



Outlook for Construction

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January 2024



Agenda

Inflation may be calming but base rate remains stubbornly high.

Cost of borrowing directly impacts investment levels in construction, and output is therefore falling.

From stagflation to greedflation, inflation was a much-discussed topic in 2023. What are the prospects for 2024. **Is this the new normal?**

We'll examine current inflationary pressures in construction, looking at:

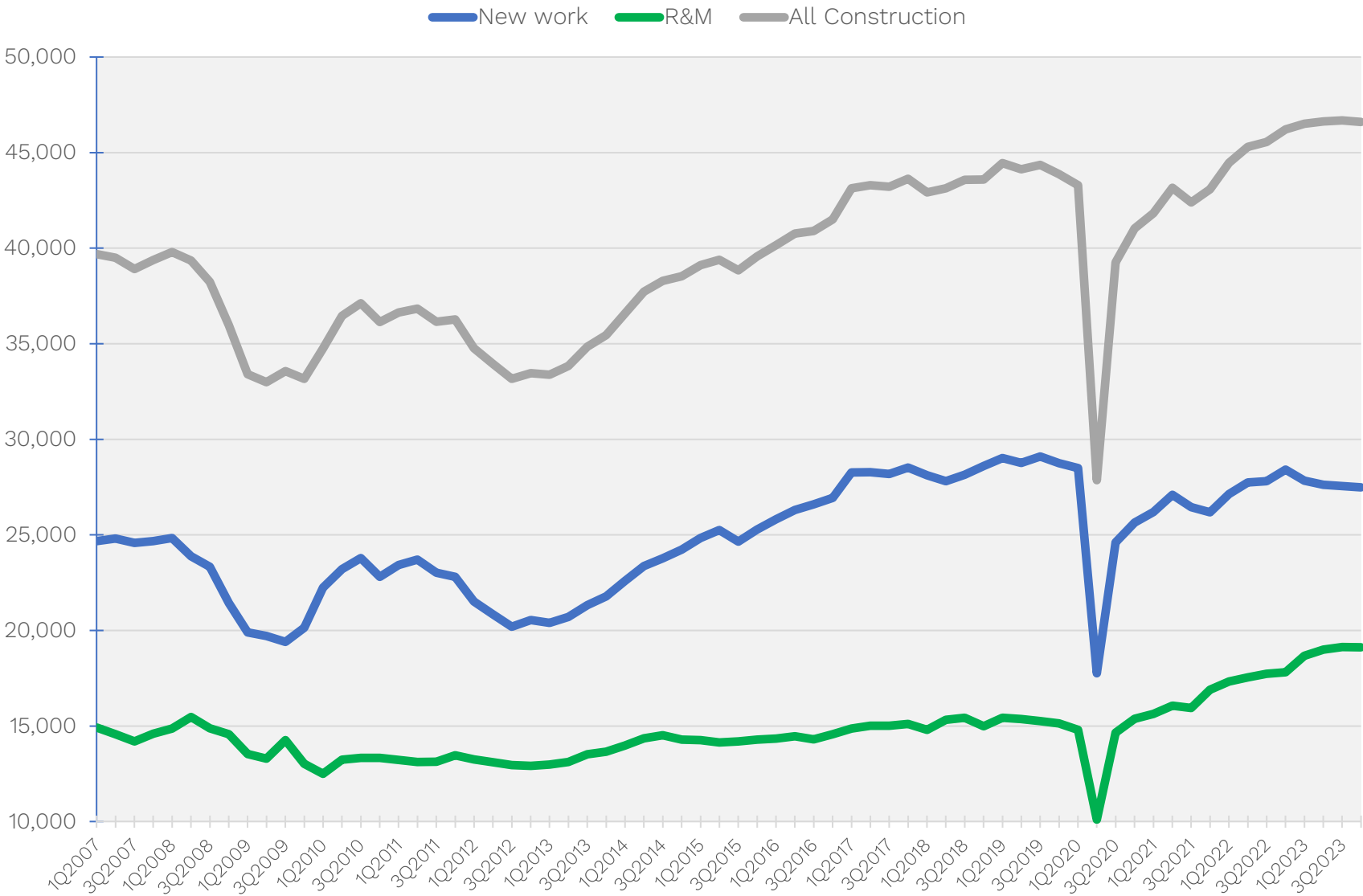
- ▶ Forecasts of future demand levels
- ▶ Cost and price movement in construction, including wages
- ▶ Draw some conclusions
- ▶ Questions

Setting the scene

- ▶ Lurching from one crisis to the next
- ▶ Election year (globally)
- ▶ Construction output stagnating
- ▶ Persistent low growth has become characteristic
- ▶ Volatility in materials prices calmed during 2023
- ▶ Labour became “topic” of the year
- ▶ Highly likely that construction currently in recession (although perhaps won't be reported in official data until later in the year)

