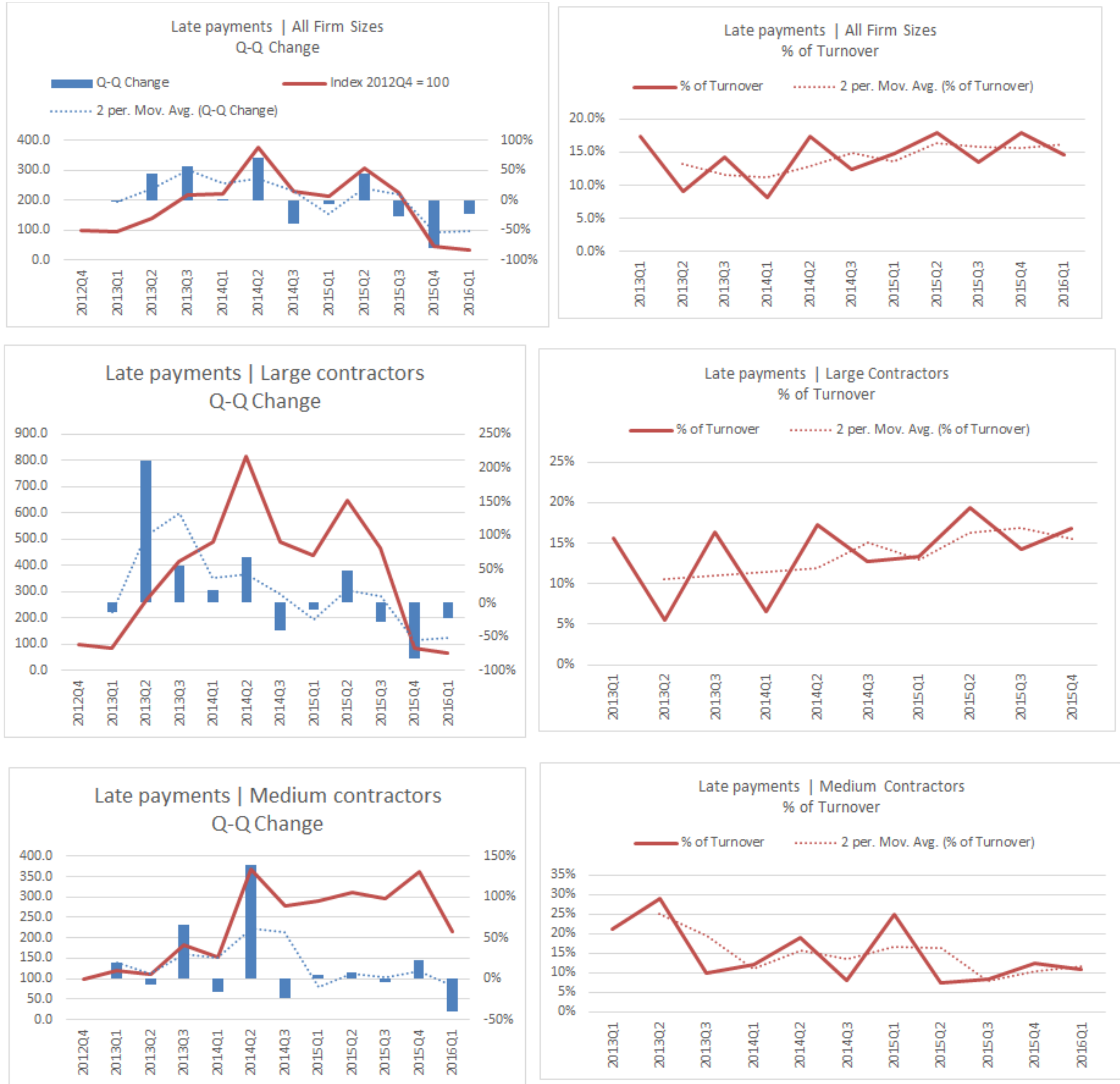
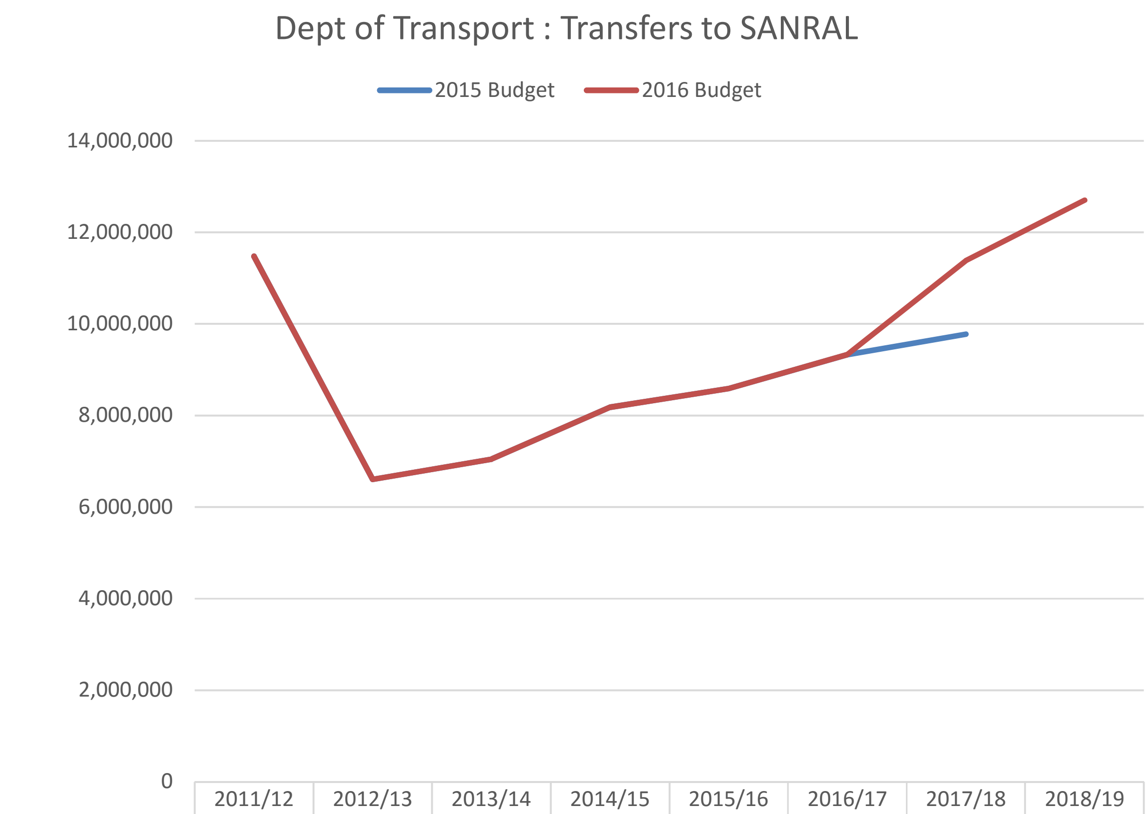



*Figure 13: Late payments*

# Industry Profile

- The following section provides a snapshot view of responding firms' turnover earned by project type, client and province during the 4th quarter 2015 (surveyed in the 1st 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 55.3 percent to total turnover, with medium size firms highly exposed to road contracts earning 76.6 percent of turnover from this market segment. Larger firms are able to diversify with power bulk infrastructure contributing 16 percent to turnover, although road remain the priority market segment, contributing 53 percent.
- 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 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.




| | 2011/12 | 2012/13 | 2013/14 | 2014/15 | 2015/16 | 2016/17 | 2017/18 | 2018/19 |
|---|---|---|---|---|---|---|---|---|
| 2015 Budget | 11,477,300 | 6,602,600 | 7,043,500 | 8,180,800 | 8,590,900 | 9,329,400 | 9,777,600 | |
| 2016 Budget | 11,477,300 | 6,602,600 | 7,043,500 | 8,180,800 | 8,590,900 | 9,329,400 | 11,384,500 | 12,704,600 |

*Figure 14: Department of Transport: Transfers to SANRAL*

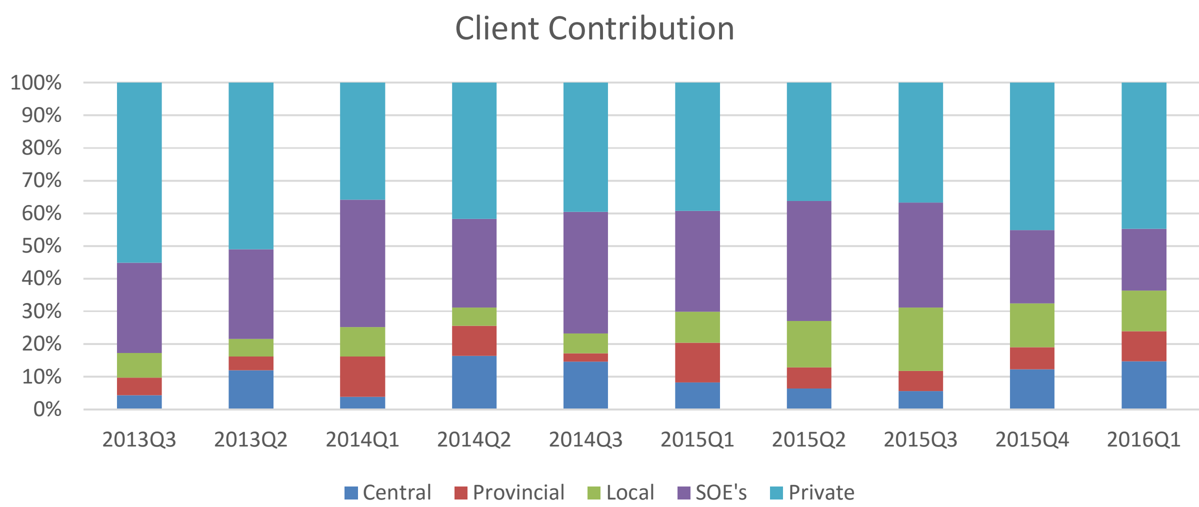
Table 4: Turnover distribution by sub-discipline

