



Market Pulse



The Construction Margin Squeeze: Productivity Declines and Escalating Cost Pressures

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Productivity Declines and Escalating Cost Pressures



The construction industry faces a critical dilemma as escalating cost inflation and flatlining productivity threaten to squeeze industry margins and suppress demand. While the industry successfully passed through the increased material and labour costs over the 2023 to 2025 period, the continued increase in costs and declining labour productivity may compress its ability to continue this strategy. Data from Equifax highlights that the recent improvement in corporate profitability may be under immediate threat from structural bottlenecks and geopolitical developments.

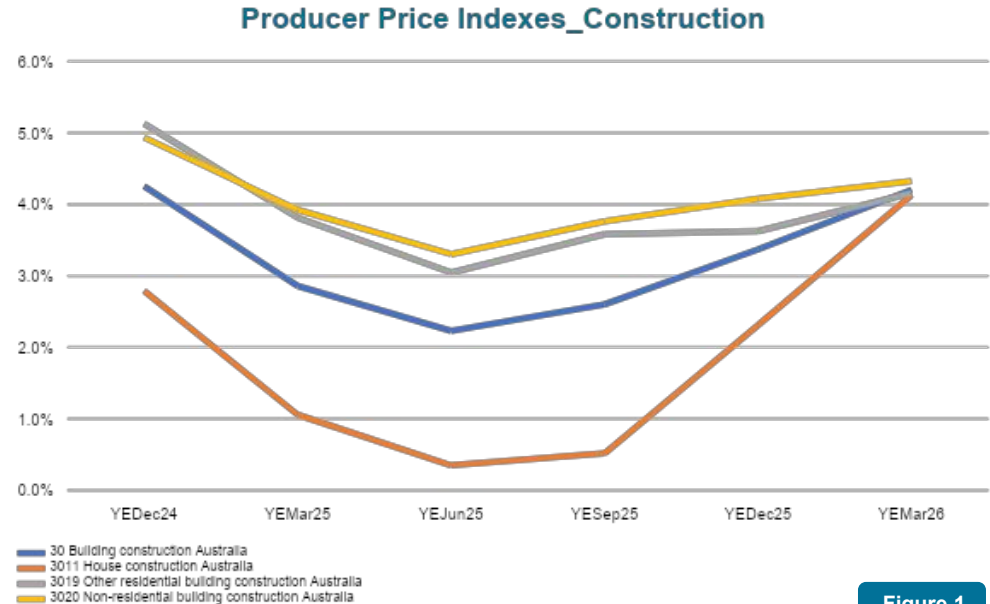
Driven by these macro trends, a sharp contrast has emerged between specific sectors within the industry. The private residential and high-rise commercial sectors are facing the most acute cost increases and margin pressures, whereas the civil engineering, utilities, and data centre sectors remain buoyed by robust government funding and targeted institutional capital. Balancing the tight constraints of the current economic environment, the industry must now navigate localised capacity constraints alongside global structural shifts. Further challenges are likely to eventuate as long-term post war reconstruction in Europe and the Middle East may heavily divert global tier one contractor capacity and potentially trigger severe international competition for raw materials.

Cost inflation and weak productivity are squeezing construction margins.

Escalating Producer Prices and Hidden Inflationary Pressures



Australian Bureau of Statistics data reported in figure 1 shows a 4.2% annual increase in the Producer Price Indexes for the year ended 31 March 2026 for building construction in Australia. Although this is not as high as the double-digit levels experienced during the pandemic period between March 2022 and December 2022, it represents a significant acceleration from the 2.2% annual increase recorded for the year ended June 2025. More concerning is that this price acceleration is highly likely to expand in the June 2026 quarter. The national statistical agency noted in its March 2026 release that the closure of the Strait of Hormuz had not yet affected prices in the construction industry due to the timing of pricing collections occurring prior to the beginning of the conflict on 28 February 2026.