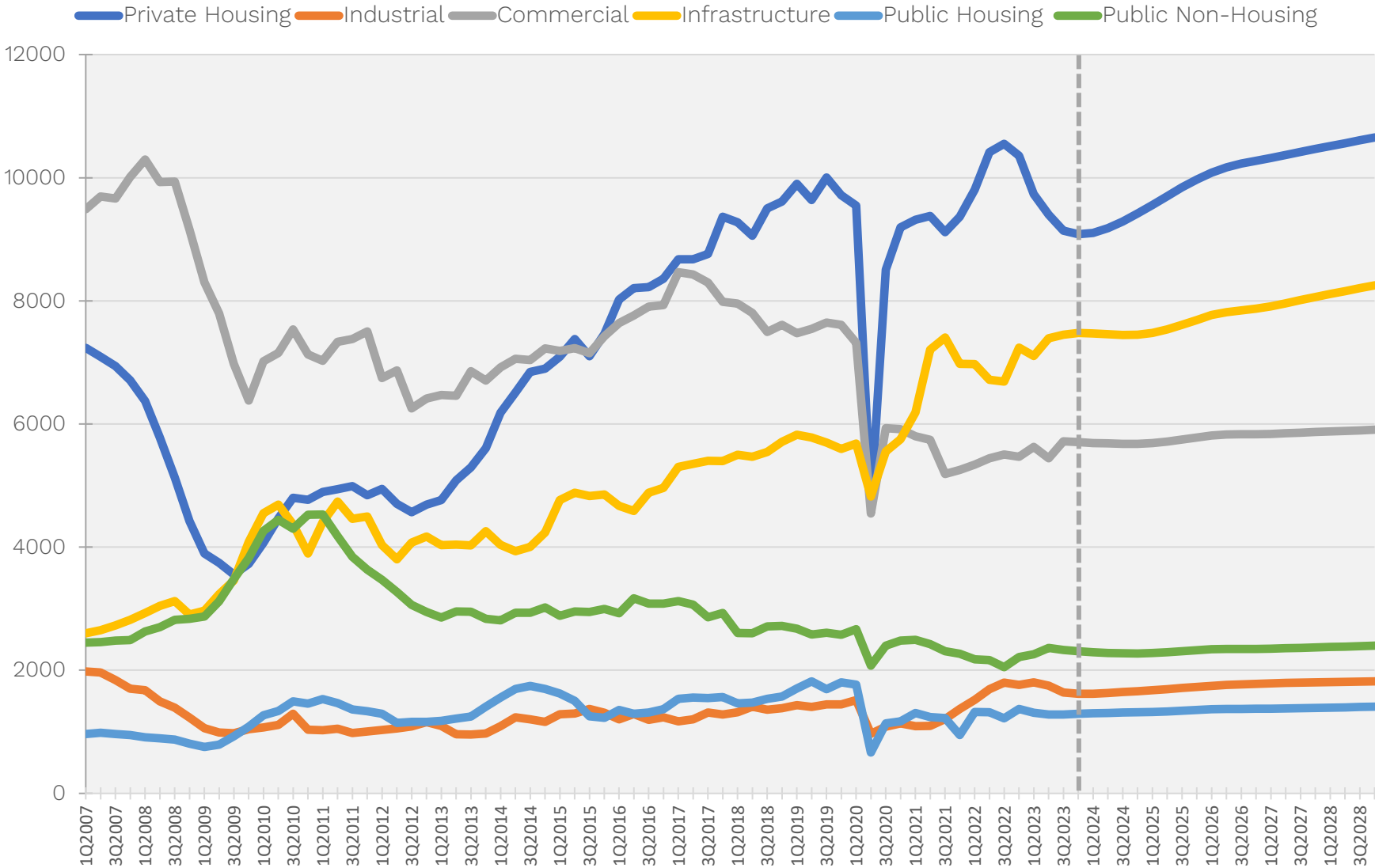
Inflationary drivers

Construction output (ONS: Quarterly volume, seasonally adjusted £m) **BCIS**[®]