| Discipline | Large | Medium | Small | Total 2015Q1 | Total 2015Q2 | Total 2015Q3 | Total 2015Q4 |
|---|---|---|---|---|---|---|---|
| *Roads* | 53.5% | 76.6% | 0.0% | 32.3% | 42.5% | 45.7% | 55.3% |
| *Earthworks* | 3.5% | 2.5% | 0.0% | 5.7% | 5.6% | 4.2% | 3.5% |
| *Water Bulk Infrastructure* | 2.1% | 6.2% | 85.7% | 8.3% | 9.6% | 15.0% | 2.6% |
| *Water and Sanitation* | 2.9% | 12.2% | 0.0% | 5.9% | 6.7% | 3.9% | 3.6% |
| *Rail* | 1.8% | 0.0% | 0.0% | 1.6% | 3.4% | 2.1% | 1.7% |
| *Harbours* | 2.2% | 0.0% | 0.0% | 3.3% | 1.4% | 1.1% | 2.0% |
| *Power (bulk)* | 16.3% | 0.0% | 0.0% | 19.7% | 12.3% | 11.7% | 15.0% |
| *Power (services)* | 2.5% | 0.0% | 0.0% | 0.0% | 0.0% | 1.7% | 2.3% |
| *Airports* | 0.2% | 0.4% | 0.0% | 0.0% | 0.0% | 0.3% | 0.2% |
| *Mining Infrastructure* | 4.9% | 0.0% | 14.3% | 12.3% | 5.6% | 5.2% | 4.6% |
| *Mining (Surface earthworks)* | 1.8% | 0.0% | 0.0% | 0.0% | 0.0% | 0.6% | 1.6% |
| *Other* | 8.3% | 2.1% | 0.0% | 10.9% | 13.0% | 8.6% | 7.8% |
| *Total* | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

Table 5: Turnover distribution by client

| | Large | Medium | Small | Total 2015Q1 | Total 2015Q2 | Total 2015Q3 | Total 2015Q4 |
|---|---|---|---|---|---|---|---|
| *Central* | 15.9% | 0.0% | 0.0% | 6.1% | 2.2% | 12.3% | 14.7% |
| *Provincial* | 5.8% | 50.1% | 0.0% | 4.0% | 6.6% | 6.8% | 9.3% |
| *District/Local/Metropolitan Councils* | 10.2% | 35.1% | 85.7% | 14.1% | 25.2% | 13.4% | 12.3% |
| *Parastatals* | 20.0% | 8.8% | 0.0% | 41.1% | 35.7% | 22.4% | 19.0% |
| *Private* | 48.0% | 6.0% | 14.3% | 34.6% | 30.3% | 45.2% | 44.7% |
| *Total* | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% | 100.0% |

*Data for the third quarter not available*




- The contribution by the private sector in this survey increased to 44.7 percent, because of the higher exposure by the larger firms to private sector infrastructure. Medium size firms in this survey were more exposed to provincial government (compared to previous surveys where local government represented the largest share of turnover), while smaller firms earned a higher portion of turnover from local government.
- 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.

Table 6: Geographic Distribution of the value of civil engineering construction work (turnover)

| Province | Large | Medium | Small | 2015Q1 | 2015Q2 | 2015Q3 | 2015Q4 |
|---|---|---|---|---|---|---|---|
| *GAU* | 15% | 22% | 0% | 22% | 33% | 23% | 16% |
| *WC* | 15% | 18% | 0% | 6% | 15% | 12% | 15% |
| *EC* | 9% | 3% | 86% | 9% | 10% | 8% | 9% |
| *NC* | 5% | 1% | 0% | 7% | 2% | 4% | 5% |
| *MPU* | 18% | 15% | 0% | 22% | 11% | 18% | 18% |
| *FS* | 6% | 7% | 0% | 6% | 6% | 11% | 6% |
| *LIM* | 7% | 5% | 0% | 12% | 12% | 8% | 7% |
| *NW* | 2% | 10% | 14% | 3% | 1% | 5% | 2% |
| *KZN* | 24% | 19% | 0% | 12% | 9% | 12% | 23% |
| *Total* | 100% | 100% | 100% | 100% | 100% | 100% | 100% |

- Gauteng contributed 16 percent to this survey, followed by 18 percent in Mpumalanga, 15 percent in Western Cape and 23 percent in Kwazulu Natal. Medium size firms reported a fairly diverse geographical profile of turnover, but were more active by comparison to larger firms in Gauteng, and Western Cape.

## Economic Indicators

*Economic indicators generally depict the "opinions" of respondents related to work conditions, tempo of work activity, and competition for tenders, profitability and prices. It measures contractors' sentiment during the survey period (4th quarter 2015).*

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 4th quarter of 2015 (past quarter), remained in deep negative territory -52.9, although this was an improvement from -60,8 reported in the 4th quarter survey. 35 percent of respondents reported very quiet conditions, with a similar view on the current quarter (1st quarter of 2016).
- The nett % satisfied with working conditions in the current quarter improved to -29.9 from -48.1 and -79.9 in the previous two surveys, with close to 30 percent saying conditions were quiet. Only 11 percent reported quite busy conditions.
- Expectations for the current quarter is more mixed, as fewer contractors expect very quiet conditions (17 percent) and an increasing number of contractors expecting satisfactory conditions to prevail. Around 6 percent expect busy conditions (down from 11 percent as reported in this survey for the current (2016Q1) quarter.
- **Competition for tenders** remain fierce, although there was some improvement from the previous survey. 64.7 percent of contractors said that there were more than 11 bids per contract, from 70 percent in the previous survey. However this is still higher compared to a year ago when on average 55 percent reported more than 11 bids per contract.
- **Tender prices** remain under pressure, although fewer contractors (41 percent, compared to 48 percent in the previous survey) reported very low prices.
- Larger firms have seemingly become more comfortable with the (lower) levels of profitability, as close to 60 percent reported satisfactory levels, a sentiment not shared by medium or smaller contractors. Majority of

medium size firms (43 percent) reported low profitability while 66 percent of smaller firms also felt profitability levels were low.

- Majority of contractors (supported mainly by medium size contractors) expect profitability trends to recede (58 percent), while less than 6 percent expect improved margins. Larger firms are however more optimistic, as fewer expect a further deterioration in profitability, while majority expect margins to stabilise. Encouraging is that 14 percent of larger firms now expect an improvement in profitability, a welcome development since the 1st quarter of 2015 when 60 percent of the larger firms expected further deterioration in profitability. According to financial statements available, majority of contractors have managed to stabilise, if not improve, profit margins, even though these may not be necessarily related to increased volume of work, but rather due to diversification, restructuring, internal optimisation and selling off of non-core assets.

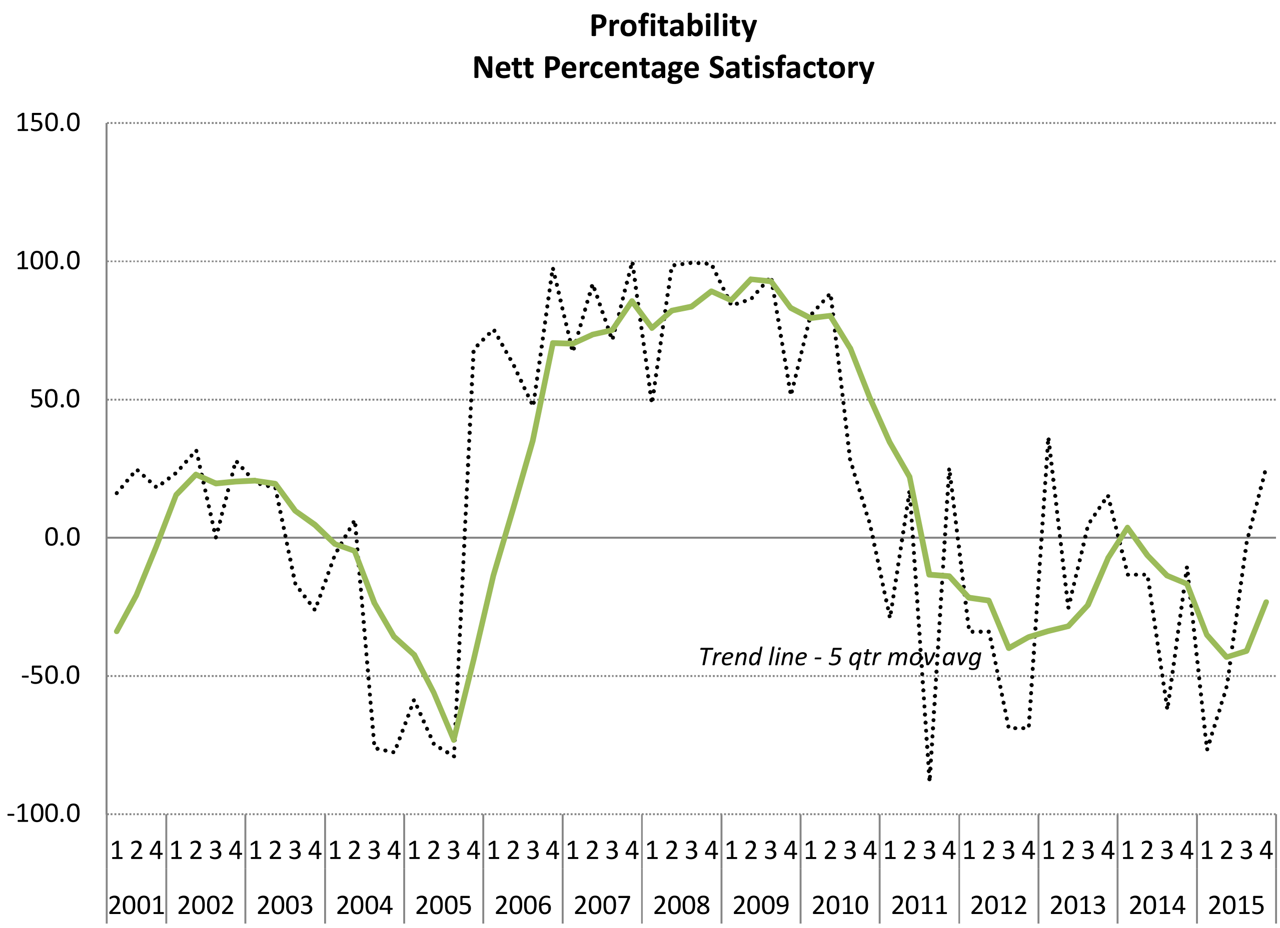
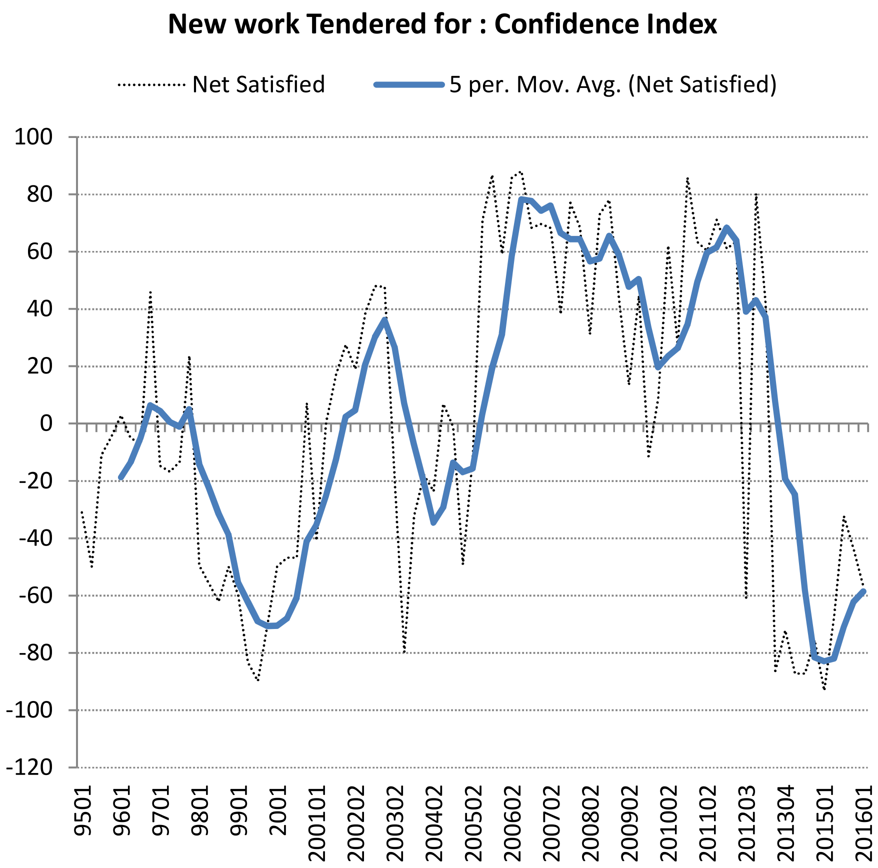