Australian Bureau of Statistics (March 2026), Producer Price Indexes, Australia, ABS Website



Escalating Producer Prices and Hidden Inflationary Pressures

Connecting these macro blockages directly to local sectors, there is a steep yearly cost increase in the house construction sector to 4.1% for the year ended March 2026, which contrasts with the 1.1% recorded in the year ended March 2025 and the 0.3% seen in the year ended June 2025. Consumer housing inflation was notably higher at 6.2% as reported in the Consumer Price Index for housing, given that the consumer metric includes additional operational variables such as market rents and new dwelling purchases by owner-occupiers. The broader Producer Price Indexes for construction encompass the final output charged by builders, factoring in materials, labour, administration, and regulatory costs alongside profit margins. This escalating cost inflation over the year ended March 2026 has been heavily impacted by concurrent spikes in material prices and structural labour shortages.

4.2% Annual increase in building construction costs (March 2026).

4.1% Annual rise in house construction costs, up from 1.1% a year earlier.

6.2% Consumer housing inflation in the year to March 2026.

Construction cost inflation nearly doubled from 2.2% (June 2025) to 4.2% (March 2026).

House construction cost growth increased more than 13-fold, from 0.3% (June 2025) to 4.1% (March 2026).



Escalating Producer Prices and Hidden Inflationary Pressures

The construction producer price index data reported in figure 2 explicitly underscores how input pain has intensified post June 2025, stripping away the temporary breathing room builders secured during the brief mid contract improvement periods. Driven by this acceleration, the year ended weighted average materials cost across the six capital cities reveals an aggregate increase of 2.5% for the year ended March 2026, a compounding jump from the 1.1% and 1.3% increments seen in the preceding two twelve-month intervals. Within this weighted capital city basket, the steepest escalations have concentrated in electrical equipment due to surging global copper prices, installed gas and electrical appliances, timber board, joinery, and energy intensive cement products. The flow through effect of the closure of trade routes and increased domestic energy bills is expected to show a more pronounced impact on the overall materials price index in the June 2026 quarter.

PPI: Year Ended-Weighted Average of 6 Capital Cities

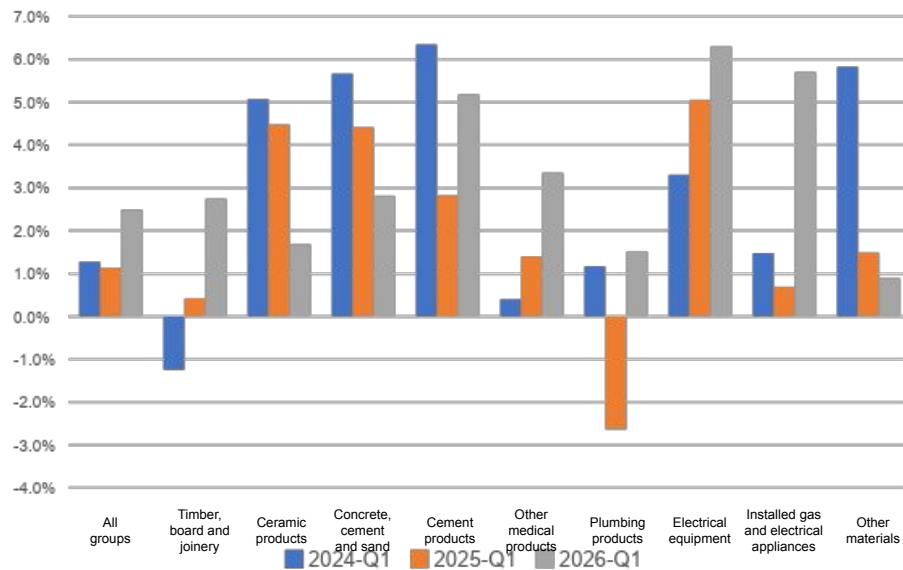


Figure 2

Australian Bureau of Statistics (March 2026), Producer Price Indexes, Australia, ABS Website

The Productivity Logjam and Labour Market Asymmetry



Australian Bureau of Statistics wage data shows that the annual percentage increase to December 2025 in the hourly rate of pay, excluding bonuses, for the construction industry was 3.5%. A major structural concern in the construction industry is poor labour productivity occurring in conjunction with continued pressure for wage increments, a trend exacerbated by a severe shortage of skilled labour. Official labour data states that there were 21,600 job vacancies in the construction industry in February 2026, representing a sharp increase from the 18,100 vacancies reported in November 2025.

