

2023

CONSTRUCTION

SUPPLY CHAIN

Q1 UPDATE



EBOSS

THE CURRENT SITUATION:

Supply issues have eased dramatically, but in a softening market suppliers need to carefully position their business and resources.

In July 2021, eight in ten businesses were having issues supplying the market. This has dropped back to just three in ten in February 2023.

With supply getting back to pre-covid levels, what is the impact on the price of building products and the buildability of residential and commercial buildings? Over the last two years the price of building products has increased 45%, however, current pricing suggests that price increases will become a thing of the past with one in ten suppliers forecasting that they will lower the prices of products over the next six months.

It is a delicate position for suppliers, who require careful management to navigate a softening market. They need to balance:

- Residual impact of a 79% increase in the costs of their materials over the last two years
- Rising domestic costs driven by staff costs and operational costs
- Holding higher levels of stock and increased finance costs

The February 2023 BRANZ forecast paints a 18% drop in residential consents and a stabilisation at near record levels for commercial construction. This suggests that the industry may not be as badly impacted as previously reported.

THE SURVEY

The data for this update was gathered in February 2023, with responses from managers of 224 leading product suppliers across all main product categories.

CATEGORY:

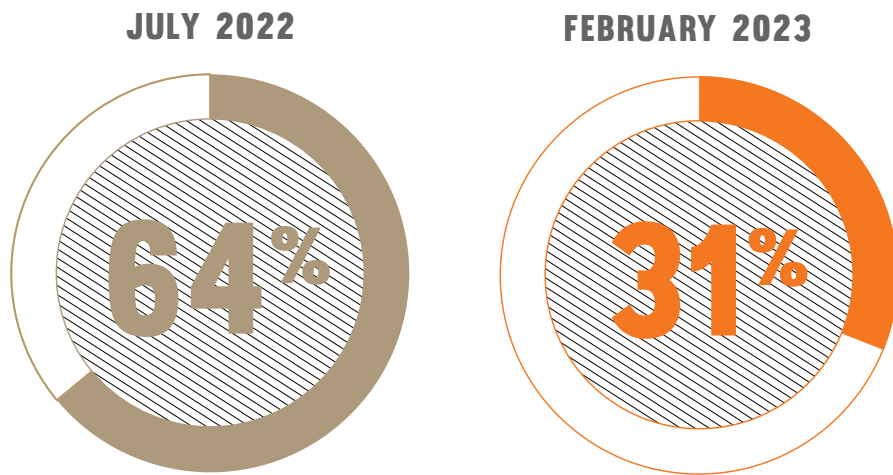
Structure	n=38
Enclosure	n=77
Interior	n=71
Finish	n=44
External & Other	n=43

REVENUE:

Under \$10m	n=41
\$10m - \$49.9m	n=44
\$30m +	n=32
Not provided	n=107

SUPPLY CONSTRAINTS HAVE REDUCED DRAMATICALLY

THE PROPORTION REPORTING ISSUES SUPPLYING THE MARKET HAS HALVED

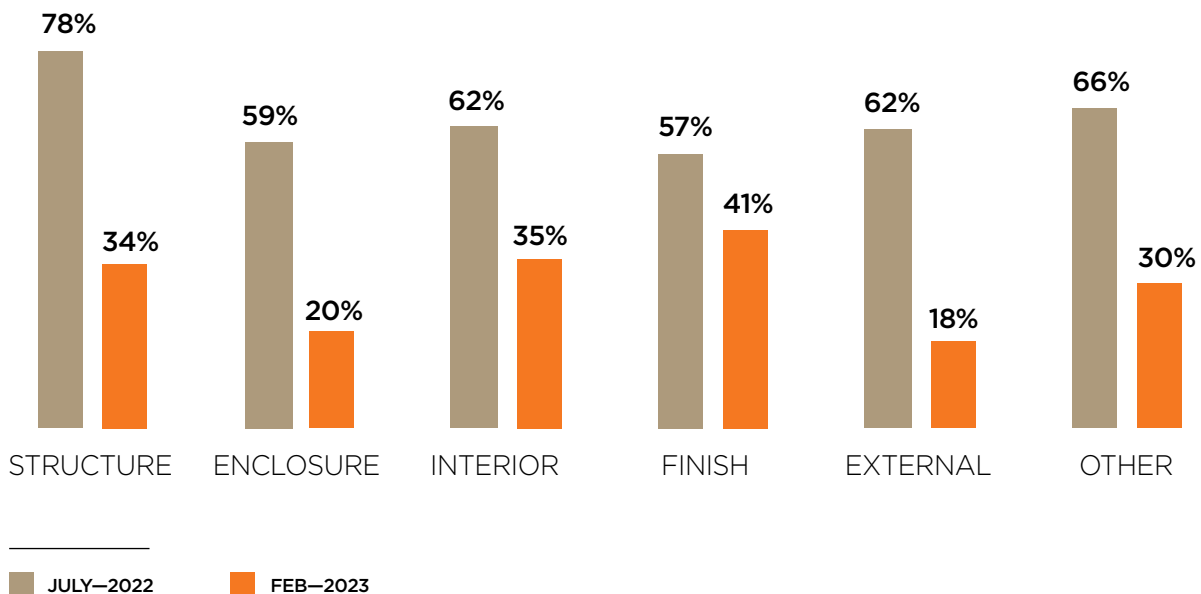


The proportion of suppliers experiencing issues supplying the market has halved in the last six months as freight and supply chain issues have eased.

What suppliers are faced with now is balancing stock levels against softening demand, and balancing the cumulative impact of historical price increases while maintaining price competitiveness.

Thus, while it may look like a more positive picture in terms of constrained supply, we are still at a critical point in terms of business' financial sustainability.