Figure 15: Opinions related to Profitability

## 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 16: Opinions of new work tendered for*

- The negative sentiment towards tenders continued in this survey, as the nett satisfaction rate fell to -57.0 from -43.7 in the previous survey. This is mainly as a result of 78 percent contractors reporting on low tender volume conditions (compared to 71 percent in the previous survey) while 8 percent felt that tender activity was satisfactory (compared to 27 percent in the previous survey).
- The estimated value of tenders published during the three last quarters of 2015 was lower compared to last year, down by 12,9 percent, 9,6 percent and 11,2 percent respectively. Nominal values dropped by 5,6 percent y-y, following the increase of 20 percent y-y in 2014. In the 4th quarter of 2015 however there was a shift in favour of water projects, with an increase of 60 percent from the 3rd quarter (which translated to a 2 percent y-y increase), while the value of road projects out to tender fell by 41 percent since the 3rd quarter, down 32 percent compared to the same quarter in 2014. 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.

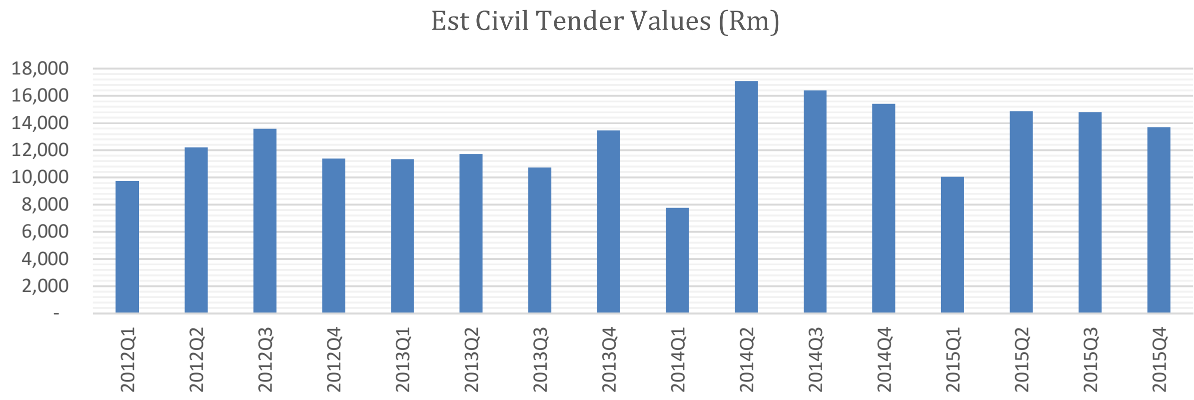



*Figure 17: Estimated Tender Values (RM)*

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) |
|---|---|---|---|---|---|---|---|---|---|
| *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% |
| *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% |

## Awards

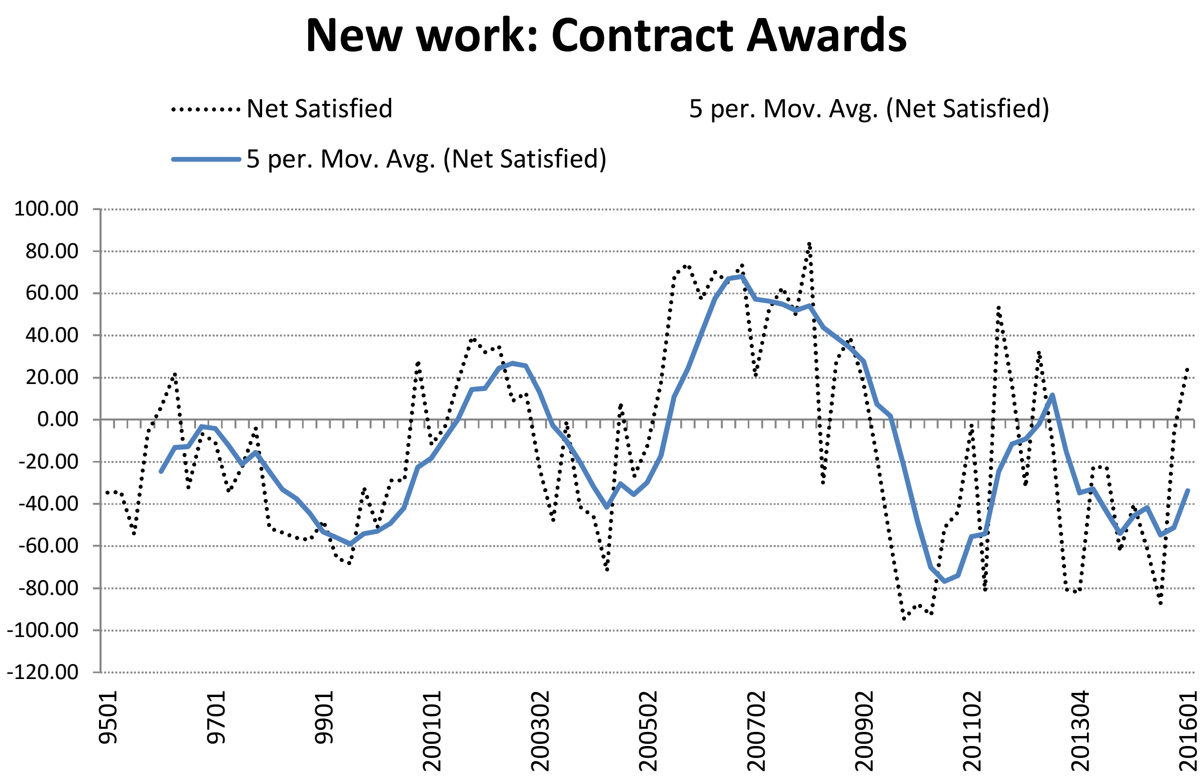



*Figure 18: Opinions related to Awards*

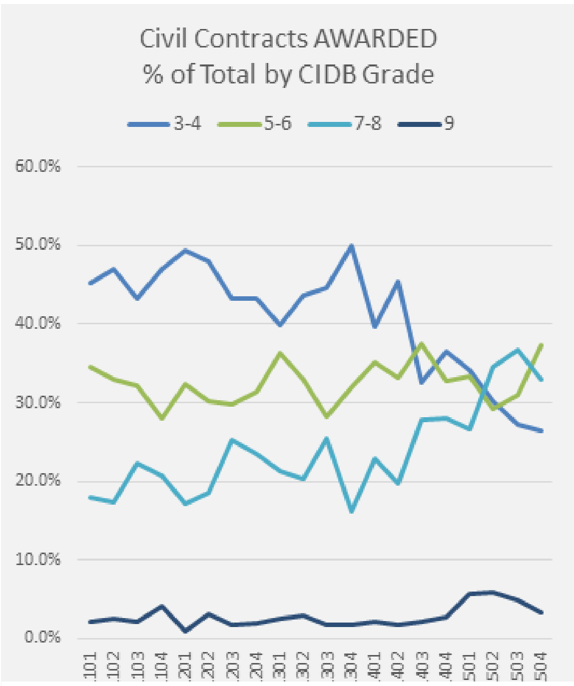



*Figure 19: Civil contracts awarded by CIDB grade*

- On the upside, contractors were more optimistic regarding the awarding of contracts. 47 percent reported that conditions were satisfactory, the best level since 2012, while around 35 percent said conditions were still low (compared to 50 percent in the previous survey). As a result the nett satisfaction rate improved from -5.0 to a positive 24.9.