The construction value per employee per quarter data shown in figure 3 reveals that there has been no tangible improvement in labour productivity for the year ended December 2025. The real value per employee stood flat at \$243,175, compared to \$243,222 for the year ended December 2024 and \$236,333 in for the year ended December 2023, representing nil net increase over the past twelve months. This stagnation follows a 2.9% increase for the year ended December 2024 and a 12.6% increase for the year ended December 2023. The sizeable positive correction recorded for the year ended December 2023 reflected the immediate exit from the pandemic, where the total workforce downsized by 140k to 1.26 million employees and the total value of work done increased by \$25.5bn to \$299 billion as materials were released from opening supply chains.

3.5% annual increase in construction wages (December 2025).

21,600 construction job vacancies in February 2026, up from 18,100 in November 2025.

\$243,175 value of construction per employee, virtually unchanged from \$243,222 a year earlier.

0% labour productivity growth over the year to December 2025.

12.6% productivity rebound in 2023 has stalled, with no growth in 2025.



The Productivity Logjam and Labour Market Asymmetry

Value per employee: quarterly versus. Annual Trends (2022 to 2025)

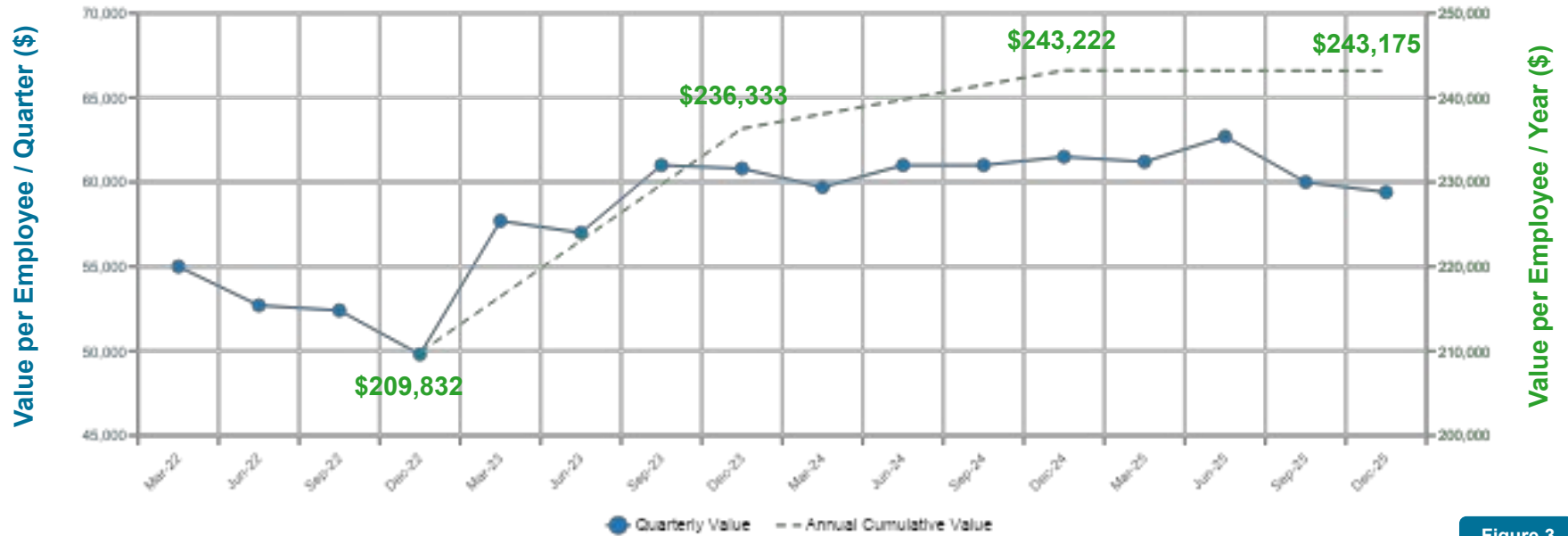


Figure 3

Australian Bureau of Statistics, Construction Work Done, Australia (Seasonally adjusted chain volume measures and Labor account, Australia)

Divergent Trends and the Mechanics of the Margin Squeeze



Deeper insights emerge when analysing the percentage change in construction value alongside total employee numbers per quarter shown in figure 4. The respective trend lines are in reverse order of what is commercially desirable. The percentage change in the total number of employees is flat, while the actual dollar value of work completed is trending downwards, with the clear crossover point occurring in the mid to later part of 2025. When these lines converge, it signals an operational margin squeeze.