THE PROPORTION OF SUPPLIERS EXPERIENCING SUPPLY ISSUES DIFFERS BY CATEGORY

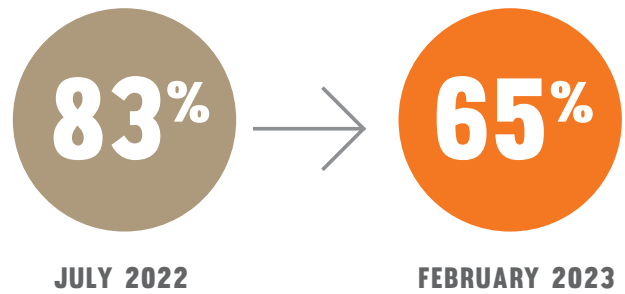


FREIGHT PRESSURES ARE SHIFTING CLOSER TO HOME

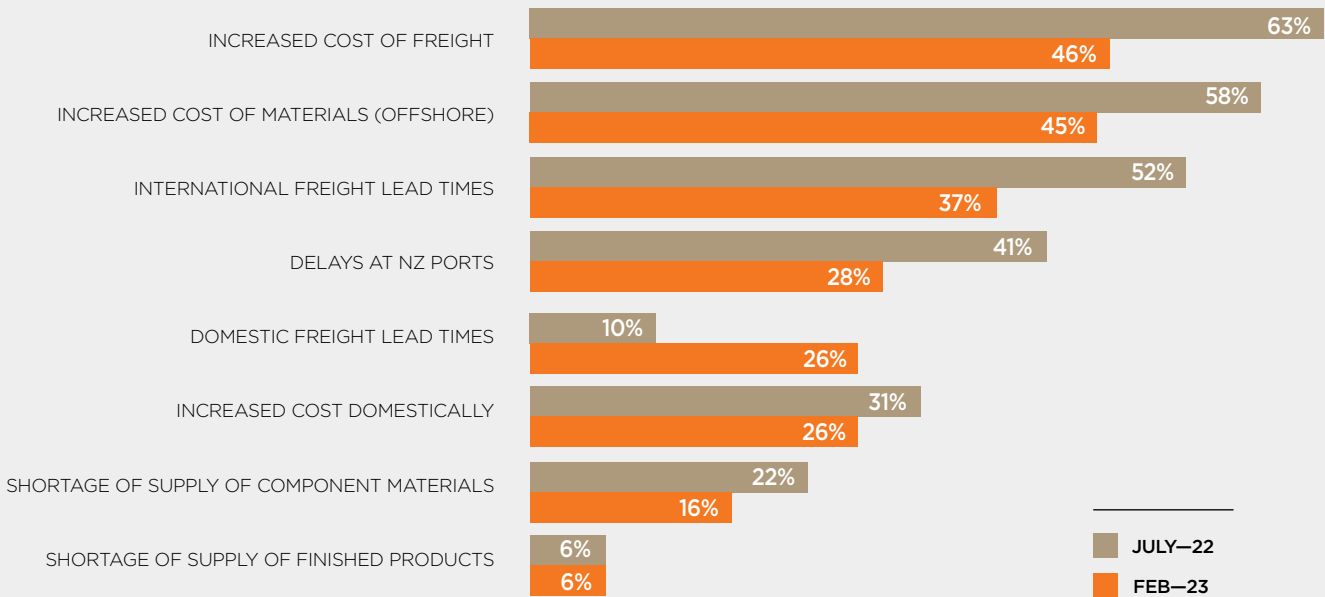
The picture around freight has changed in the last 12 months, from constrained international freight to constrained domestic freight. The recent weather events will have a further impact on this issue.

One in three (31%) say they are facing delays with domestic freight due to longer lead times compared to a year ago, while just 11% say the same for international freight.

EXPERIENCING FREIGHT ISSUES



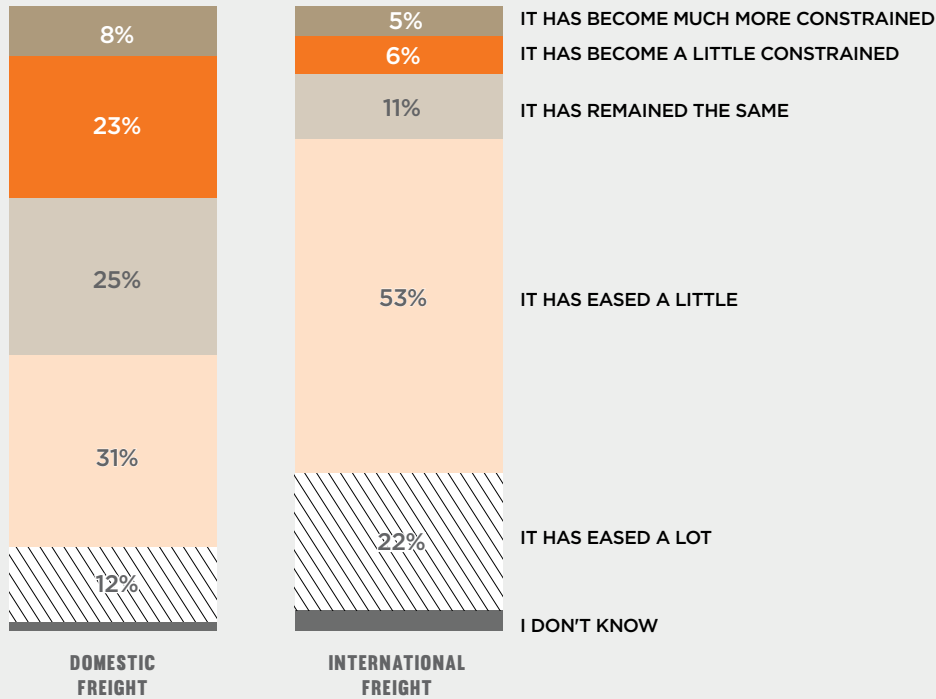
FACTORS IMPACTING YOUR ABILITY TO SUPPLY RIGHT NOW



“International container shipping costs are still higher than pre-pandemic levels but are substantially coming back closer to normal.”

“There is not enough personnel to get the product onto the floor. This is the main issue right now — skilled trades people. This results in project delays, and subsequently increased costs as product hasn’t been ordered.”

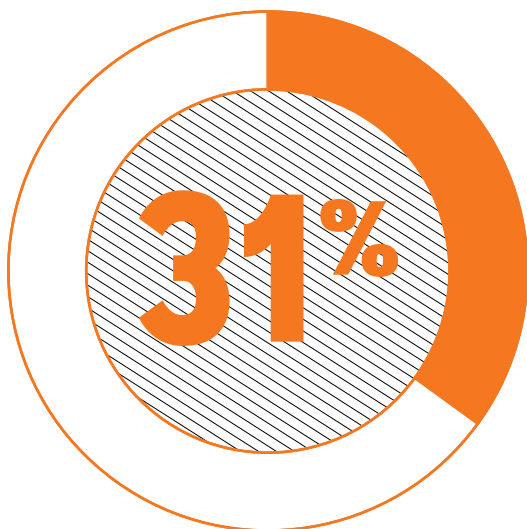
COMPARED TO A YEAR AGO, HOW HAS DOMESTIC AND INTERNATIONAL FREIGHT CHANGED?



“[There will be] long term effects on the logistics industry within NZ due to the damage to our roading infrastructure.”

“It’s not so much the cost of the freight, it’s more the logistical challenges with so many bridges gone and roads closed.”

DOMESTIC FREIGHT HAS BEEN HAMPERED BY RECENT WEATHER EVENTS



OF SUPPLIERS HAVE BEEN IMPACTED BY THE RECENT NORTH ISLAND WEATHER EVENTS

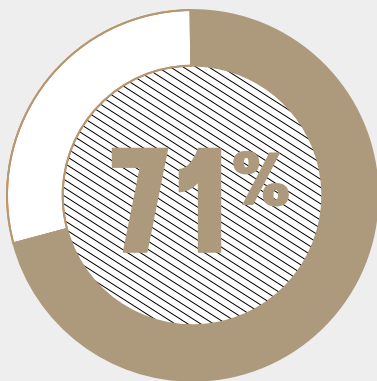
This survey was conducted after the anniversary weekend floods and Cyclone Gabrielle. While just 4% said they had been significantly impacted, a further 27% said they were somewhat impacted. When added to inflationary pressures and other factors impacting supply, it’s just one more issue to deal with.

The impact of the weather events was higher for larger revenue businesses — 38% of \$30m+ businesses say they are impacted, compared to just 24% of businesses with revenue under \$10m.

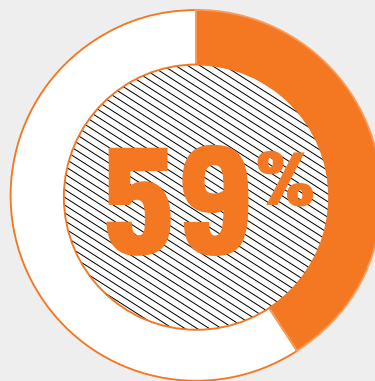
“We experienced delayed service initially. The expectation is a significant upside once the extent of the damage is realised and remedial work is actioned.”

“One major supplier out of action for 4 months. We are able to cope with alternative supply.”