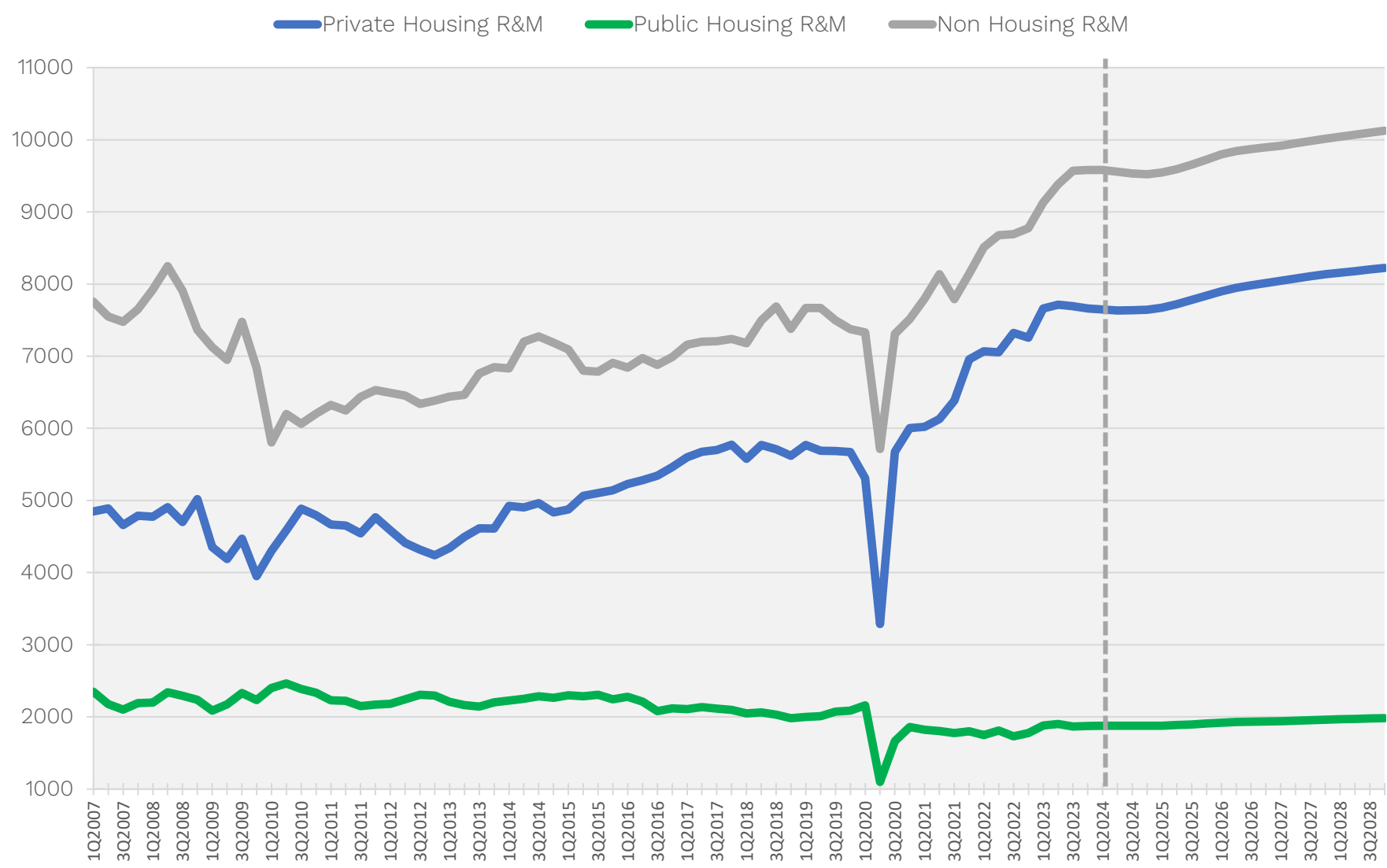
Total output remains above pre-crisis levels but growth is flatlining. New work growth has fallen over the last year. Following sustained growth, R&M sector has started to level out

Forecast for NEW construction output by sector (ONS/BCIS, 2024 £m) **BCIS[®]**



New work output expected to decline in 2024, primarily from decreasing output in housing. Subdued growth likely in infrastructure, while all other sectors stagnating