- The nominal value of civil contracts awarded increased by 10 percent y-y in 2015, compared to 2014. This more optimistic growth rate must be seen in context with the depressed conditions experienced in 2014, and is therefore coming off a lower base.

- There has been a notable increase in the number of civil projects awarded to CIDB grade 7-8 contractors, increasing their contribution to total awards from around 16 percent in 2012 to 33 percent by 2015. Fewer Grade 3-4 contracts were awarded, while the contribution by grade 5-6 remained relatively stable at around 33 percent, although it did show a stronger increase to 37 percent in the last quarter. The contribution by grade 9 projects improved to 6 percent of total awards in the 1st quarter of 2015, before slowing to just over 3 percent towards the end of the year.

## Orderbooks

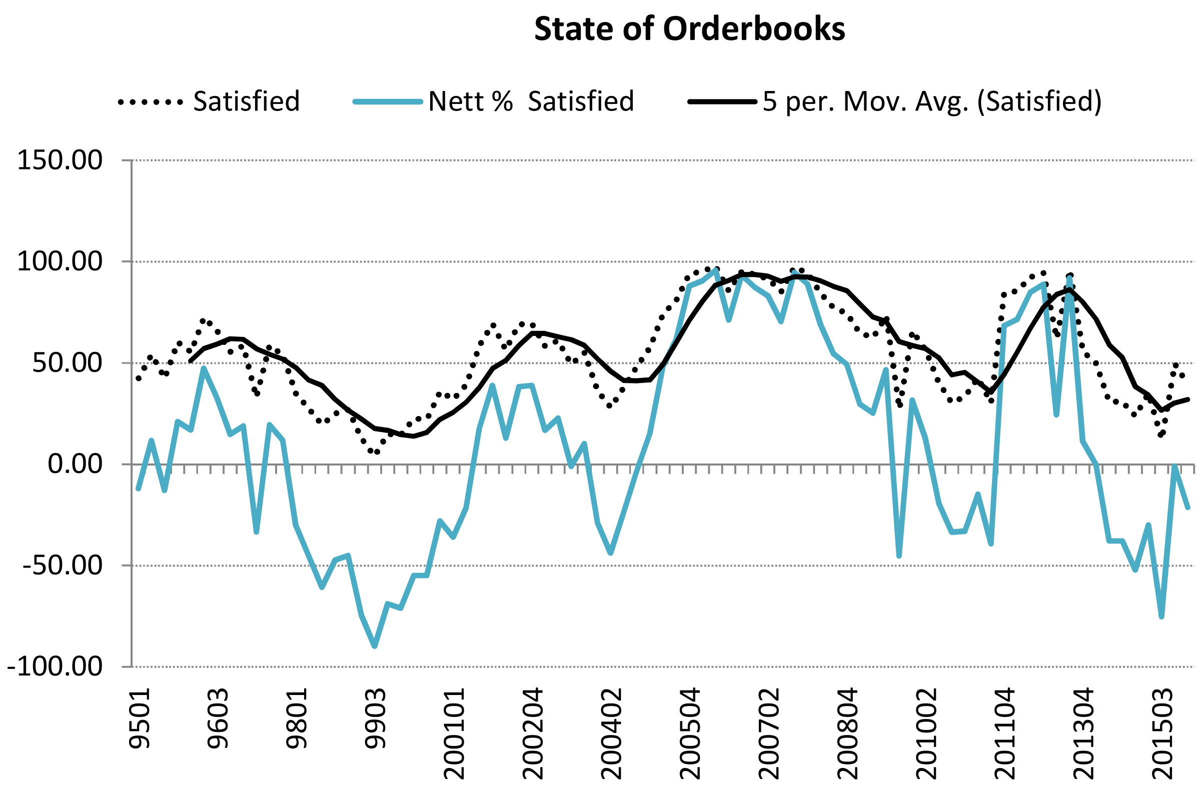



*Figure 20: State of Orderbooks*

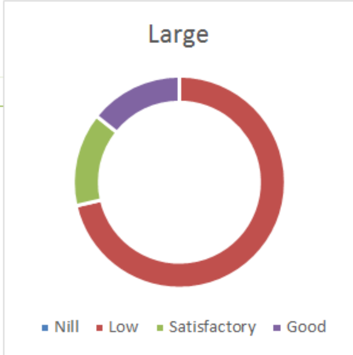
- The improvement in the nett satisfaction rate reported in the 4th quarter of 2015 was reversed in the 1st quarter of 2016, and deteriorated from a nett satisfaction rate of -1.0 to -21.3, as an increasing number of contractors expressed their dissatisfaction related to the state of their respective order books.
- Over 60 percent of contractors reported low volumes in order books, while less than 5 percent reported levels as good.

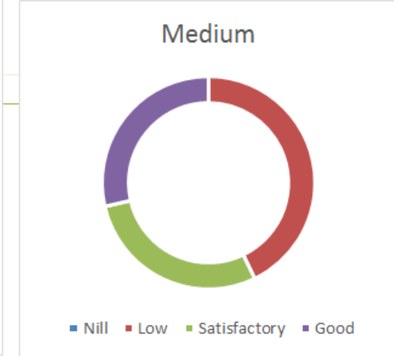
## Turnover

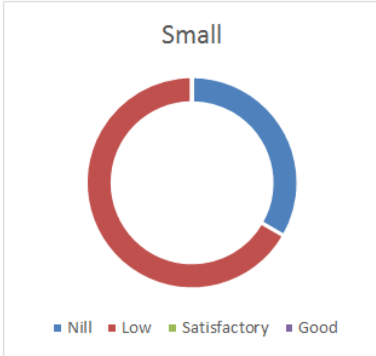
- The nett satisfaction rate in terms of opinions related to turnover also deteriorated from 22.8 percent in the previous survey to -6.0 percent. Fewer firms reported satisfactory conditions (41 percent, from 55,5 percent). Interestingly it was the larger firms that expressed some improvement in turnover, as 14 percent experienced relatively good levels of turnover. This sentiment was not shared by any of the medium or smaller contractors.

  Details of the current survey's opinions by firms size category are provided below.