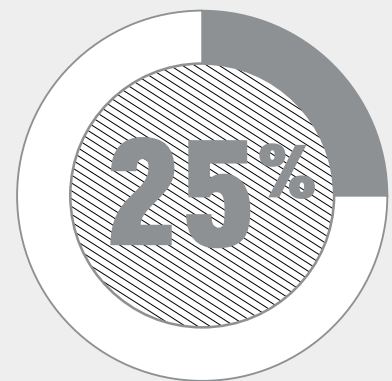
BALANCING THE RISK OF ELEVATED STOCK LEVELS IN A SOFTENING CONSTRUCTION MARKET



**INCREASED THEIR STOCK HOLDINGS
FEB TO JULY 2022**



**INCREASED THEIR STOCK HOLDINGS
AUG 22 TO JAN 23**



**MAINTAINED (LIKELY ELEVATED) STOCK HOLDINGS
AUG 22 TO JAN 23**

We asked suppliers in July 2022 whether they had increased, decreased, or kept stable their stock holdings compared to six months prior. We asked the same again in February.

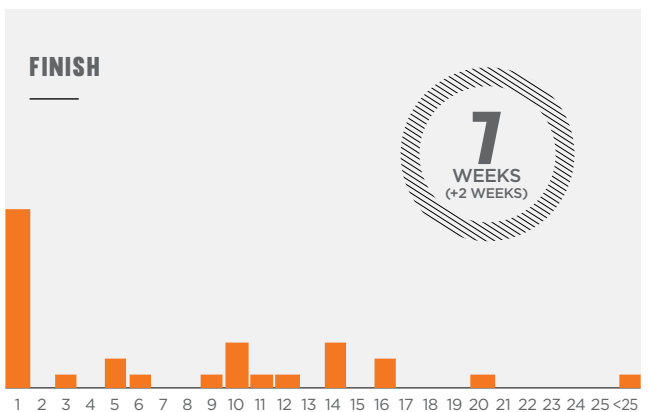
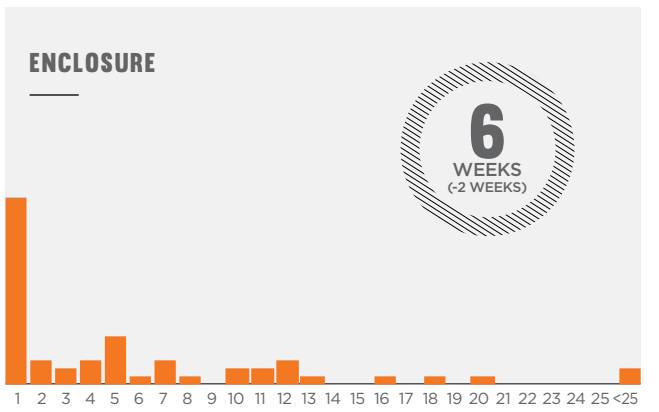
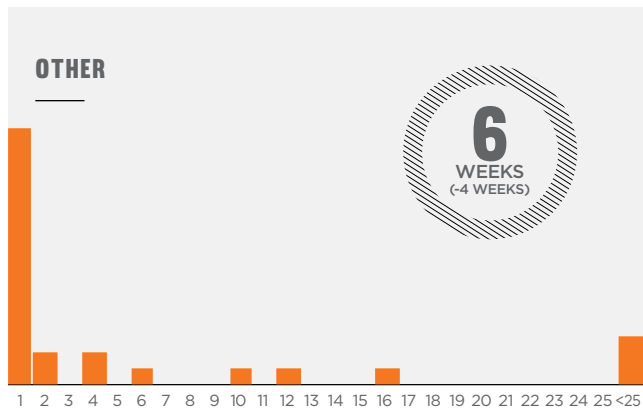
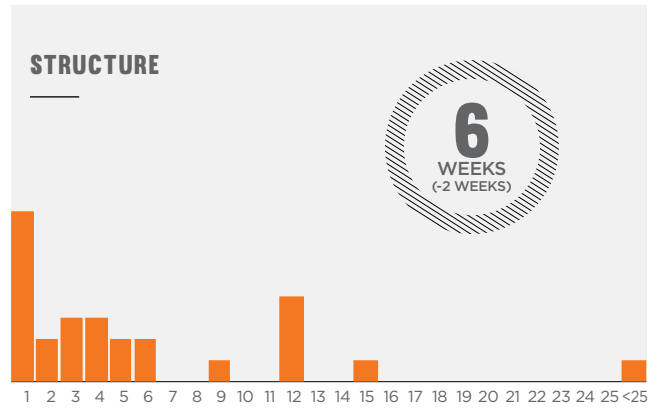
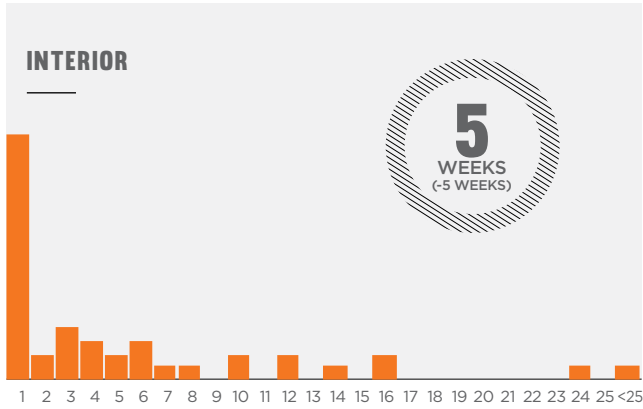
In July last year, 71% of suppliers had increased their stock holding. Since then the majority of suppliers (59%) have further increased their stock levels, with a quarter stabilising their already elevated stock holdings.

What this means is that the already elevated stock holdings from last year remain, and have likely increased again from where they were six months ago.