Forecast for R&M construction output by sector (ONS/BCIS, 2024 £m) **BCIS[®]**



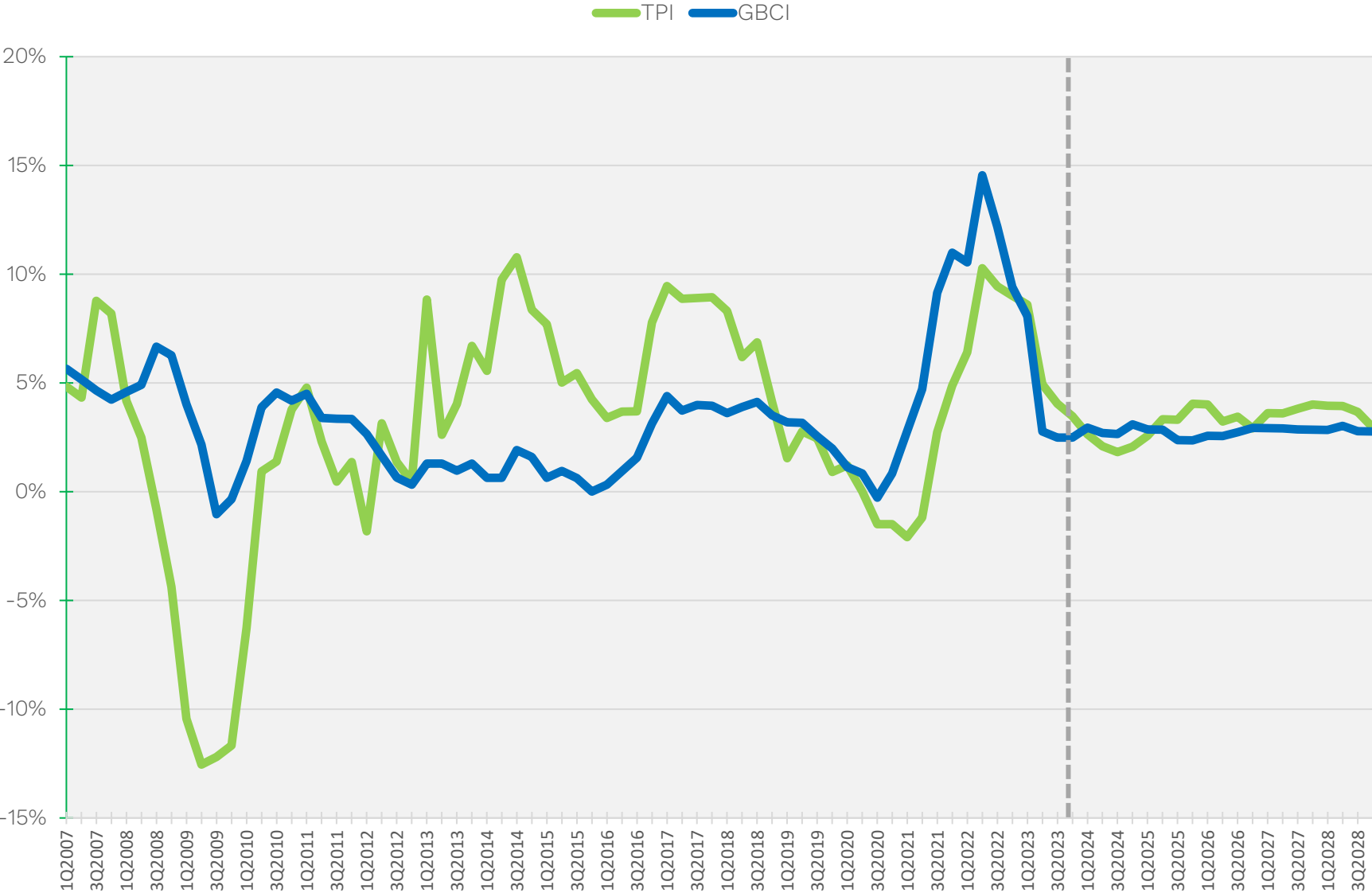
Repair and maintenance
output forecast to
plateau through 2024
before recovery in
2025, driven by growth
in public and
private housing R&M

Summary of growth predictions by sector using latest data

First time in a while
that this chart has only
one red. Have we
turned a corner?