It indicates the hours the industry is paying for are producing less physical volume of construction assets.

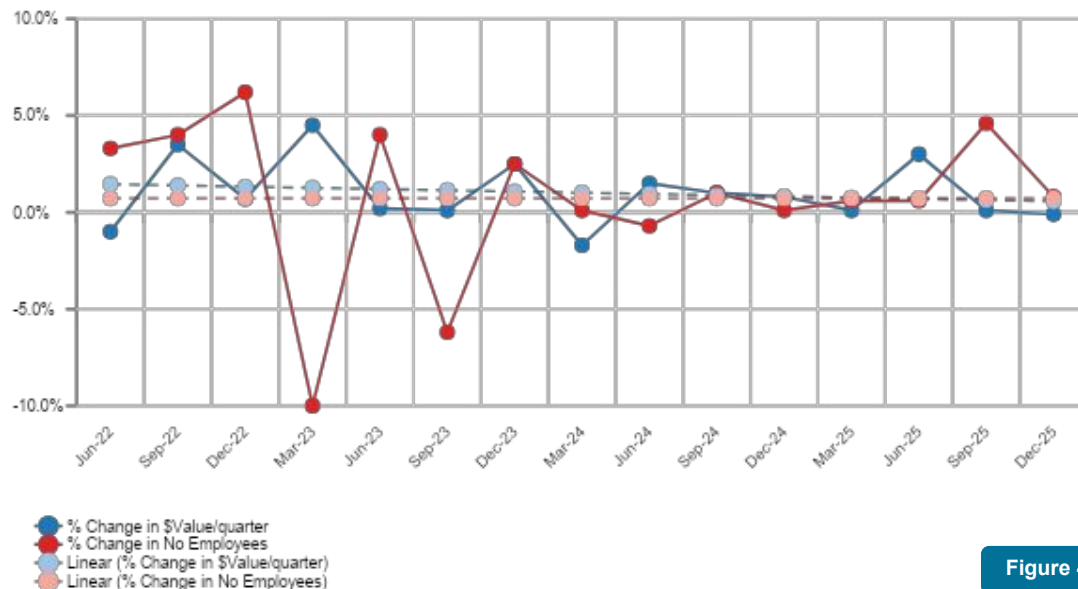


Figure 4

Australian Bureau of Statistics, Construction Work Done, Australia
(Seasonally adjusted chain volume measures and Labor account, Australia)



Divergent Trends and the Mechanics of the Margin Squeeze

There are notable anomalies within this timeline, such as the March 2023 quarter, where the industry successfully transitioned from a labour hoarding phase to an execution phase. This resulted in a 4.5% productivity spike as 140,000 headcount positions were shed while productivity was supported by major civil engineering projects hitting full operational speed. Conversely, the September 2025 and December 2025 quarters experienced an efficiency decline. Labour counts increased consecutively from 1.27 million in June 2025 to 1.34 million in September 2025 and 1.35 million in December 2025, representing quarterly gains of 4.6% and 0.8% respectively, but the actual value of work done flattened or contracted by 0.1% in the December 2025 quarter (Sep-25 Qtr: 0.1%). This divergence signals that the industry is becoming structurally less profitable, highlighting the need for rigorous due diligence when engaging commercial counterparties.

4.5% productivity spike in March 2023 quarter following a **140,000** reduction in workforce.

1.35 million construction workers by December 2025, up from **1.27 million** six months earlier.

4.6% workforce growth in September 2025 quarter outpaced project output.

0.1% decline in construction output despite rising labour numbers.

More workers, less output signals declining industry productivity and profitability.