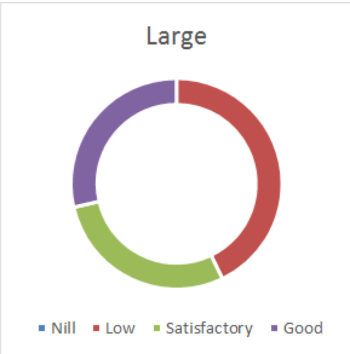
## TEnder Volumes

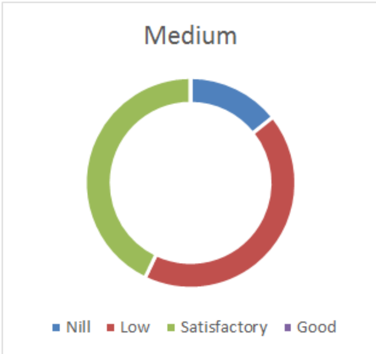


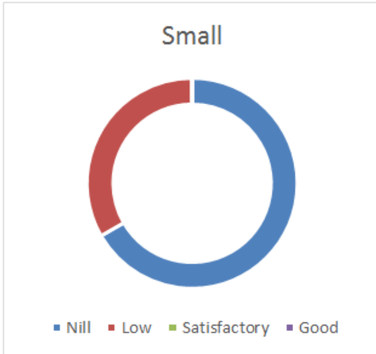



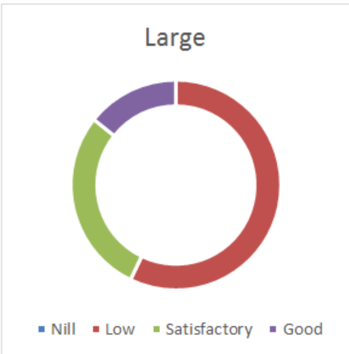

## Contract Awrads

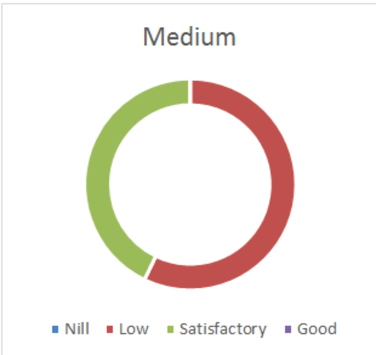


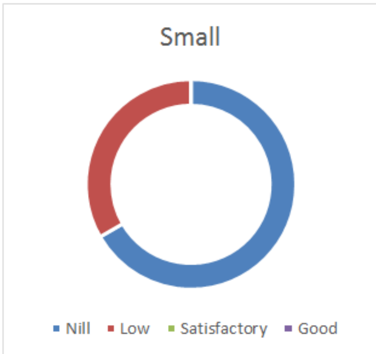



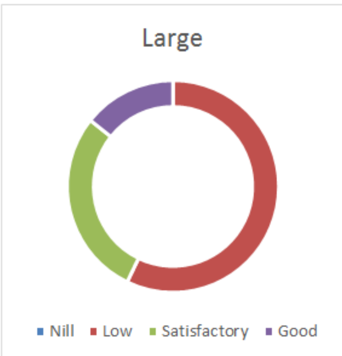

## Order Book

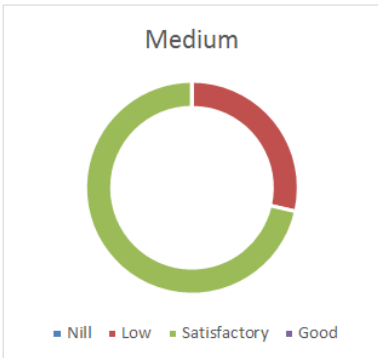


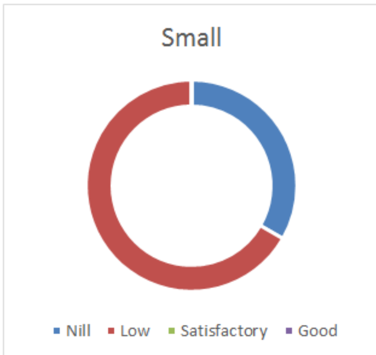




## Turnover



## Capacity Utilisation and Plant Equipment

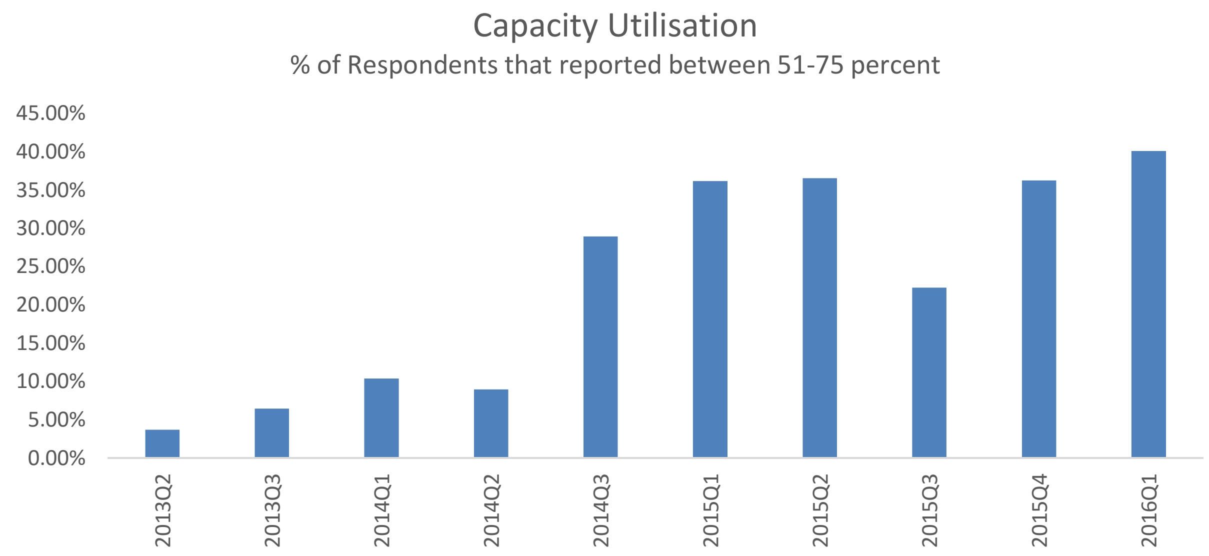
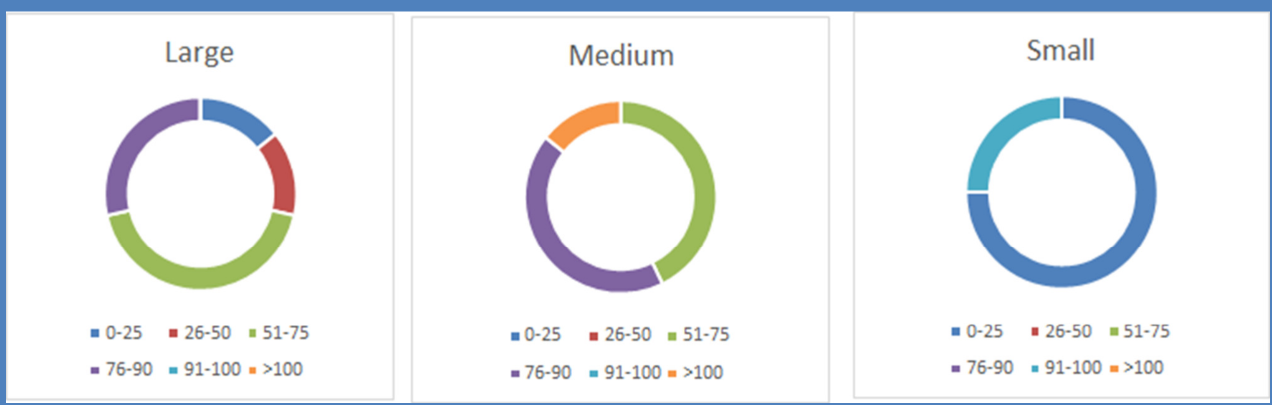



*Figure 21: Capacity Utilisation, % of Respondents that reported between 51-75 percent*

## CAPACITY UTILISATION AND PLANT EQUIPMENT

Majority of firms (40%) reported capacity utilisation in terms of general plant and resources of between 51-75%. in the 1st quarter of 2016, with an increasing number of firms (20%) saying utilisation was less than less than 25%. Since the last survey utilisation levels have clearly started to deteriorate. An increasing number of larger firms (71% from 62% in the previous survey) reported utilisation rates at below 75%, compared to 42 percent medium and 75 percent by smaller firms. All firm sizes categories reported lower utilisation rates in the current survey compared to the last survey.



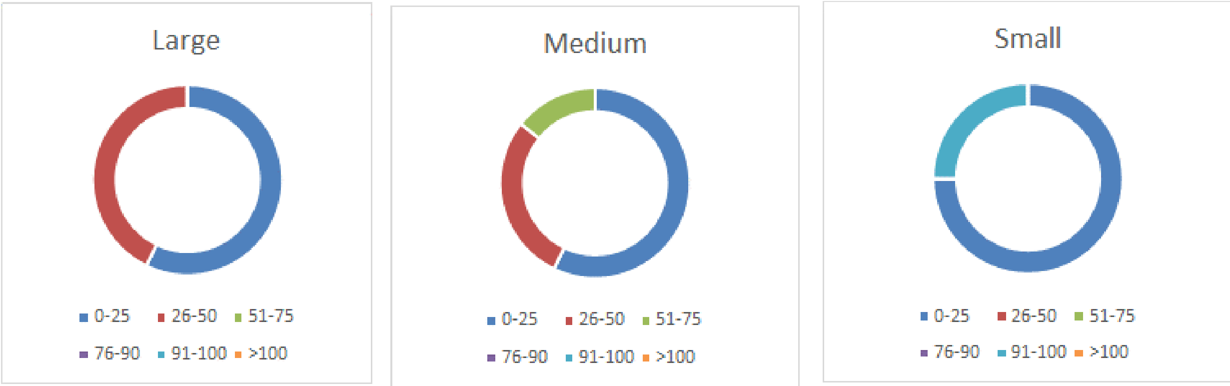



*Figure 23: Percentage of company's internal plant idle, by firm size*

The percentage of plant equipment standing idle increased in this survey. Although the majority still reported that less than 25 percent was idle (61 percent), an increasing number of mainly medium size firms reported levels of between 26% and 50% (37 percent vs 28 percent and 10 percent in the previous survey).

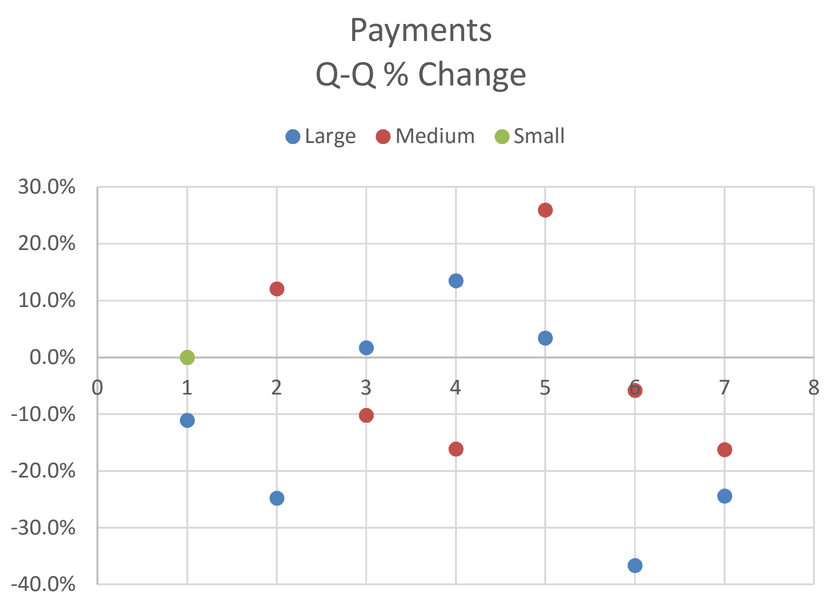

# Firm Size market segmentation

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

## Industry Turnover and Employment




According to responding contractors, nominal turnover based on certified payments received, fell by 10 percent q-q since the 3rd quarter, but was still up by 11 percent compared to the same quarter in 2014, coming off a much lower base. 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 firms reported experienced more difficult period in terms of payment compared to the 3rd quarter, while medium size firms ended flat (up 0.7 percent q-q). The nett satisfaction rate in terms of turnover, deteriorate to -38.6 percent in the current survey from (positive) 9.1 percent in the previous survey. Close to 70 percent of contractors were of the opinion that turnover was low.

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 Medium Term expenditure framework (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.