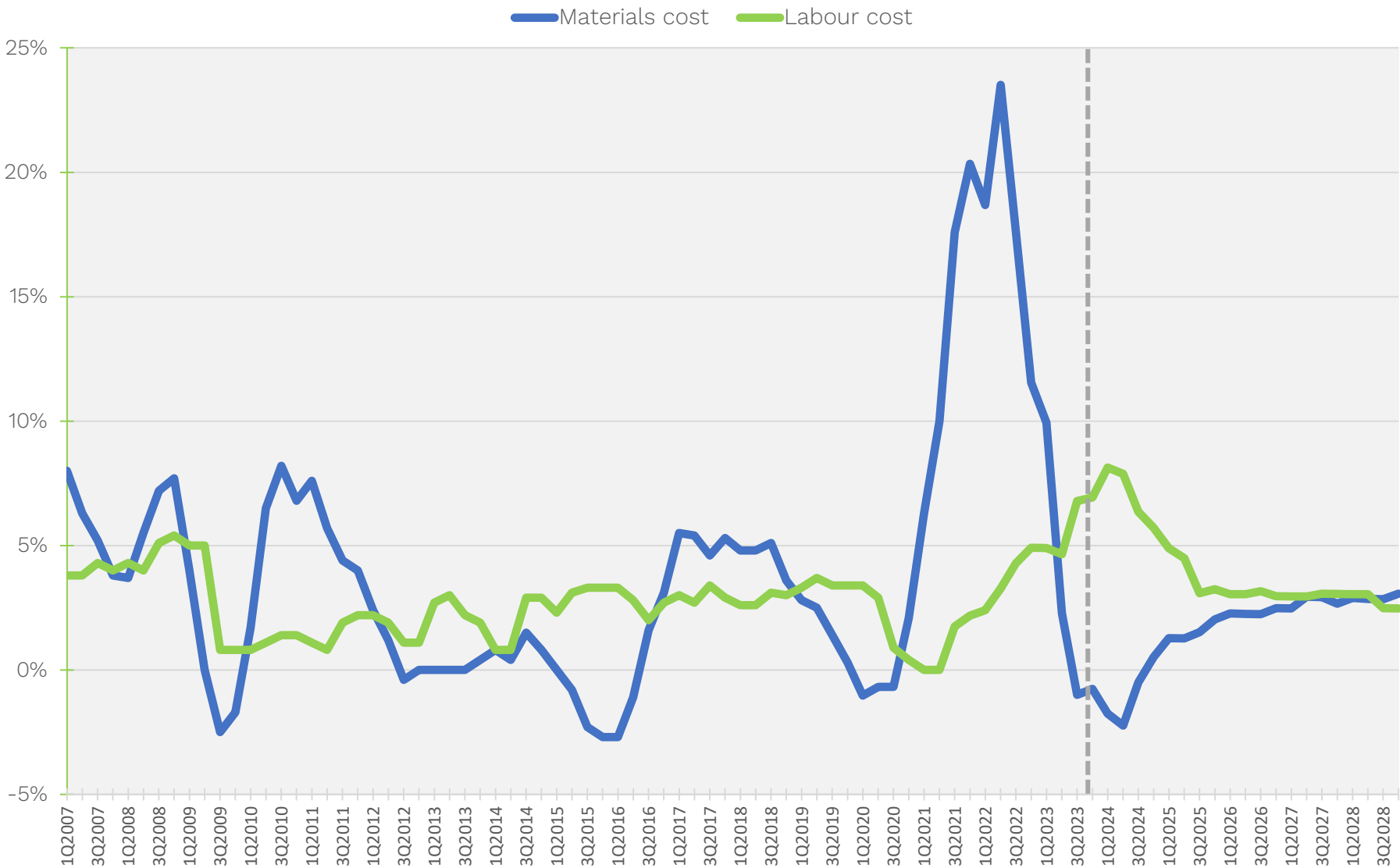


Growth in BCIS GBCI & TPI (BCIS 2024)