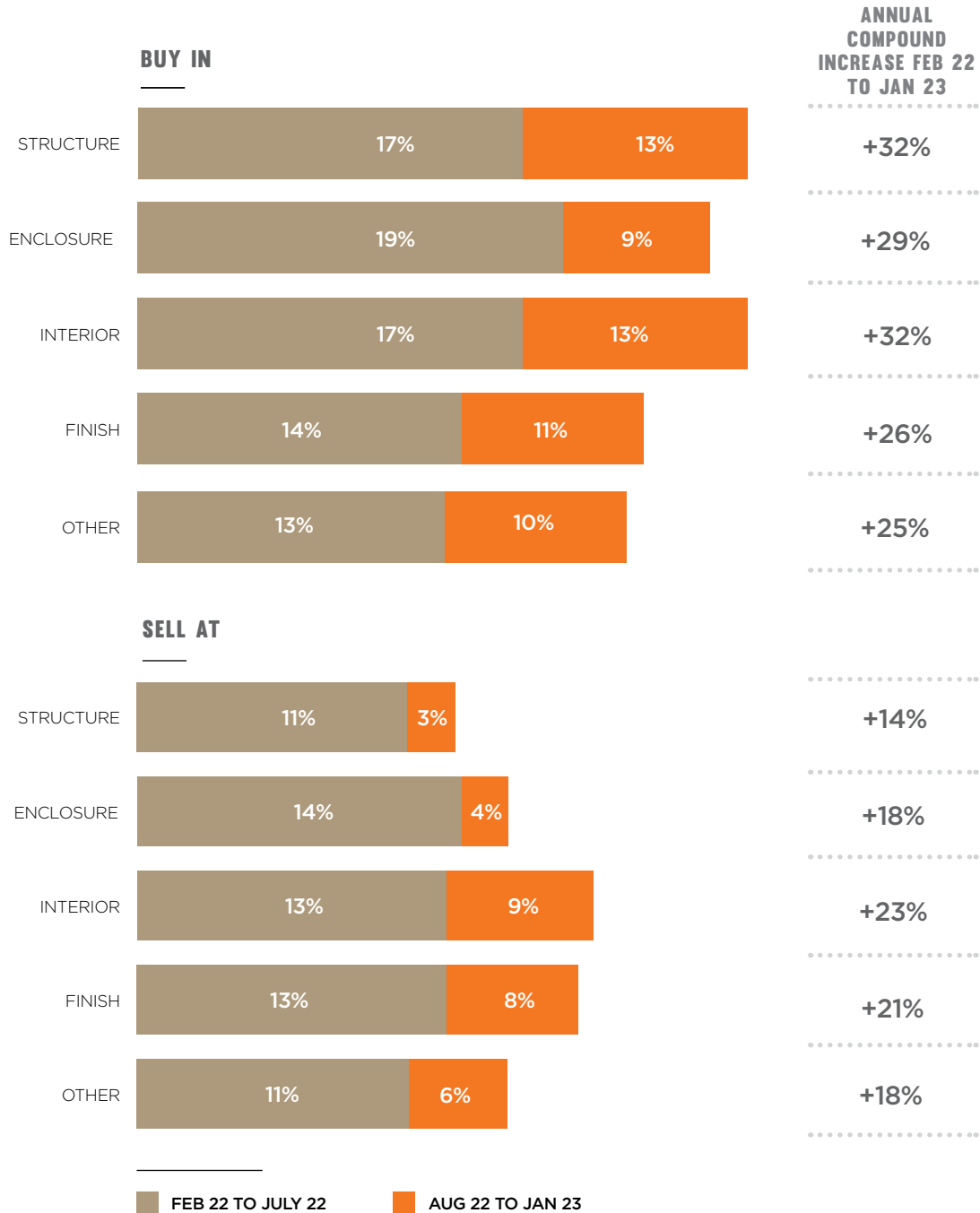
While average lead times are declining, this may be at the expense of cash flow for suppliers. It also means that even if buy-in costs start to decline, suppliers are holding stock purchased at an elevated rate with higher overheads and increased finance costs, and it will take a while for this to filter through the market.

LEAD TIMES CLOSING IN ON PRE-COVID LEVELS

AVERAGE LEAD TIME



PRICES INCREASED BY 19% ON AVERAGE IN THE LAST YEAR



SQUEEZED MARGINS LED BY STRUCTURAL PRODUCTS

ACTUAL JULY 22 TO JAN 23



11% IS THE AVERAGE INCREASE TO THE COST OF MATERIALS TO SUPPLIERS (SUPPLIER BUY COST)

6% IS THE AVERAGE INCREASE TO CUSTOMERS (SUPPLIER SELL PRICE)

Structural products show the most price disparity. Suppliers of products in this category are most likely to say there are increases they won't pass through (54% say this).

Comments suggest that this is in an effort to maintain a competitive position.

SUPPLIERS ARE REDUCING MARGINS TO MAINTAIN STABILITY:

"We have sacrificed margin as much as we can to maintain stability in the market. We are definitely making less money but hope that the international reductions in raw material costs and exchange rate rebounds we are seeing will bring that right as new stock lands."

WITHOUT THAT PRICE STABILITY, THERE'S A FEAR OF LOSING PROJECTS:

"Our product is a high-end item and we already struggled with costs to the client before any increases happened from our supplier. We will find it harder in today's market to push projects across the line."

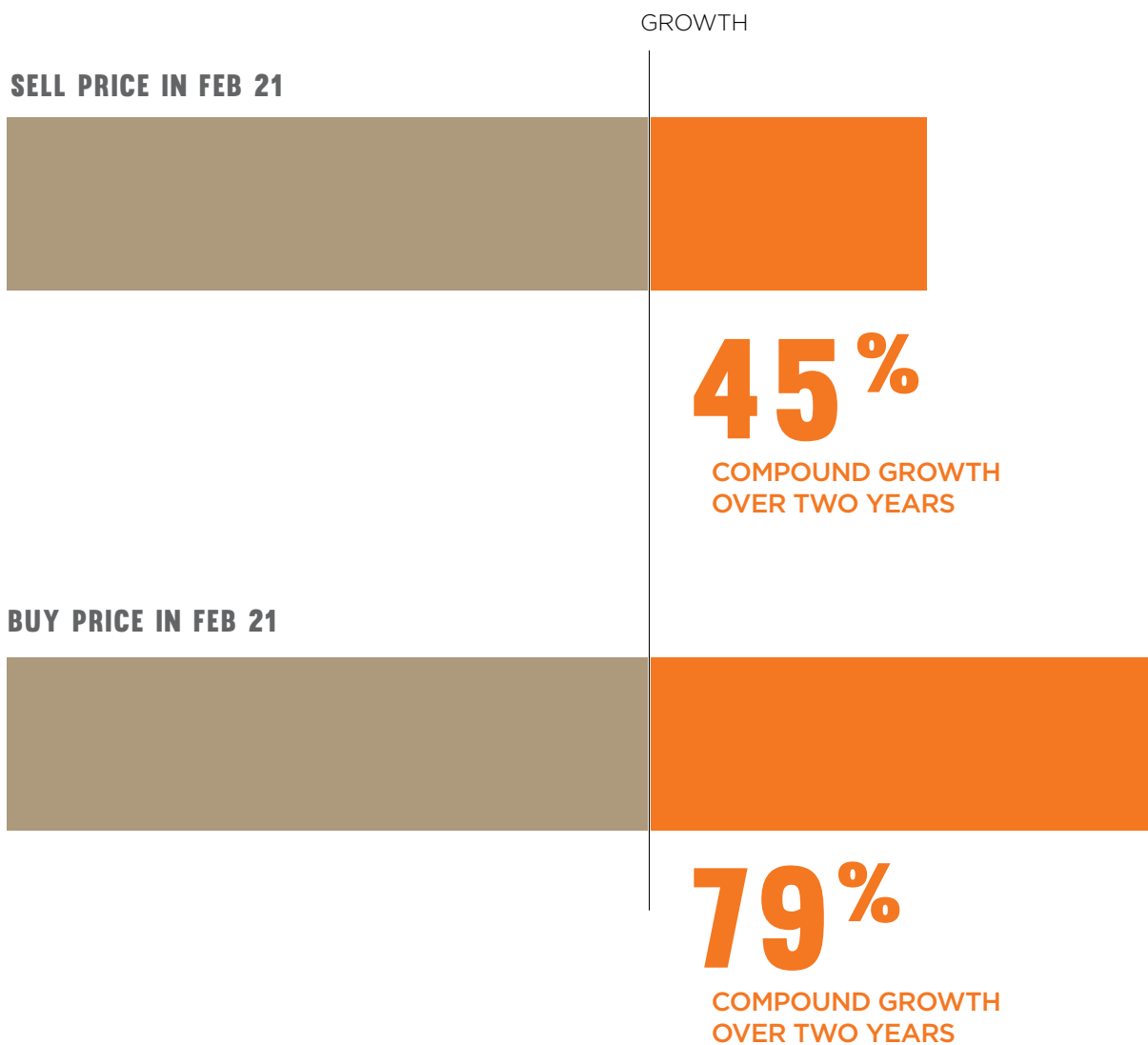
THOUGH THERE ARE PLANS TO START PASSING THROUGH HISTORICAL INCREASES:

"The buying cost increases which we have experienced in the last 6 months will be passed to the customers from March onwards."

