RAPID GROWTH IN EMERGING MARKETS CREATES 2-SPEED RECOVERY

Construction costs in the UK have slipped a couple of places down the 'league table' of international costs and the UK is now 10th in Europe and 14th overall, compared to all countries covered in the EC Harris survey of International construction costs. The outlook for the UK construction sector remains tough over the next couple of years and pricing has remained keen as contractors have looked for workload at the expense of profits. Tender prices are expected to continue to fall through this year with recovery across much of the country not expected until the start of 2013, although London should pick up in mid 2012.

Compared to the UK, construction prices in Switzerland - the most expensive country in the survey - have soared and are now some 70% up on the UK although the comparison has been complicated by a rise of 17% in the value of the Swiss Franc.

The problems with the UK economy remain insignificant when compared to the ongoing problems in the PIIGS which will not be solved in the short term. The immediate results of these problems are cuts in construction costs over the past year of approx 14% in Ireland, 8% in Spain and 5% in Greece; with their economies still struggling, prices can be expected to continue to fall in those countries.

Commodity prices

Commodity prices across the world have risen significantly over the past 12 months and steel, copper and oil prices have been close to all-time highs with associated risks for contractors tendering on fixed price schemes.

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"Higher commodity prices continue to present problems, particularly in low cost countries where they can make a big impact on construction prices; in contrast, continuing economic problems and weak demand in parts of Western Europe mean that the supply chain continues to absorb price rises. Slow recovery in the USA means that construction prices have moved little since last year. Looking forward, growth in Asia will be broadly based; markets in Europe and the USA will underperform in comparison." **Simon Rawlinson, Head of Strategic Research and Insight**

Recent worldwide price increases have been driven by a number of common factors:- increased demand across the world, as countries/regions recover from the recession; the growing role of the BRIC countries as consumers and difficulties in supply.

However there are signs that the worst of the commodity prices rises are now behind us. Oil prices are already some 10% below their peak and prices falls are expected across a number of key commodities in 2012 and 2013.

Europe

Economic growth in Western Europe has been slow and the Eurozone is expected to grow by 1.9% this year with a further 1.7% in 2012. The slow recovery from recession has hit the construction sector and construction price movements have generally been restrained. Construction prices in France, Germany and Italy have remained virtually unchanged over the past year and remain 13%, 7% and 1% respectively above the level of pricing in the UK.

In Eastern Europe, there are more signs of recovery with growth in the new EU member countries expected to be 3.0% this year followed by a further 3.6% increase in 2012 while the economies of both Poland and Russia are expected to grow by 4-4.5% this year and next. Construction price in Russia rose by 9% over the past year, according to the EC Harris figures, while prices in Poland are approx 30% cheaper than the UK and fell by around 5% over the year. The fall in prices in Poland comes despite the ongoing preparation for the Euro 2012 Football Championship and substantial investment of EU structural funds in major infrastructure works.

The former Soviet satellite states and the countries which made up Yugoslavia are the cheapest in Europe, with costs, on the whole running at a level of 50-65% of UK costs. Croatia and the Czech Republic are exceptions to that rule, with prices running at around 65-70% of UK prices.

North America

Average construction prices in the USA remain around 10% below those of the UK, although US prices can show huge variations between the North East Seaboard and the poorer states of the Deep South.

The economies of most states are now growing once again with strong performances in the Northeast and Midwest. Growth in New York and Massachusetts was up by 5.1% and 4.2%, respectively although at the other end of the scale, Florida's economy grew just 1.4%, and Nevada's continued to shrink.