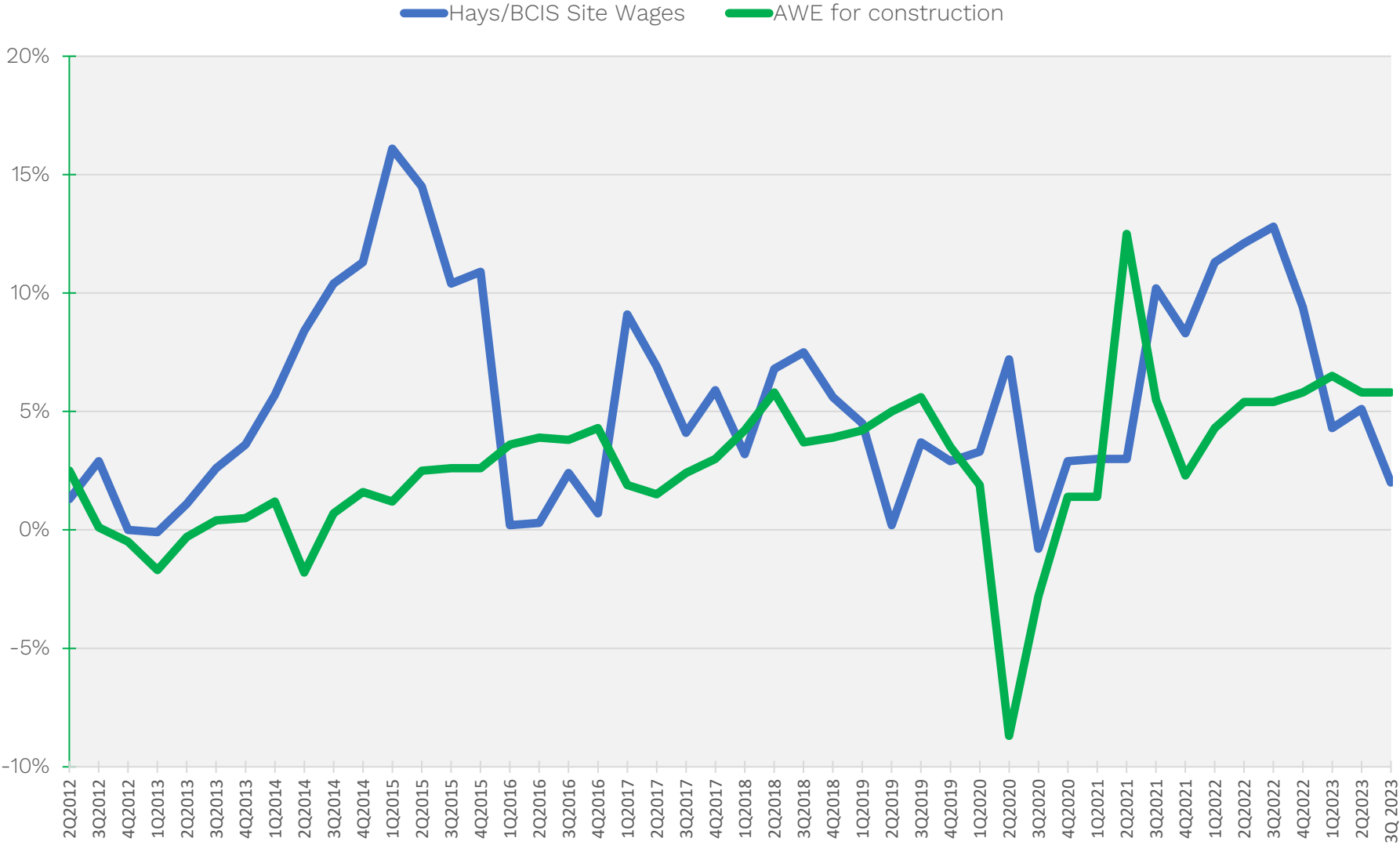
Forecasts relatively benign compared to recent past. Some evidence of minor uptick in TPI next year, while GBCI returns to some stability

Growth in BCIS materials & labour cost indices (BCIS 2024)