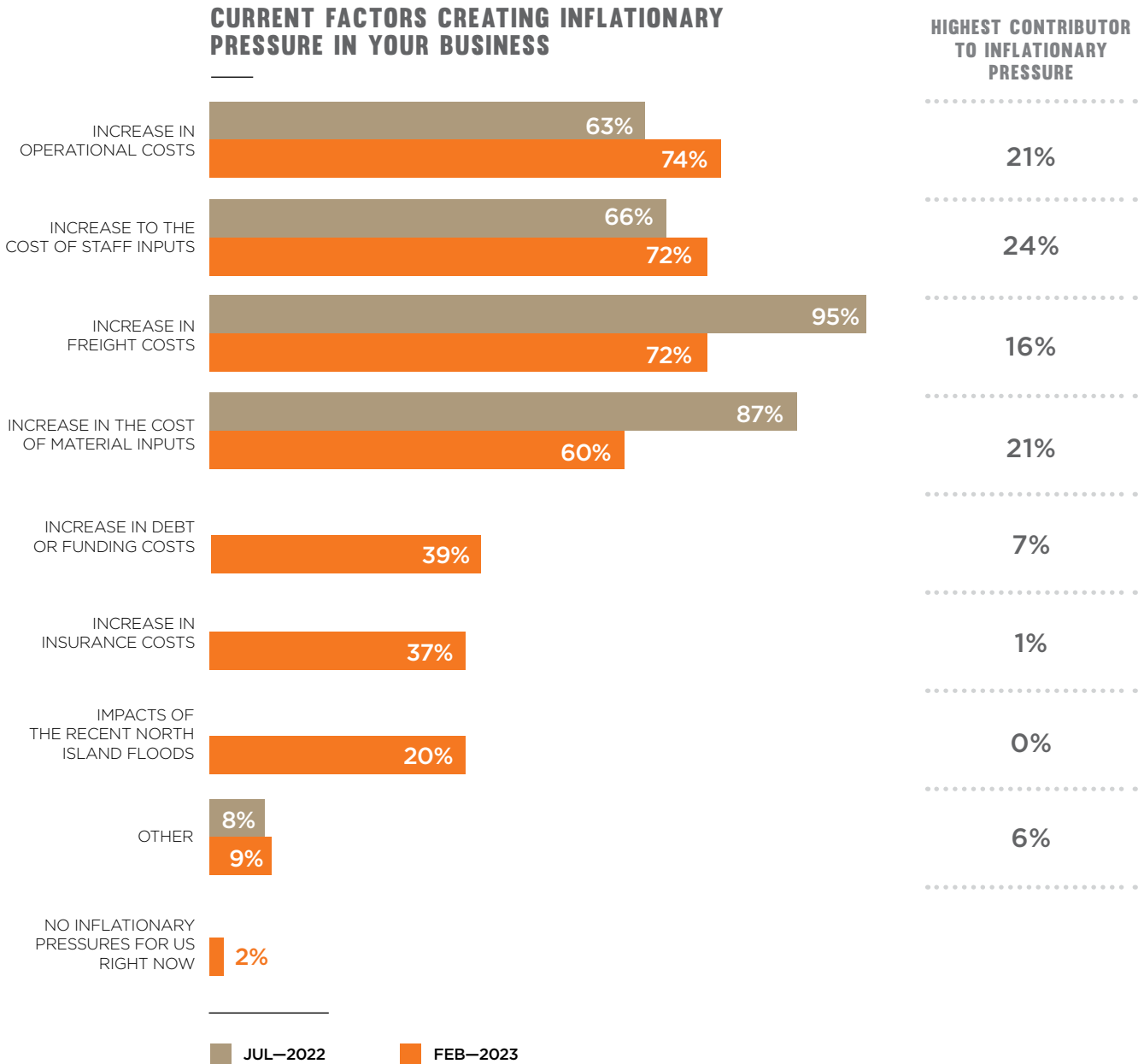
THE LAST TWO YEARS SHOW SHRINKING MARGINS

COMPOUND PRICE GROWTH FEB 2021 TO FEB 2023

Over the last two years building products sold in NZ increased an average of 45%. Over the same period the buy-in costs of these products increased by 79% on average. N.B. The cost increases do not cover staff and overhead costs which are the two highest inflationary factors.



LOCAL FACTORS ARE BUILDING UP PRICING PRESSURE

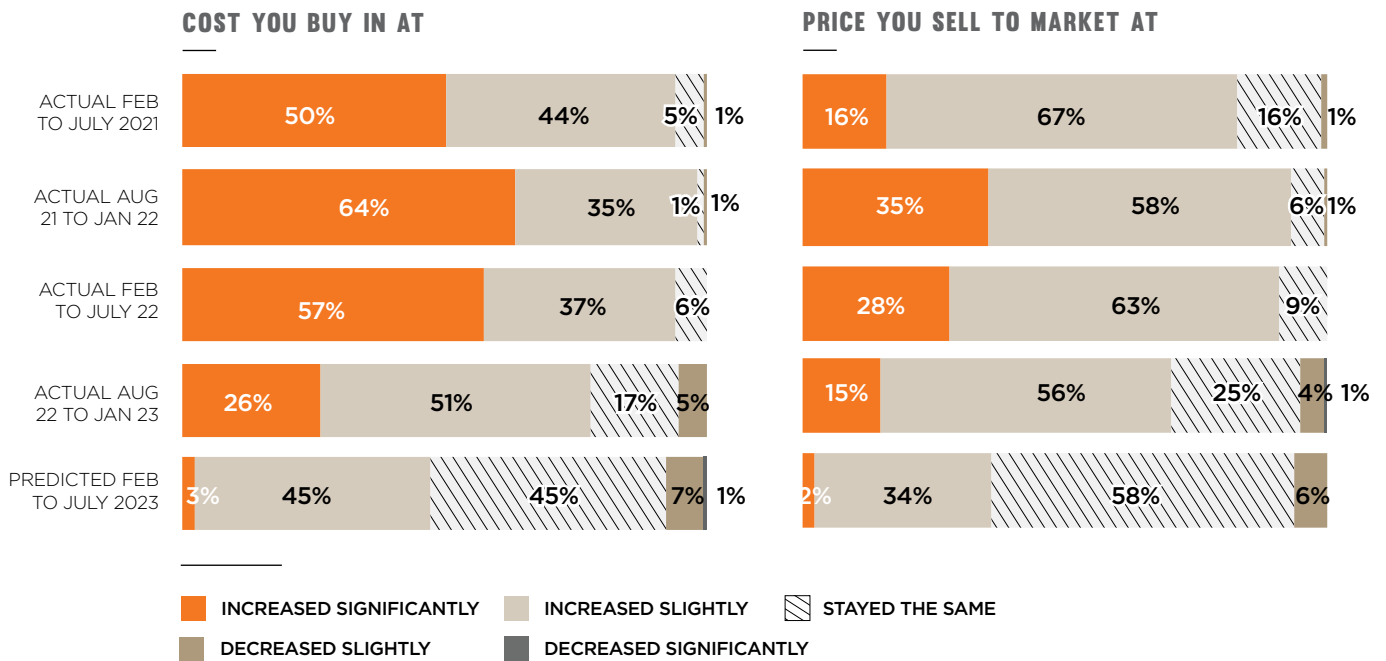


While freight costs and input costs have reduced, more businesses are feeling the pinch of operational costs and staff inputs. Added to that, one in five are feeling the impacts from the recent North Island weather events.

Businesses have responded to inflationary pressures by focussing on sales and marketing, delaying expenditure, and decreasing costs. The reaction has differed depending on business revenue. Lower revenue businesses are more likely to push sales and marketing, and to lower their headcount. By contrast businesses with \$10m-\$29m are more likely than others to enter new markets or categories.