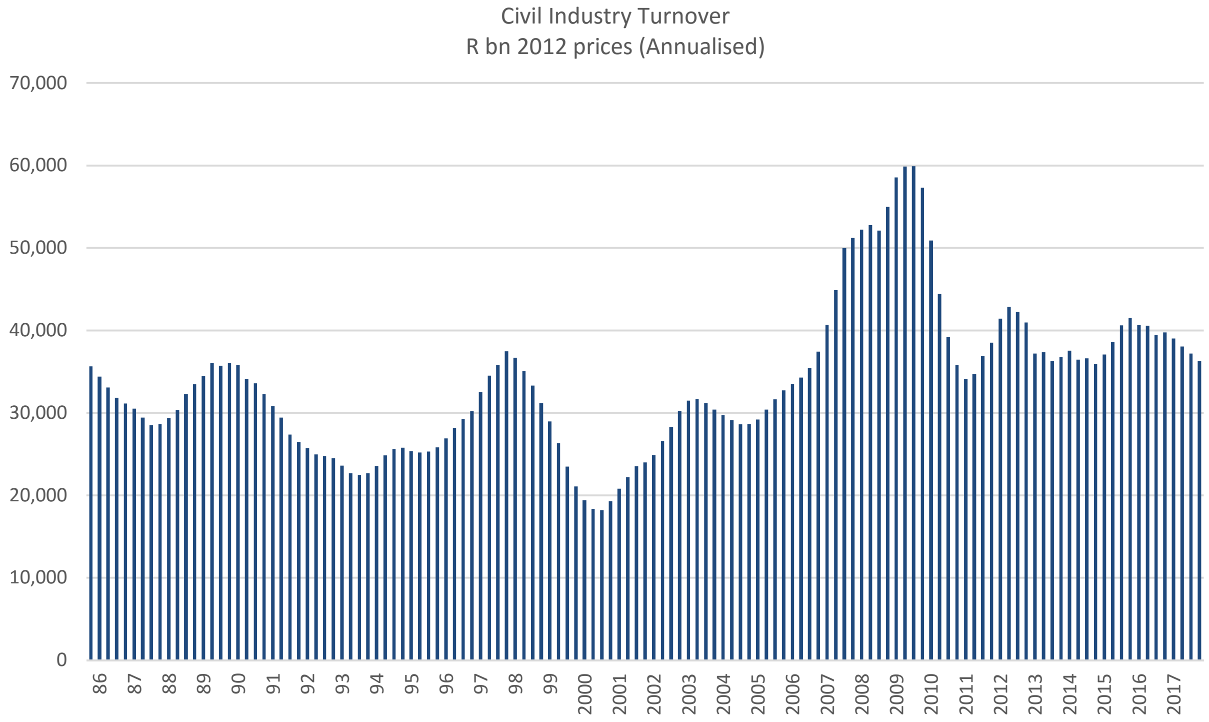



*Figure 24: Civil Industry Turnover, Rm 2012 prices (annualised)*

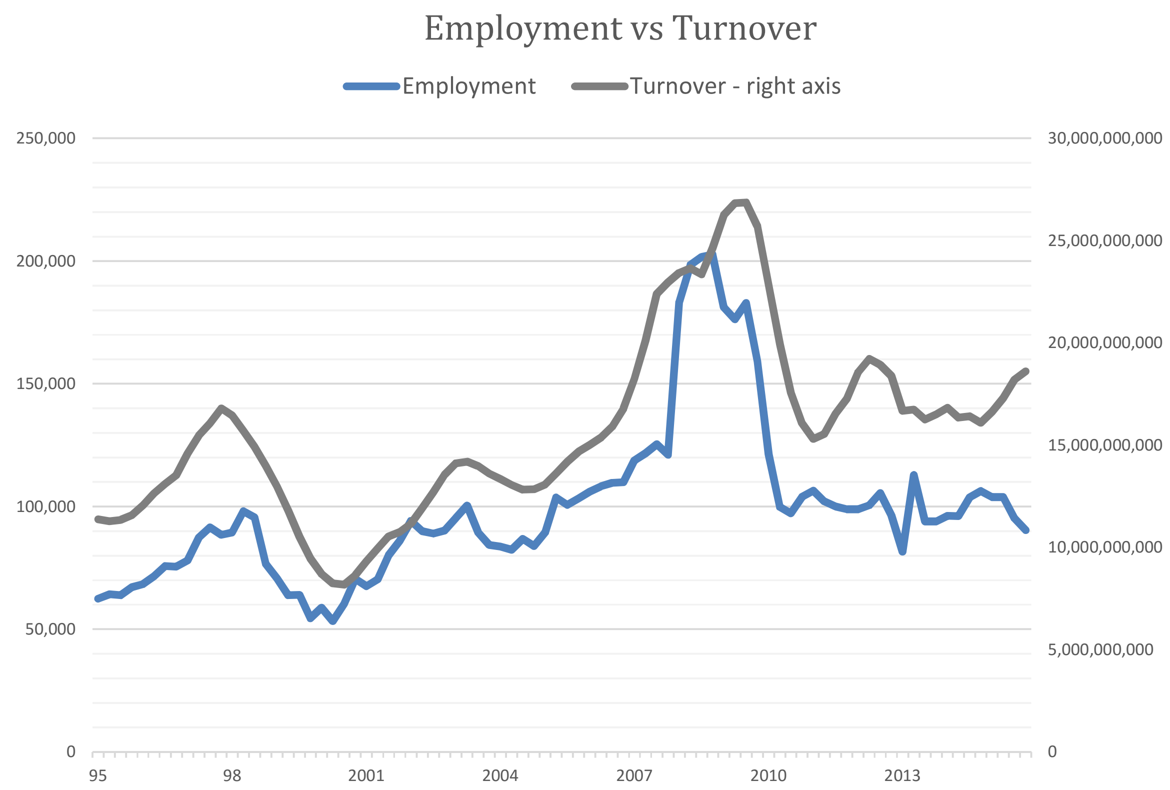



*Figure 25: Employment vs Turnover*

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 |

# Performance by listed contractors

WBHO: Revenue for the period ended December 2015, increased by 7 percent to R15.4 bn, largely due to a 19 percent increase in its operations in Australia. Revenue from operations in Africa fell by 5 percent. Revenue from roads and earthworks fell by close to 17 percent, with a 9 percent increase in the reported order book and although marginal growth was reported in building and civil engineering of 2.2 percent, this order books is up by 26 percent. Profitability improved by 26 percent, with a slightly improved margin of 3.2 percent.

Murray & Roberts: Interim results from Murray & Roberts for the period ending December 2015, reported a 4 percent decrease in revenue, as revenue across most of its divisions contracted expect for underground mining where revenue increased by 20 percent. M&R's order book increased by 7 percent, with robust growth reported in infrastructure and buildings (up 16 percent), power and water (up 43 percent), underground mining (up 18 percent), but with a 25 percent contraction in the oil and gas order book.

Aveng: Interim results for period ending December 2015, reported a 25 percent decrease in revenue, hard hit by a 40 percent decrease in revenue in Australasia and Asia (accounting for 39 percent of total revenue) while revenue in Africa fell by 10 percent. The order book improved marginally by 1 percent, although pipeline from Australasia improved by 22 percent, this was offset by a 20 percent contraction in the value of its mining order book.

Group Five: Interim results for the 6 month period ending December 2015 reported a 5 percent increase in revenue to R7.3 bn, supported largely by a 13 percent increase in revenue in its Building and Housing division and a 40 percent increase in Projects, while revenue in Civil Engineering fell by 22 percent and energy by 2.4 percent. Profitability improved and increased by 41 percent to R289million, improving its comparative profit margin from 3.1 percent to 4.0 percent. In spite of the groups improved revenue in its Building and Housing division profit fell by 24 percent, lowering its margin from 2.0 percent to 1.3 percent. Profit margins (loss) in the Civil Engineering division remained negative but improved from -2.7 percent to -1.4 percent. The company's overall order book fell 6 percent to R17bn.

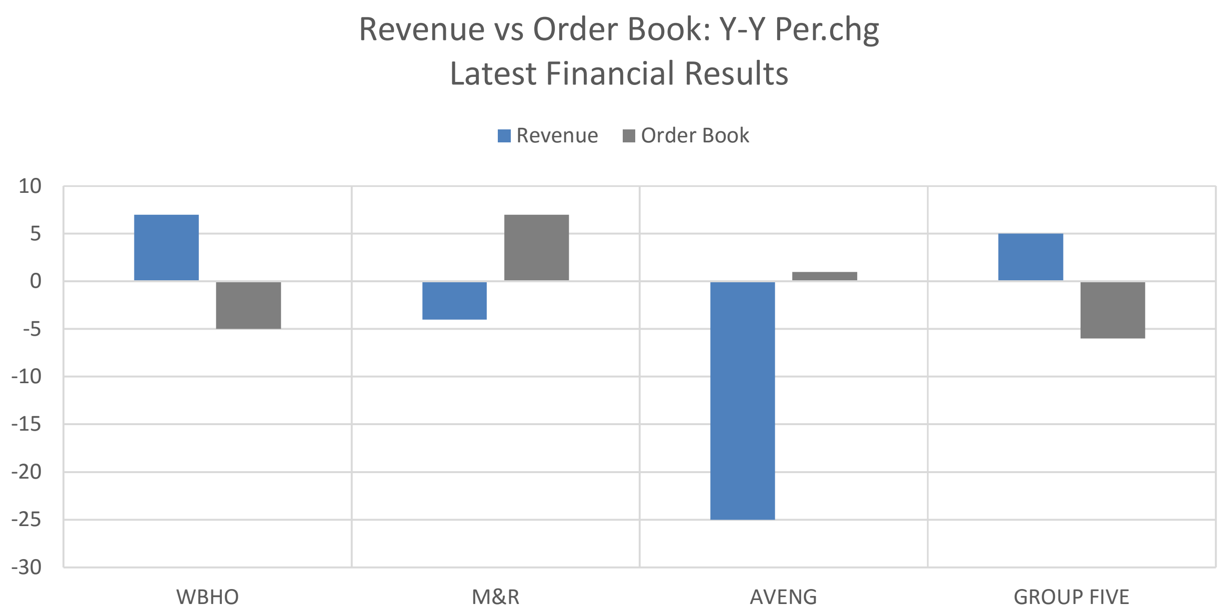


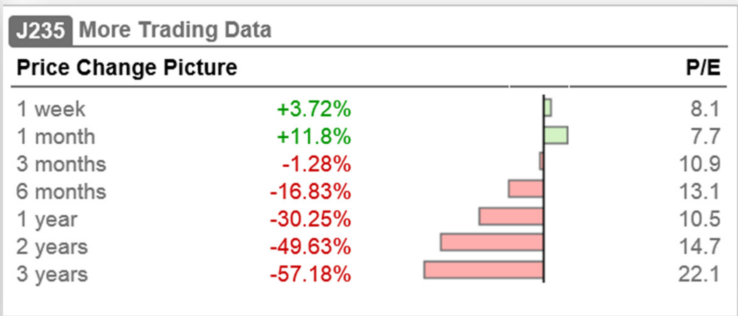

*Figure 26*

## Summary: Construction & Materials Index


*Figure 27: 3-month view*


*Figure 28: 3 year view*


*Figure 29: 10-year view*



**J235** More Trading Data

| Price Change Picture | | P/E |
|---|---|---|
| 1 week | +3.72% | 8.1 |
| 1 month | +11.8% | 7.7 |
| 3 months | -1.28% | 10.9 |
| 6 months | -16.83% | 13.1 |
| 1 year | -30.25% | 10.5 |
| 2 years | -49.63% | 14.7 |
| 3 years | -57.18% | 22.1 |