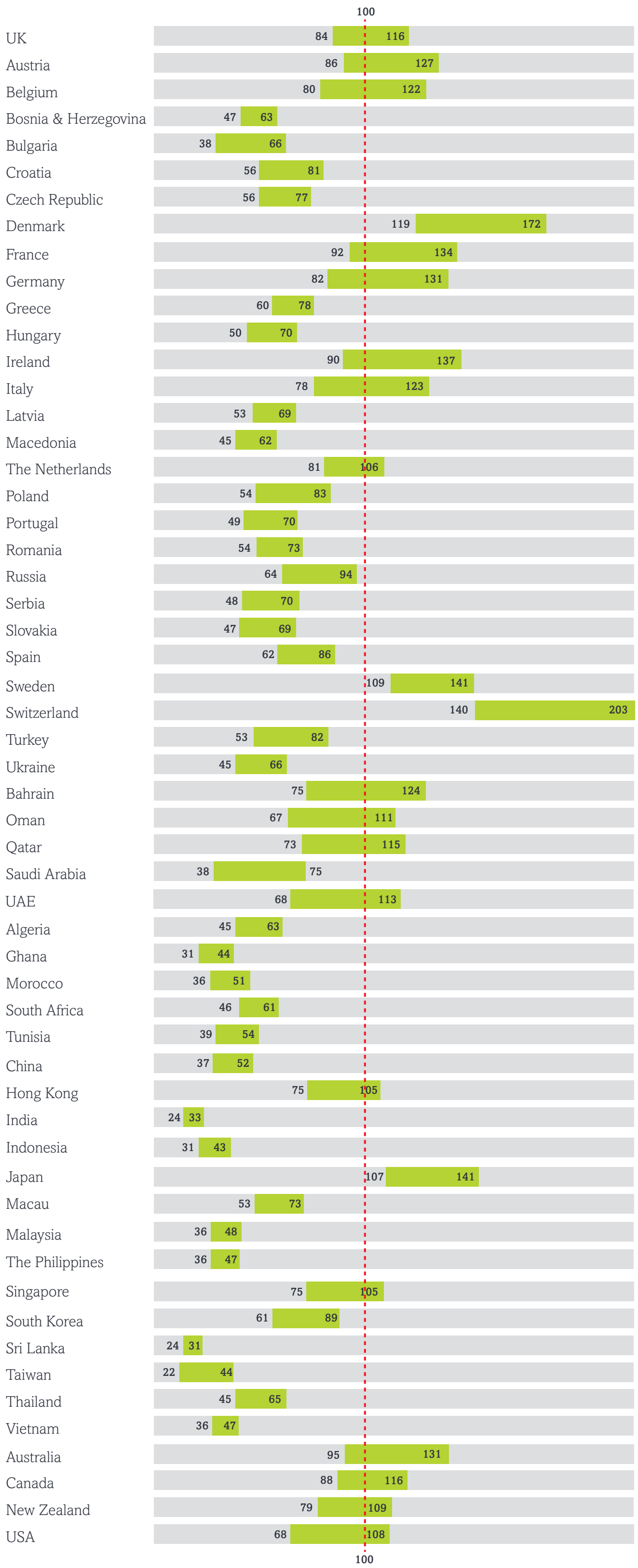
Even though the financial sector seems to be returning to health, financing remains a challenge for contractors across the USA and the depth and the duration of the recession put a severe strain on contractors' working capital. As the market recovers, bidders are expected to be in a position of having little or no cash from current projects, just as they are looking to increase activity.

Construction costs in Canada are marginally above prices in the UK although the differential has fallen over the past year partly due to a fall in the value of the Canadian dollar. Canada's economy has performed strongly in the past, and future economic growth looks secure due to its large reserves of natural resources. Canada is the leading crude oil supplier to the United States and high oil prices should ensure that the extraction of oil from the vast reserves of the Alberta tar sands is likely to play an important part in Canada's economy.

Middle East

The Middle East is showing signs of recovery with a number of specific sectors and markets benefitting from the Arab Spring. Huge social expenditure programmes have been announced in many countries for projects covering affordable housing, education, health and transportation sectors although progress in actually starting projects is slow.

International cost comparison graph



Note. The chart indicates the range of costs that can occur in each country when compared to costs in South East England - represented as the base of '100' in the graph.

Dubai has seen a restructuring of debts which should increase the appetite for external investment and some sectors are coming back including the leisure and hospitality sectors while the award of the 2022 Football World Cup in Qatar could eventually see a booming market in Doha.

Pricing In the region is grouped quite closely and is on the whole around 90-100% of UK costs. Bahrain is the most expensive of the GCC countries with prices around 11% above UK prices; at the other end of the scale, prices in Saudi Arabia are around 60% of UK prices.

Construction workload in the region is expected to be steady towards the end of 2011. In Qatar and the Kingdom of Saudi Arabia (KSA) a shortage of skilled labour is expected to push up labour costs. Inflation is expected to be very similar in the UAE and Saudi Arabia, but is expected to increase significantly in Qatar as a result of global energy demand. By mid 2012 it is anticipated that construction costs in the GCC will be very different to historic levels, with KSA prices rising at a sustainable pace and prices in Qatar reaching similar levels to those witnessed towards the end of 2007.

Asia Pacific

China and India are now the two main drivers of economic growth across the world and it is fortunate therefore that the Chinese economy is expected to continue to grow at a rate close to 9% p.a. while growth in India is expected to be not far behind.

However, in China, high levels of price inflation have forced the government to continue its tightening of monetary policy and are raising concerns over an economic slowdown. Sustained demand for residential, industrial and infrastructural expansion has generated the need for a multitude of new construction projects with increasing numbers being funded from the private sector.