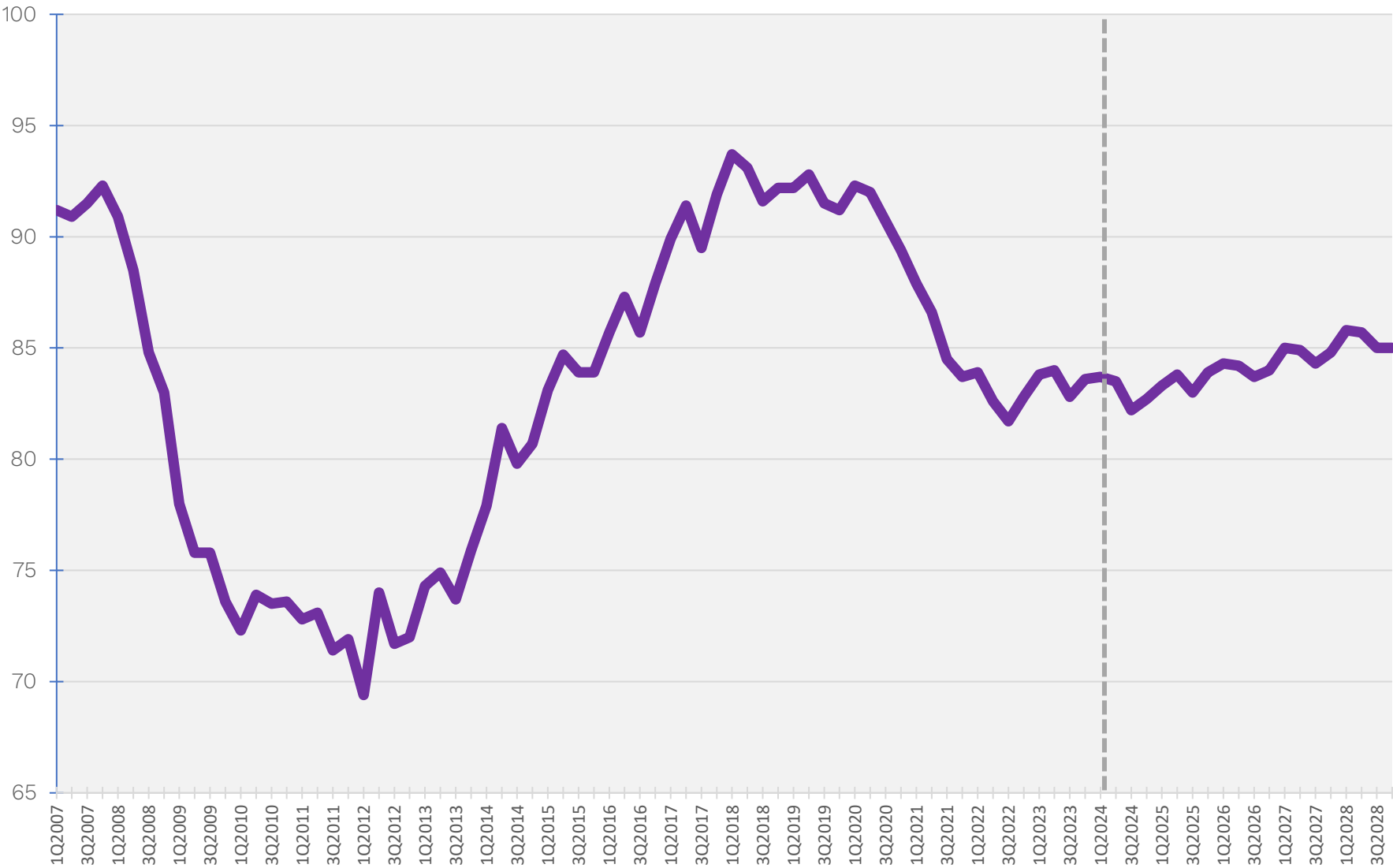
Labour costs overtaken materials costs as key cost driver, though growth much more subdued, peaking at 8% in 1Q2024 before returning to trend in 2025