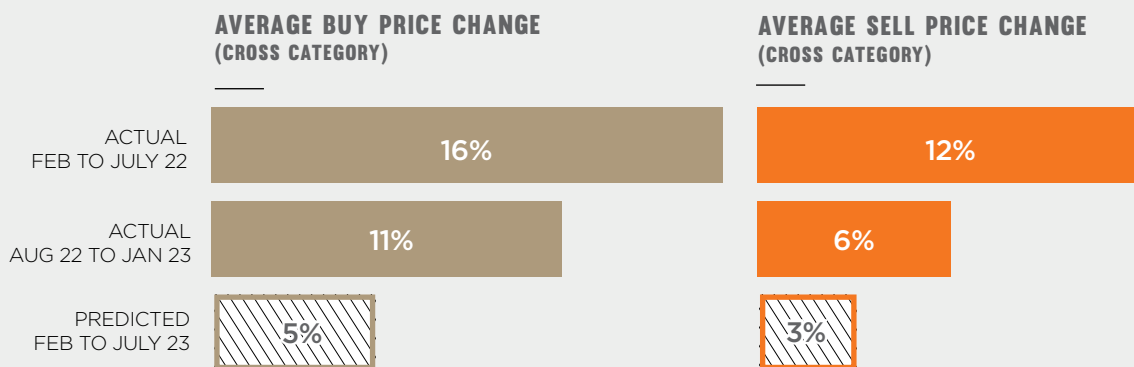
50% OF SUPPLIERS EXPECT COSTS TO STABILISE

The average increase to sell prices has halved to 6% over the last six months, across all categories combined. In addition, we see over 50% of suppliers expecting the next six months to bring stable or decreased buy-in costs.



THE AVERAGE PRICE INCREASE IS ON A DOWNWARD TRAJECTORY

The average increase to sell prices has halved over the last six months across all categories combined, now sitting at 6%. In fact, one in 12 suppliers have decreased sell prices over the last six months.



6% OF SUPPLIERS SAW A DECREASE IN BUY-IN COST AUG 22-JAN 23

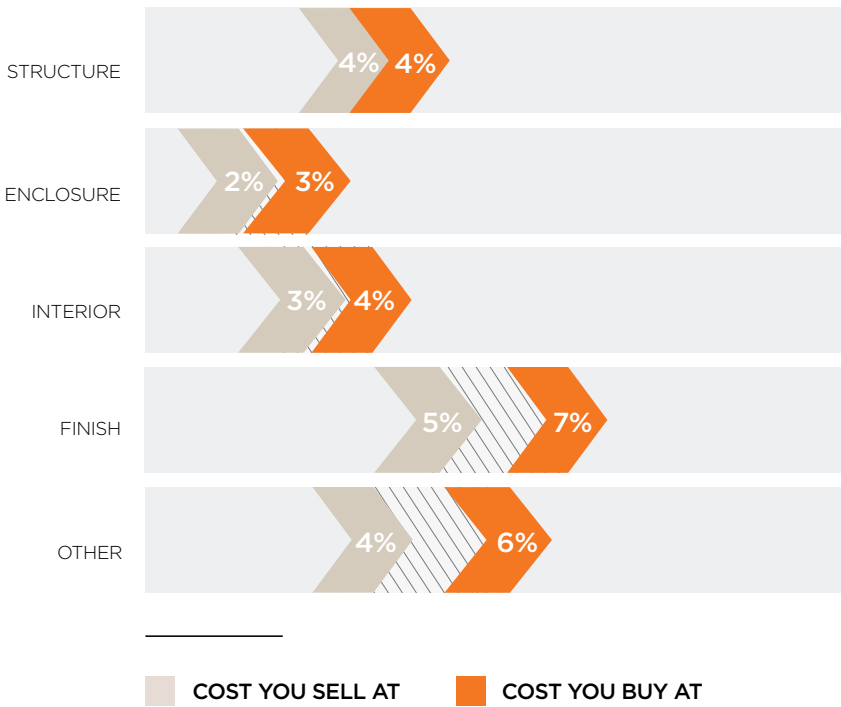
15% OF SUPPLIERS PREDICT A DECREASE IN BUY-IN COST FEB-JUL 23

8% OF SUPPLIERS SAW A DECREASE IN SELL PRICE AUG 22-JAN 23

11% OF SUPPLIERS PREDICT A DECREASE IN SELL PRICE FEB-JUL 23

CLADDING AND ROOFING LEAD PRICE STABILISATION

PREDICTED AUG 22 TO JAN 23



5%

IS THE AVERAGE INCREASE TO THE COST OF MATERIALS TO SUPPLIERS (SUPPLIER BUY-IN COST)

3%

IS THE AVERAGE INCREASE TO CUSTOMERS (SUPPLIER SELL PRICE)

“We are starting to see evidence of lower import freight costs and some supplier decreases and hope these will be enough to cover additional staff and electricity costs.”

DEMAND LIKELY TO INFLUENCE SHORT TERM PRICING

Just three in ten suppliers have passed on all cost increases to date. A similar proportion still have historical increases to be passed on, while 35% say they are going to absorb historical increases.

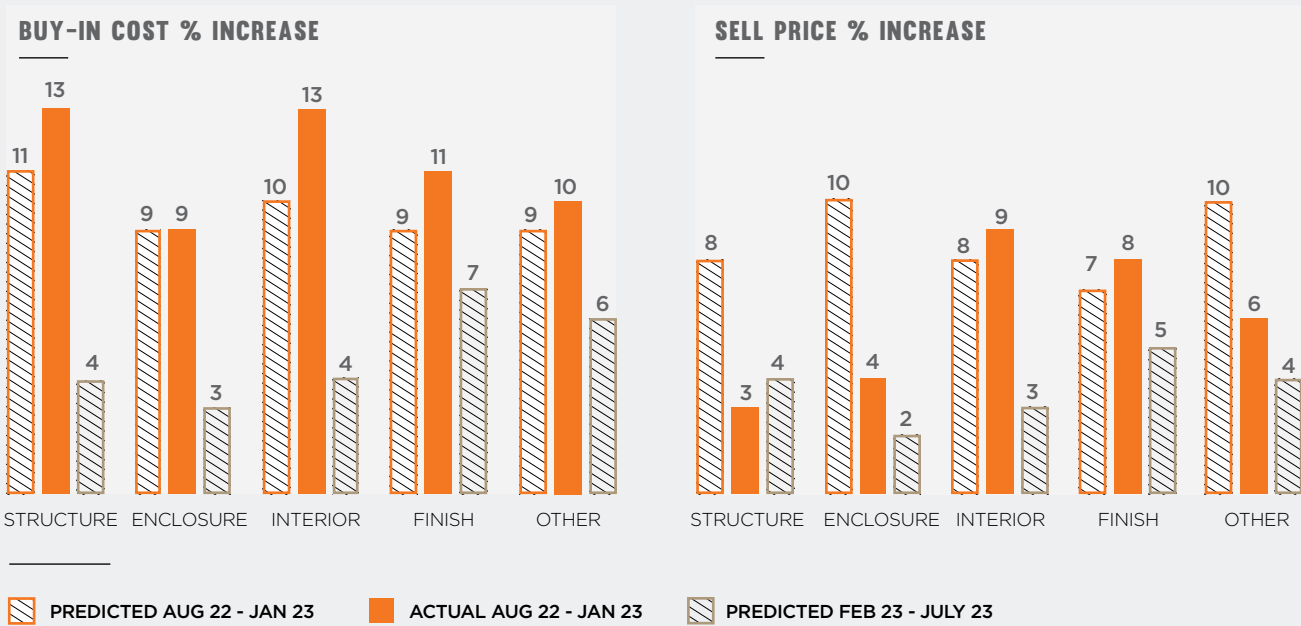
What this means is that even if buy prices stabilise, sell prices are likely to continue to increase for a while longer. This also raises concern for the near term sustainability of some suppliers. Over the last two years, EBOSS report data suggests margin shortfalls, with repeated price increases that have not been fully passed on. Ultimately local demand will dictate this — if demand falls suppliers may be forced to meet the market at reduced pricing.