Corporate Profitability and Future Forecast Risks

While construction companies managed to cover these high costs for the three years to June 2025, existing challenges are escalating and could negatively impact future corporate profitability. Entities in the construction industry modified their risk pricing post pandemic, adopting an approach akin to the old adage of once bitten, twice shy. The industry incorporated higher initial margins and cost variation clauses, which led to a temporary improvement in net profit margins from the year ended June 2023 to the year ended June 2025 as shown in the following table (Equifax data).

Industry Sector	YE Jun-23	YE Jun-24	YE Jun-25
Total Construction Industry	4.10%	5.50%	5.70%
Construction (Excl. Civil/Engineering)	3.30%	4.70%	4.90%

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..... Corporate Profitability and Future Forecast Risks

The underlying profitability shifts across the broader industry profile, as shown in the above table, saw average net profit margins improve from 4.1% in June 2023 up to 5.7% by June 2025, while the non-civil building sectors ticked upward from 3.3% to 4.9% over the same period. Based on this clear change in strategy from builders, customers have carried the financial burden of the higher cost environment. However, post June 2025, this pricing dynamic is likely to shift. The improvement in net profit margins slowed significantly in the year ended June 2025 compared to the prior year. Since June 2025, the construction Producer Price Indexes accelerated from 2.2% to 4.2%, reflecting high-cost increases that are likely to compress the net margin levels achievable in future contracts.

5.7% average industry net profit margin by June 2025, up from **4.1%** in 2023.

4.9% non-civil building margins, up from **3.3%** over two years.

Construction cost inflation doubled from **2.2%** to **4.2%** after June 2025.

Margin gains are slowing as accelerating costs outpace pricing power.

..... Corporate Profitability and Future Forecast Risks

Balancing these tight constraints, industry reports in the later part of 2025 forecast growth for the sector, though it remains at a moderate level of less than 3% and is heavily supported by high capital expenditure on data centres and government funded infrastructure projects. While road and rail megaprojects are hitting their expenditure peaks, utilities encompassing electricity generation, transmission grids, and renewables are surging. However, the high rise in the construction PPI post these forecasts may negatively dampen real output, particularly outside of data centres and public works.

At the same time, continued upward pressure on construction costs emanates from unresolved geopolitical conflicts, upward pressure on wages, and high job vacancies for skilled workers. The National Australia Bank Monthly Business Survey for April 2026 states that pressure on margins is increasing as purchase cost growth is more than one percentage point higher than output prices across all industries. In manufacturing and construction, this margin pressure is more extreme, with purchase cost growth 3.4 percentage points and 3.8 percentage points higher than price growth respectively. Business confidence rose five points to minus 24 index points in April, while business conditions fell three points, fully unwinding the gains seen over 2025 and signalling slower economic activity in coming quarters.

Industry forecasts point to moderate construction sector growth of less than 3%, driven primarily by data centre investment and government-funded infrastructure, while rising construction costs and margin pressures threaten broader real output and signal slower economic activity ahead.

Global Post-War Reconstruction and Long-Term Structural Shifts



Construction costs in the Australian and international markets are likely to take another substantial hit when the geopolitical conflicts in Ukraine, Russia, and the Middle East eventually transition to peace, with post war rectification expenditure estimated to be well into the hundreds of billions and potentially reaching one trillion dollars. Massive multilateral funding from the World Bank, the European Union, and the Gulf states will likely divert the world's largest tier one contractors, engineering firms, and project managers toward these massive international rebuilds. Although lower global freight insurance and shipping costs are likely to normalise, the global demand for raw material and specialised labour is likely to escalate dramatically.

While the short to medium term remains highly pressured, a longer-term silver lining exists for the Australian industry. Local contractors and developers are likely to benefit from the systemic innovations born out of the reconstruction rebuild, which will likely rely heavily on modular, prefabricated building components and advanced building information modelling to speed up delivery. This shift is poised to set a new global standard for rapid, sustainable disaster recovery construction, though for Australia, these technological efficiencies appear unlikely to materialise in the short term.

Presently, Australia has a high and increasing cost structure, emanating from a varied number of sources that continue to evolve and are expected to persist, creating headwinds for corporate order books and net margins.

Further Information

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