## 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.

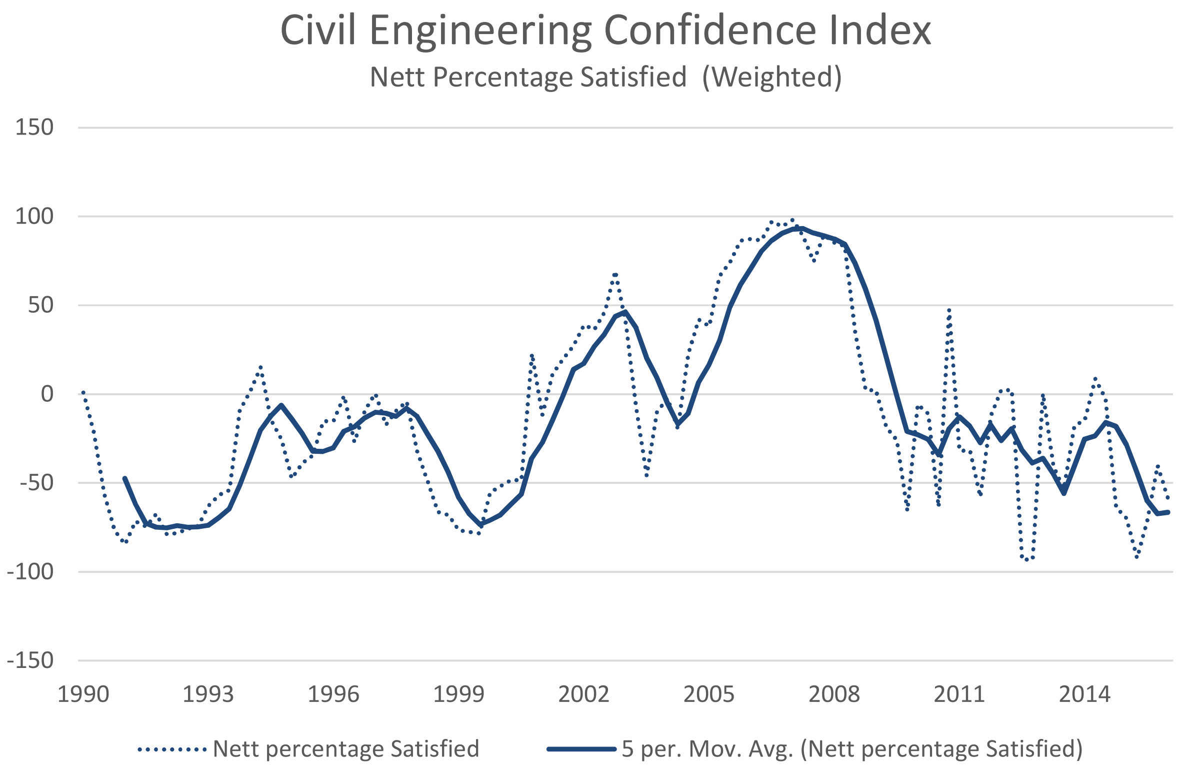



*Figure 30: Civil Engineering Contractors Confidence Index*

Culminating all the other indicators already discussed, the nett satisfaction rate fell to -59.0 in the current survey, from -40 in the 4th quarter survey. 55 percent of contractors surveyed reported current working conditions as being quiet (compared to 39 percent in the previous survey), while fewer reported satisfactory conditions (down from 52 percent to 39 percent). Medium and smaller size contractors are considerably more negative in this survey, as 43 percent of the medium size contractors reported "very poor" conditions. By comparison none of the larger firms shared this sentiment, and 42 percent reported conditions to be" poor" (as opposed to being very poor as reported by medium size contractors). This is some improvement amongst larger firms from the previous survey where 12 percent of contractors reported "very poor" conditions. In fact in the current survey, majority of the large contractors felt that conditions were satisfactory (57 percent, from 50 percent in the previous survey). Nonetheless survey results are subject to a relatively large degree of volatility, which is why data is smoothed over a five quarter period., and this shows a stabilisation of the trend line in the confidence index, albeit at a very low level of (negative ) -66.0.

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, recorded a marginal increase to 42 percent (from 39 percent) in the 4th quarter (latest available data), but has been below a satisfaction rate of 50 percent (except for a few short-lived quarters), 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.

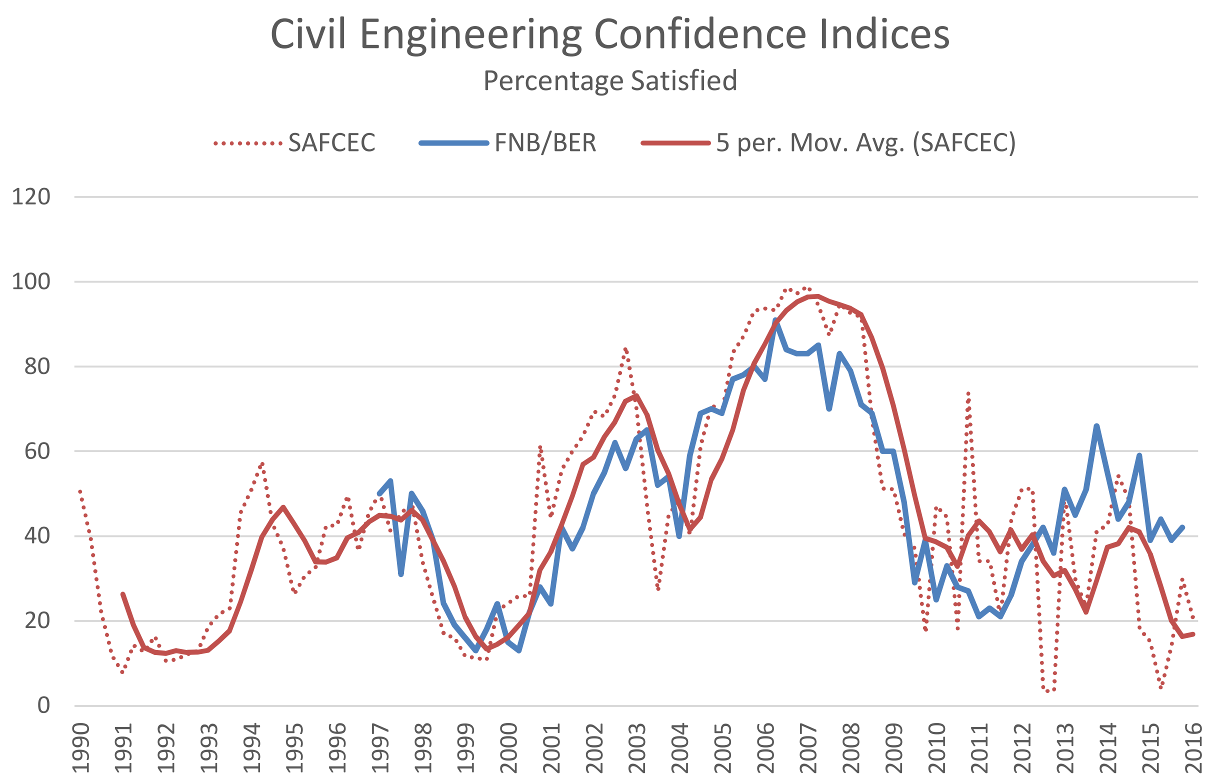



*Figure 31: FNB/BER Confidence index vs SAFCEC Confidence Index*

## Survey results EX-RSA

*Table 7: Business Conditions during the past two quarters*

| | *Previous quarter* | *Current Quarter* |
|---|---|---|
| *Very poor* | 29% | 0% |
| *Poor* | 29% | 67% |
| *Satisfactory* | 43% | 33% |
| *Good* | 0% | 0% |
| *Very Good* | 0% | 0% |
| *Nett Satisfaction* | -57% | -67% |

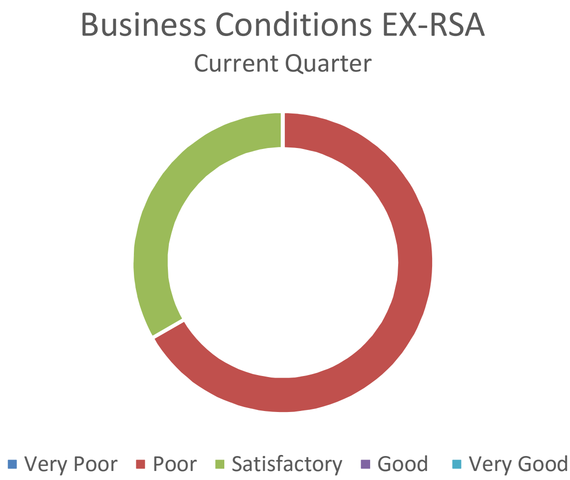
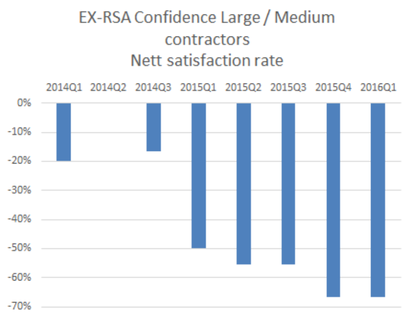
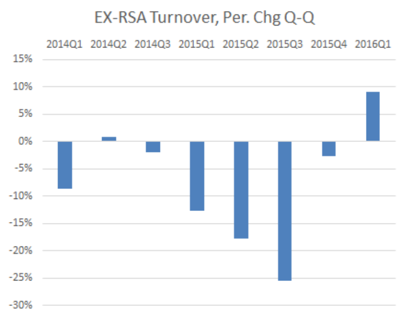
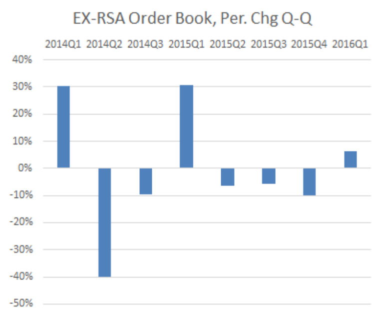