WHICH OF THE FOLLOWING BEST DESCRIBES YOUR POSITION AROUND COST INCREASES?



HOWEVER, SUPPLIERS HAVE BEEN POOR AT JUDGING FUTURE PRICE CHANGES

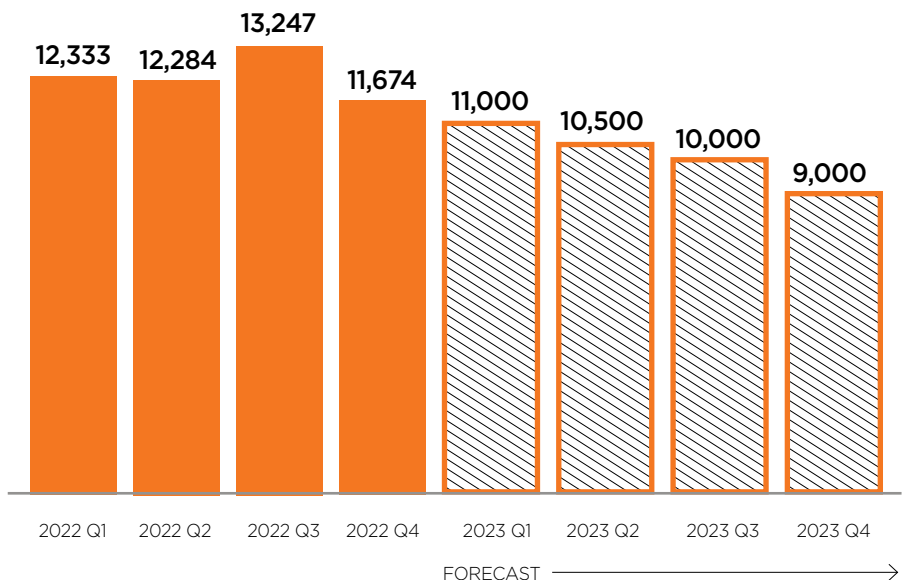
Historically suppliers have underestimated price increases which leaves them in a position where they are forced to continue to increase prices, even when their cost prices are stable or decreasing.



NEW DWELLING CONSENTS – NO CLIFF IN SIGHT AS MANY ARE EXPECTING

The latest BRANZ forecasts continue to show residential consents for new builds falling over the remaining quarters of 2023 after the record numbers seen last year. However, the expected 32% drop from the record number of 13,000+ consents in Q3 has eased to 24% for Q3 23. BRANZ forecasts estimate ~40,000 residential consents for 2023.

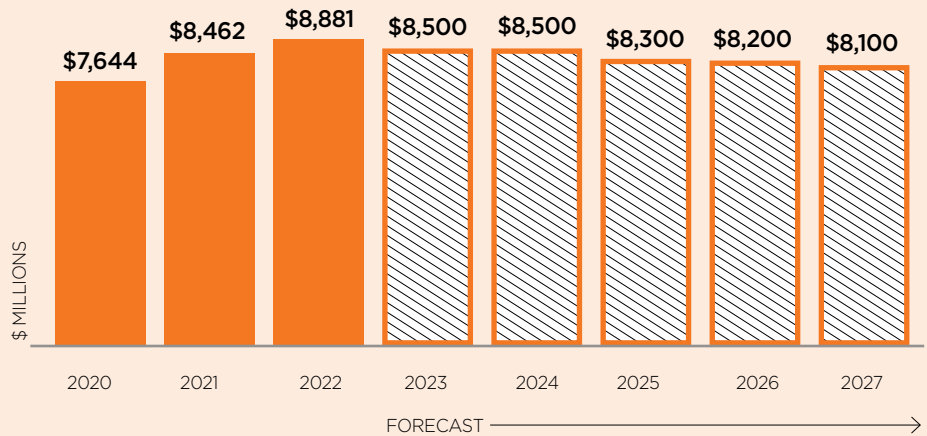
BRANZ QUARTERLY RESIDENTIAL DWELLING CONSENTS FORECAST



COMMERCIAL WORK SET TO CONTINUE AT NEAR RECORD LEVELS

Thanks to a strong pipeline of education and health work from the government, commercial construction forecasts remain healthy. Industrial activity currently represents approximately 30% of construction consent value in a continued response to bolstering domestic production and storage capacity.

BRANZ ANNUAL COMMERCIAL CONSENT VALUE FORECAST

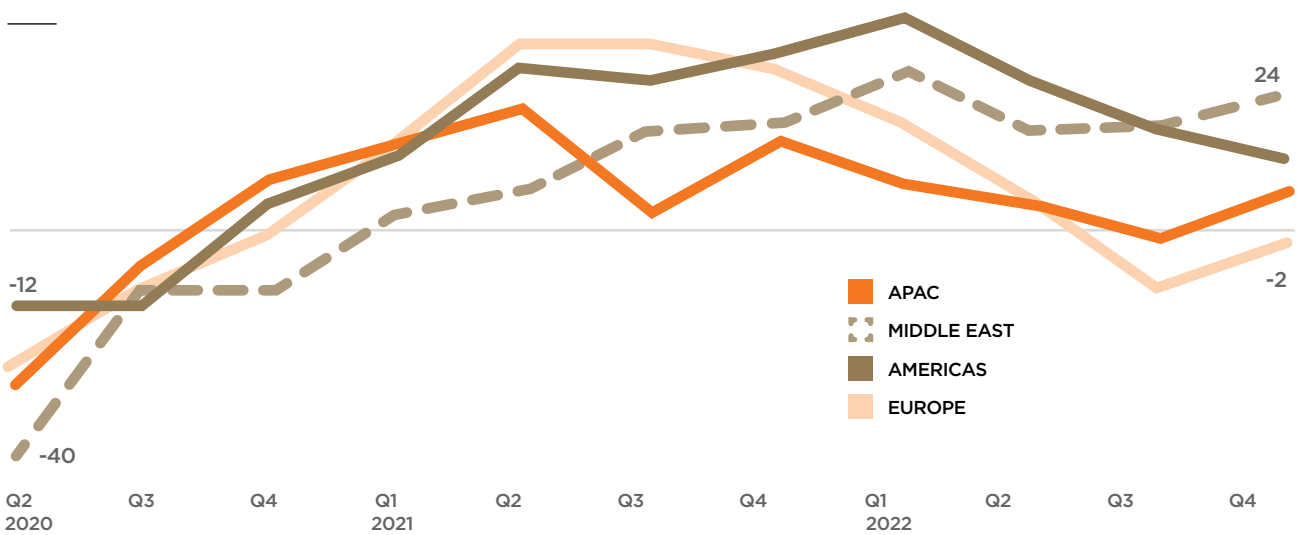


GLOBAL PERSPECTIVES ON CURRENT AND EXPECTED CONSTRUCTION ACTIVITY

In Q4, the RICS Global Construction Activity Index (CAI) saw global sentiment improve slightly from +3 to +8, driven by a strengthening outlook in the infrastructure sector.