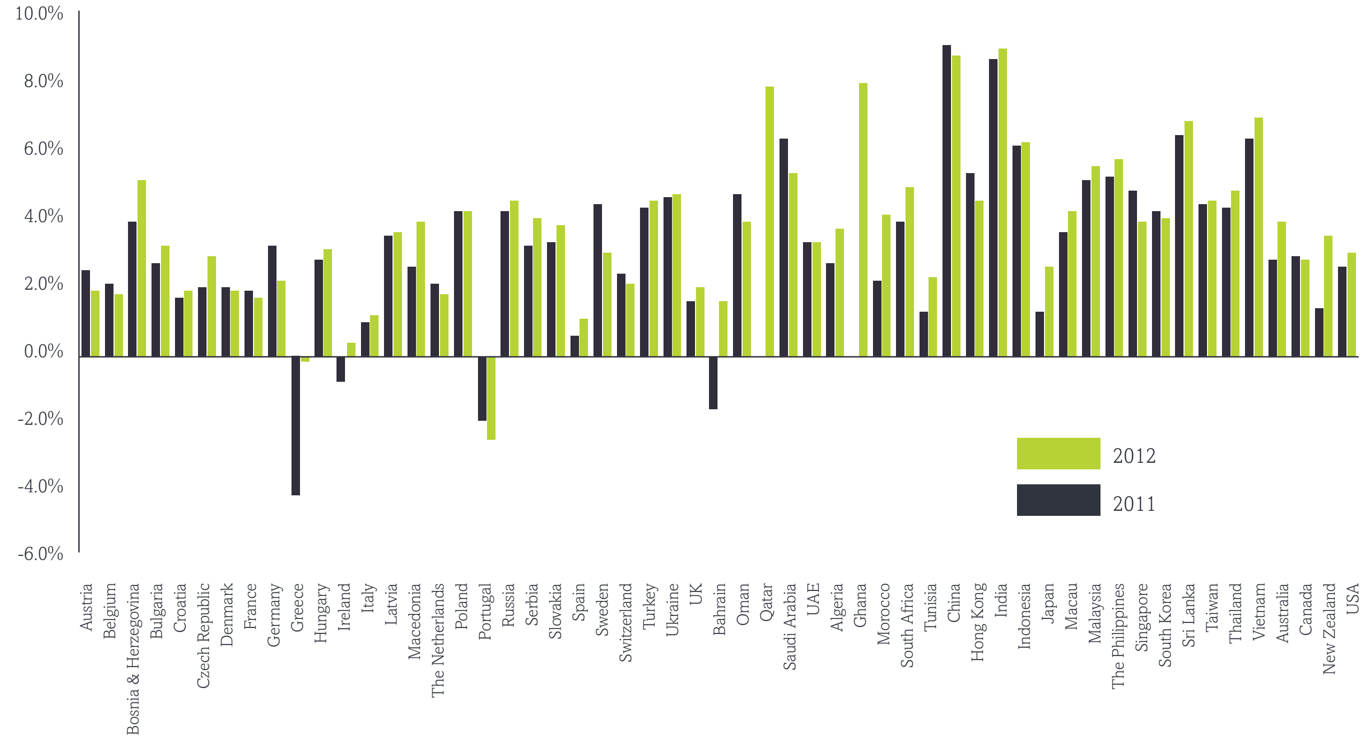
Similar to China, the Indian economy is racing ahead and facing inflation problems which, if sustained could see cuts in government construction spending. The construction industry in general has been growing at 9-11% year on year, primarily due to increased domestic and international manufacturing activities and industrial growth.

Overall construction prices across the region show huge variations. India and China are low cost countries with prices running at approx 70% and 55% respectively below UK costs. According to the EC Harris survey Japan remains the most expensive country in the region and construction costs are approx 24% above UK prices. However the survey took place before the March Tsunami which can logically be expected to push up construction prices as rebuilding starts.

Overall pricing levels in Singapore and Hong Kong are now fairly similar, running approx 10% below those in the UK, with continuing strong demand in these two regional rivals helping to maintain tender levels. The Singapore government is to introduce a number of measures to cool construction demand but workload around residential and commercial developments is expected to rise through 2011 and into 2012.

Consumer price inflation in Hong Kong is running at 5.2% and Hong Kong is going through a housing boom, despite measures taken to cool the market. Continued low interest rates and rising demand should mean that residential construction continues to press ahead while work on a number of major infrastructure projects is providing increased demand for contractors' services.

Worldwide Economic Growth (2011 - 2012)



Details of the survey

The indicative figures above have been calculated from a survey of construction costs in 56 different countries which was conducted across EC Harris' offices worldwide. Data was collected in cost per m² format for a wide spectrum of building types covering industrial, offices, retail, residential hotels, etc.

All buildings are deemed to be 'International', and constructed to Western European specification standards, but there will always be differences in specification for the same building constructed in different countries.

Procurement and contractual arrangements can also have a substantial effect on costs. Site labour costs remains one of the key drivers while the sourcing of materials, including the use of imported mechanical and electrical engineering plant, can have a profound effect on prices.

The full EC Harris publication gives cost per m² figures for 44 different building types, across all sectors.

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