Growth in construction earnings (BCIS/ONS, 2024)



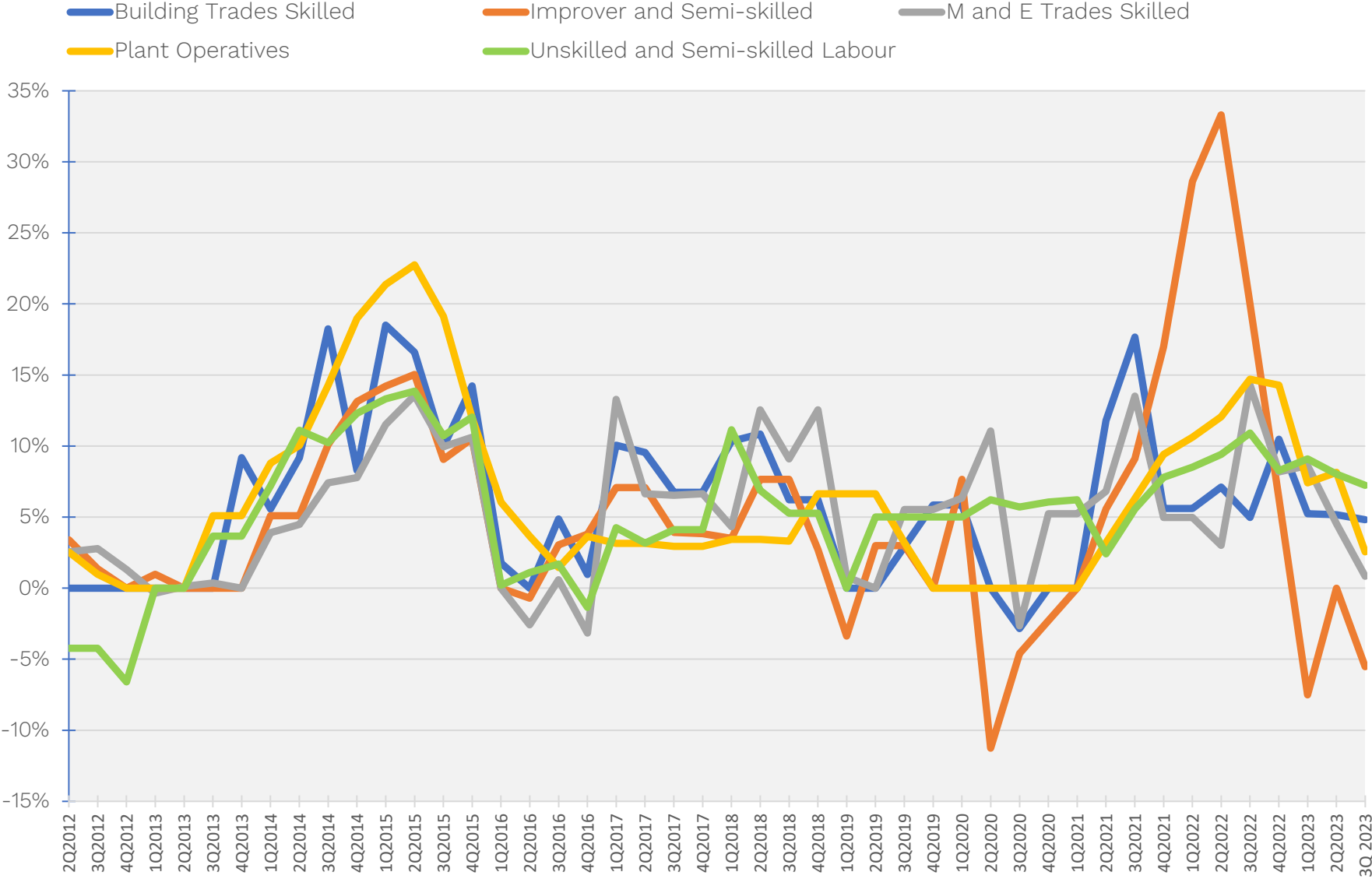
Declining trend in wage growth evident

Market conditions index (BCIS 2024)



MCI currently rising -
prices now rising
faster than costs

Growth in site wages (BCIS/Hays, 2024)



Average wage growth of around 5% across trades - reasonable given circumstances

BCIS Industry panel (View on the ground)

Procurement

- ▶ Contractors now more inclined to bid for simpler projects, aiming to mitigate cash flow problems. Significant risk premiums added for complex projects
- ▶ Greater appetite for larger projects due to slowdowns and pauses, but not manifesting in lower tender prices yet
- ▶ Risk and uncertainty still attracting significant premiums, but now being overridden by need for follow-on workload

Tender

- ▶ Contractors more selective on tender routes they are willing to work, preferably two-stage or target cost contracts
- ▶ Volatility still being priced into fixed price contracts
- ▶ Improvement in appetite for single stage, as necessity dictates, but contractors much prefer negotiated outcomes

BCIS Industry panel (View on the ground)

Packages

- ▶ Packages with increased costs - sprinklers, M&E, security, fire alarms, M&E fit out generally
- ▶ Brickwork flatlined - lack of housebuilding opportunities
- ▶ Cost impact of carbon offsetting evidenced in higher rates for concrete. Steel more competitive than previously
- ▶ Pressures generally moved from being commodity based, to energy and labour driven

Trades

- ▶ Pressures generally easing, though long-term skills and labour challenges remain
- ▶ M&E costs still rising ahead of general building work. Possibly due to larger wage increases of specialist labour and ongoing imported-plant inflation
- ▶ Still seeing some short-term capacity issues, nothing specific in terms of spikes

BCIS Industry panel (View on the ground)

Sectors

- ▶ Slowdown in residential releasing some supply chain, reports easier to get subcontractors in some areas due to reduced housebuilding activity
- ▶ Public housing benefiting from slowdown in private housing - freeing up resources and availability of supply chain

Other

- ▶ Contractors unable to secure performance bonds as number of providers assess that building sector is becoming too risky and either limit their exposure or withdraw from market
- ▶ Some investors forced to pause schemes, due to high interest rates, inflation and the upcoming general election
- ▶ Insolvency risk a concern for both those managing supply chains and those looking to fill tender lists, who are sometimes faced with a less competitive environment
- ▶ Signs residential projects in London have passed through second staircase redesign and will potentially start on site in 2024. Start dependent on viability, which is dependent on cost reduction and other adjustments achieved by working in partnership

Summary

Is this the new normal?

- ▶ Wider economy and construction sector both show clear signs of slowdown as effects of monetary tightening continue to build
- ▶ Worst impacts of inflation appear to be diminishing, although we predict CPI likely to remain above BoE's 2% target for at least another year
- ▶ The question everyone is asking: when might BoE start to reduce interest rates?
- ▶ Hopefully sooner rather than later, but some of their thinking likely to be conditioned by situation in the Middle East, particularly the Red Sea trade route
- ▶ Past four years have pushed against boundaries of what industry once perceived to be normal
- ▶ Some stability seems to be returning to construction, but likelihood is 2024 will still be a difficult year. Perhaps not quite as bad as we have become accustomed to

Is this the new normal? What does the data tell us?

- ▶ Total output falling, driven by decline in new work. R&M, which has been growth sector over past few years, also beginning to level out
- ▶ Housing in particular continues to be a drag on sector output growth, though some recovery forecast later this year
- ▶ Material costs falling for first time since onset of pandemic
- ▶ Labour costs increasing, but expected to peak early this year
- ▶ Overall costs and prices movement forecast to be relatively benign for first time since beginning of decade
- ▶ After difficult few years, we may have turned a corner.....though much will depend on timing of any interest rate cuts, outcome of the general election and ongoing situation in the Middle East

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