However, this masks a clear trend globally of a fall in residential construction where global sentiment has fallen from +20 to -16 over 2022, driven primarily by Europe and the USA. A decrease in residential and commercial construction globally should result in growing product availability and more competitive pricing from international manufacturers.

CONSTRUCTION ACTIVITY INDEX BY REGION



SOURCE: RICS GLOBAL CONSTRUCTION MONITOR Q4 2022

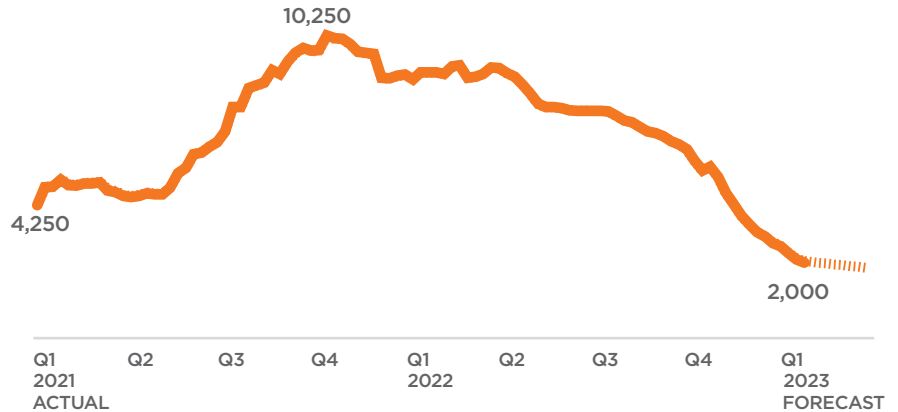
GLOBAL FREIGHT FORECAST TO EASE WITH GROWING CAPACITY

CURRENT OUTLOOK

The US\$ spot rates for 40-ft containers, referenced in the World Container Index, fell in Q1 2023 and are forecast to ease further.

With China continuing to emerge from Covid restrictions, there was no usual pre-Chinese New Year rush and in fact many carriers implemented 'blank voyages' in January — a term used when a shipping line skips a port or an entire voyage of a scheduled sailing route.

WORLD CONTAINER INDEX (WCI)³⁾



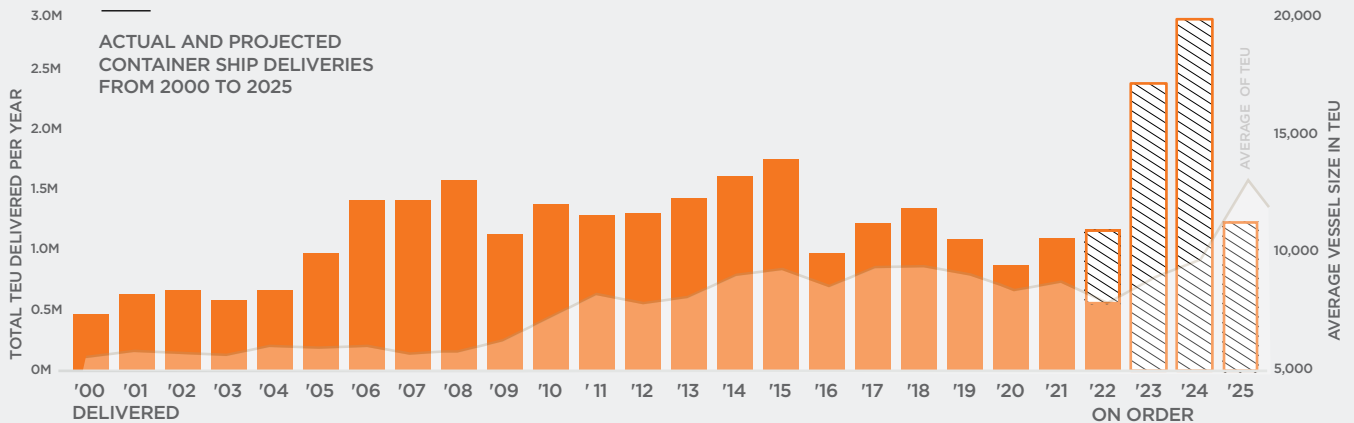
SOURCE: DHL OFR MARKET UPDATE JAN '23

THE FORECAST

Demand is expected to continue to soften globally with availability improving and delivery reliability surpassing '20 and '21 levels.

Global shipping capacity is set to increase by a third over the next 3 years, largely bolstered by significantly larger and more fuel efficient ships. As a comparison, in 2021 there was just one vessel able to carry over 24,000 containers. At the end of this year that will grow to 56. The impact of these giant “Megamax” vessels hitting the seas is twofold: global supply will quickly outstrip demand and it’s good news for lowering the carbon measurement of imported building products.

GLOBAL SHIPPING CAPACITY



SOURCE: DHL OFR MARKET UPDATE JAN '23

IN SUMMARY, HOW ARE SUPPLIERS RESPONDING TO A CHANGING MARKET?

THERE IS CONCERN FOR REVENUE OF THE FUTURE, AND A PUSH FOR MARKET SHARE:

“We believe the market is cooling — many have had projects shelved. Unless we can gain market share our business will decrease in revenue.”

“Suppliers will have a lot more stock on hand than anticipated, making the market more competitive.”

SOME ARE LOOKING TO STRONG PERFORMING CONSTRUCTION CATEGORIES AND MORE NICHE MARKETS TO MAINTAIN DEMAND:

“Currently NZ commercial construction remains strong and our ability to grow share is helping us deliver solid business results.”

“Increased competition due to a smaller pie will require re-imagining product offers & penetration into peripheral markets.”

OTHERS ARE LOOKING TO NEW OPERATING MODELS AND OFFERS TO MAINTAIN MARGIN:

“We are looking at selling direct to market to better control the end price.”

“We are actively pursuing new markets in Australia.”

SOME SIMPLY SEE THIS AS THE NORMAL CYCLE OF THE MARKET — THAT THINGS WILL BOUNCE BACK (ESPECIALLY WITH THE IMPACTS OF RECENT WEATHER EVENTS):

“We expect the pipeline will shorten, but recover before it fully empties. There will be a cull of poor/weak players.”

“The market will diminish for a period though this is cyclical which has not happened for a longer than normal period.”

APPENDIX

The categories are described as:

Structure: Aluminium, Composite Panels for Floors and Walls, Concrete, Fasteners and Connectors, Masonry, Plastics, Site Safety and Roof Access Equipment, Stainless Steel, Steel, Structural Systems, Structural Timber

Enclosure: Awnings and Canopies, Enclosure Adhesives, Sealants and Fasteners, Enclosure Balustrades and Stairs, Exterior Decorative Items, Flashings and Expansion Joints, Glazing, Insulation, Roofing and Decking, Tanking and Pre-Cladding, Wall Cladding, Windows, and Doors

Interior: Ceiling Systems, Floors, Furniture, Hardware, Joinery Fixtures and Appliances, Partitions and Interior Doors, Signs and Features, Wall, and Ceiling Linings

Finish: Applied Coatings, Carpeting, Flooring Ancillaries, Flooring Underlays, Overlay Flooring and Wall Panels, Painting, Decoration and Coating, Resilient Surfacing, Tiling

External: Engineering Works, External Heating, Landscaping, Roads and Paving, Stretched Fabric Systems

Other: Services, Central Vacuum Systems, Communications and Controls, Fire Safety, Heating and Cooling, Lighting and Electrical, Plumbing and Drainage, Sanitaryware, Tapware, Transport, Ventilation and Air Conditioning

ABOUT EBOSS

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Note: The ratings in some of the stacked bar charts may not add to 100%. This is due to rounding.