*Table 8: Late payments, order books and turnover, EX-RSA*

| 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% |



# 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

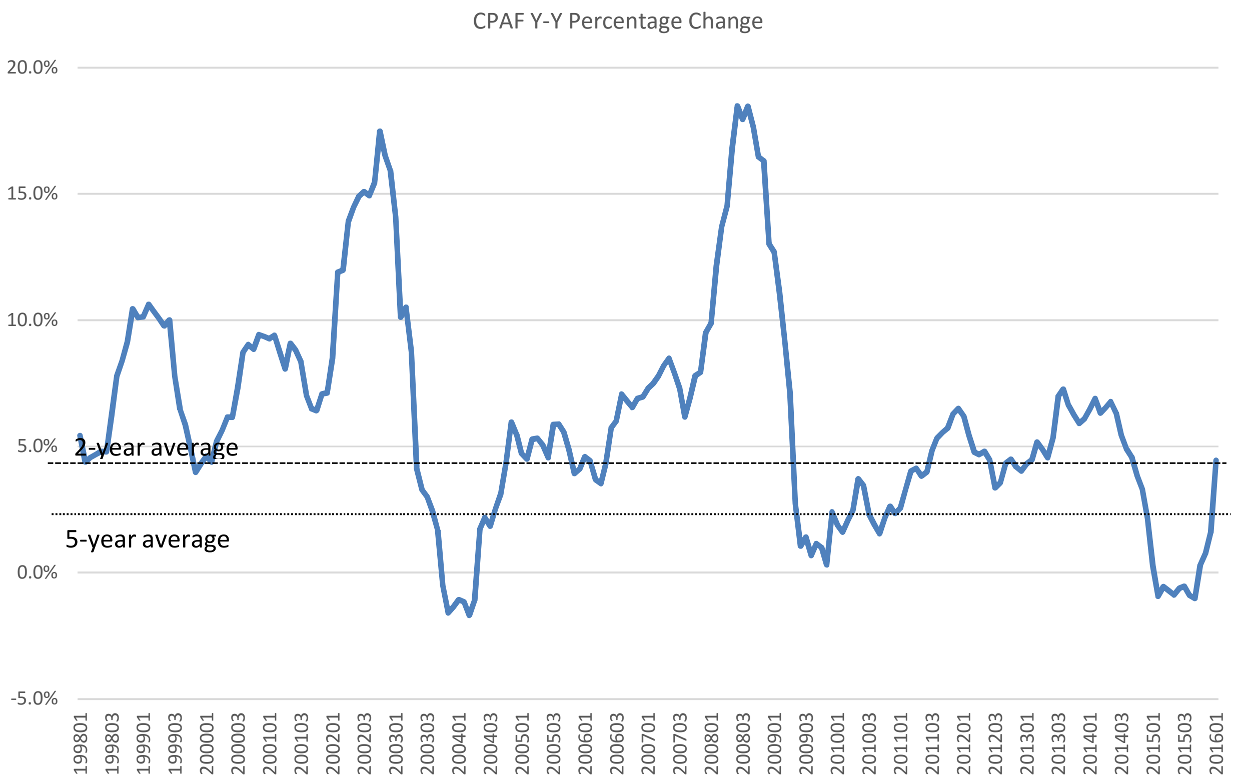
The Baxter Contract price Adjustment formula (or CPAF), is widely recognised by the industry as an accepted set of indices to adjust contracts for payment escalation. However, it is important to clarify that these set of indices are freely available and published by Statistics South Africa and is not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

Input cost price movements based on the Baxter contract price adjustment formula (CPAF) averaged (negative) -0.3 percent in 2015, compared to 5,3 percent in 2014. Deflation in the composite price index was recorded for the first three quarters of 2015, with a marginal increase of 0.9 percent in the 4th quarter, mainly due to stronger increase in plant equipment which was related to the rand's depreciation.

Contributing factors to deflation in 2015 include the between 23 percent and 25 percent y-y drop in the fuel index, and a sharper than expected contraction of around 5,2 percent y-y (average for the year 2015) in the composite material index. 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. These developments and the impact on input cost construction will be closely monitored.

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% | 5.3% |
| 2015 | -5.2 | -42.8 | 12.4% | 3.8% | -0.3% |
| 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% | 5.2% |



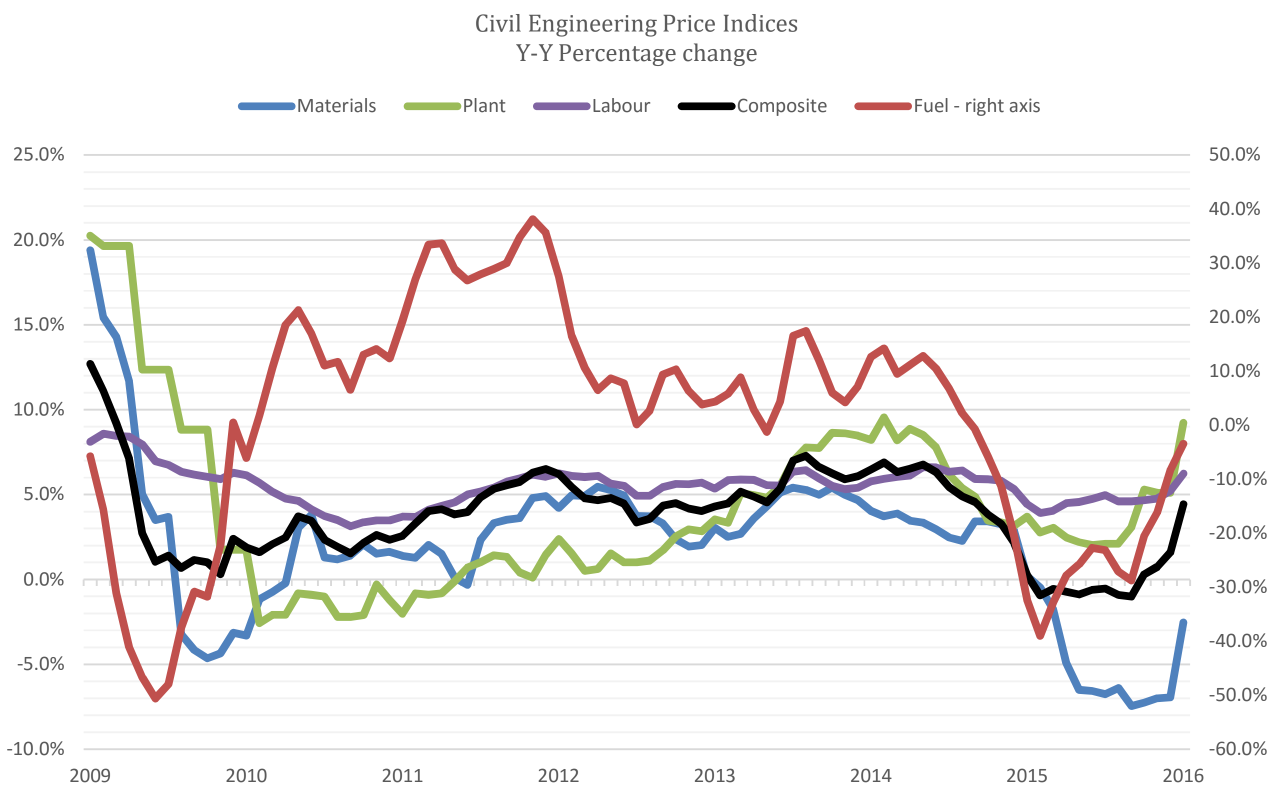




*Figure 32: Civil Engineering price movements (source Stats SA)*

*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 | 81.9 | 84.5 | 87.1 | 99.4 |
| 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 | 143.2 | 157.5 | 162.3 | 170.7 |
| Y-Y Percentage Change | | | | | | | |
| Plant | 1.6% | 6.3% | 6.4% | 12.4% | 26.0% | -1.9% | 3.8% |
| Fuel | 8.8% | 7.2% | 3.1% | -42.8% | 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% | 3.8% | 6.2% | 6.0% | 5.8% |
| Composite | 4.5% | 5.7% | 5.3% | -0.3% | 10.0% | 3.0% | 5.2% |

Table 20: CPAF Indices (Quarterly Average)

| | | CPAF Indices 2012=100 | | | | | Y-Y Inflation | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Year | Quarter | Materials | Labour | Fuel | Plant | Composite | Mater ials | 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 | 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 | 105.6 | 225.4 | 77.0 | 115.2 | 141.6 | -0.7% | 4.1% | -34.7% | 3.2% | -0.4% |
| | 2 | 101.3 | 230.8 | 85.7 | 115.8 | 142.9 | -6.0% | 4.6% | -25.5% | 2.2% | -0.7% |
| | 3 | 100.8 | 234.1 | 82.6 | 116.6 | 143.7 | -6.9% | 4.7% | -26.3% | 2.4% | -0.8% |
| | 4 | 100.9 | 234.7 | 82.8 | 119.3 | 144.7 | -7.0% | 4.7% | -14.8% | 5.1% | 0.9% |
| | *forecast | | | | | | | | | | |

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