

gleeds

2018 Q3

Economic and Regional Inflation Report

Economic

- ➔ Bank Rate rises to 0.75%
- ➔ GDP grows 0.4% in Q2 2018
- ➔ Construction output down 0.9% in Q2 2018



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overview

statistics

market

regions

- ▶ Industry News & Updates
- ▶ Economic Overview
- ▶ Background to Economic Outlook
 - UK Economics
 - Global Economics
- ▶ Statistics & Figures
 - Outlook for GDP & Inflation
 - GDP, CPI & RPI Movement Predictions
 - Annual Inflation Rates
 - Tender Price Forecasts
 - Volume of Construction Output
 - Value of Construction Output
 - Employment
- ▶ Market Reports
 - RICS Market Surveys
 - The Glenigan Index
 - Construction Output Summary of Forecasts
- ▶ Regional Reports

Regions



▶ Acknowledgements

▶ Gleeds Contacts

Industry News & Updates

Brexit white paper

The government has published its long-awaited Brexit white paper, outlining proposals for the UK's future relationship with the European Union (EU). It outlines key objectives including the development of a broad economic relationship with the EU, plans to end free movement, and to protect the Northern Ireland peace process. The aim outlined by the white paper is for a free trade area for goods in a bespoke 'facilitated customs arrangement'. PM Theresa May has now taken on the task of negotiating the UK's exit from the EU, after the resignation of former Brexit secretary David Davis. His replacement, Dominic Raab, will take a backseat to May in the 'accelerated' process.

Cladding removal

Measures to drive the removal of unsafe cladding have been announced. This follows the revelation that 297 private sector residential buildings contained harmful cladding in June, with the status of a further 170 to be confirmed. The Ministry of Housing, Communities and Local Government states that building owners hold the responsibility for making their buildings safe but local authorities have been required to instigate enforcement in many cases.

Actions to accelerate the pace of works include the formation of a new taskforce and inspection team to oversee a national programme of private sector remediation, and an industry roundtable to allow representative to present possible solutions.

Off-site manufacturing

The House of Lords select committee for Science and Technology has published their inquiry *Offsite manufacture for construction: Building for change* which considers the potential for off-site manufacturing to improve productivity in the construction sector. It also looks at what actions might be required within the industry to drive uptake of off-site methods. The inquiry is in favour of off-site construction but highlights significant barriers in the lack of collaboration across industry, the skills shortage and an absence of leadership within construction. However, it is hoped that the release of the Construction Sector Deal in July will help to drive forward off-site manufacturing and technology.

Carillion

In July, the government published its response to the findings from the joint committee inquiry into Carillion's collapse at the beginning of the year. The Business and Work and Pensions committees made five recommendations in their report published on 16th May:

1. Changes to ensure that all directors who exert influence over financial statements can be investigated and punished, not just those with accounting qualifications
2. The Financial Reporting Council (FRC) should be given more power as a regulator in order to serve as a deterrent against poor boardroom behaviour

3. A more active and interventionist approach in the forthcoming revision of the Stewardship Code, including a more visible role for the regulators to enable greater reporting and transparency in terms of investor engagement
4. Minimum standard for bonus clawback for all public companies to promote long-term accountability
5. The Insolvency Service should set and regularly review spending and performance criteria and provide full transparency on costs incurred and expected future expense for Special Managers, due to concerns over PwC's appointment in this role

The government's response did not suggest that action would be taken as a result of Carillion's collapse and referred to powers already held by the Insolvency Service, FRC, Competition and Markets Authority (CMA) and Financial Conduct Authority.

They also rejected the call for a minimum standard for bonus clawbacks saying this was a matter for the shareholders of individual firms. The government did, however, recommend that the CMA consider breaking up the 'big four' accountancy firms and that this was currently being considered. The Insolvency Service addressed the concerns about the Special Manager role, stating that "a protocol had been agreed between the Official Receiver and PwC setting out the work that the special managers carry out and the governance that applies" and confirming that a payment of £22.9m had been agreed for their services.

Heathrow expansion faces High Court challenge

Legal action from Friends of the Earth (FoE) is likely to delay transport secretary Chris Grayling's plans to commence construction as early as 2021 and have the runway operational by 2026. FoE argue that the plans breach the UK's climate change policy and sustainable development duties, namely the target for reduction of greenhouse gas emissions under the Climate Change Act 2008. They are expected to be supported in their fight by London mayor Sadiq Khan and those MPs whose constituencies would be under the new flight path (Hillingdon, Richmond, Wandsworth, and Windsor & Maidenhead).

New Projects in the Pipeline



Mixed-used development 'Free Wharf' in Shoreham, West Sussex, designed by CZWG, has received planning consent and works are expected to start in the autumn; the scheme will include 540 new homes and 2.774m² of commercial space



Plans to revamp Tottenham Hale, North London have been submitted to local planners; the AHMM and Alison Brooks Architects-design scheme involves a six-building housing scheme with over 1,000 homes, retail, office and leisure space



AHMM has submitted **plans for a £75m regeneration project in Belfast** in which will refurbish the listed former headquarters of the Belfast Telegraph, the 1886 Seaver building and redevelop the surrounding city centre



Willmott Dixon has won a **£46.5m contract for the University of Birmingham's School of Engineering** after recently completing the university's new research data centre



Vinci has won a **£27.2m D&B contract to deliver close to 400 student bedrooms** across two buildings for the University of Exeter, as part of a wider accommodation programme on its Streatham campus



Housing association Clarion has bought a **10-acre site complete with planning permission in Beck Row**, Suffolk and is set to build 115 **affordable homes** in association with Lovell



Kier has won a **£39m contract** to build a 1m ft² **B&M distribution hub in Wixams**, Bedford for developers UK Land and Property



Whittam Cox Architects has won **planning permission for the third phase of the transformation of Park Hill in Sheffield** which will deliver 74 flats to accommodate 356 students along with commercial space



Assael Architecture has submitted **plans to build 2,000 homes at 'Margarine Works'**, the former Maypole margarine factory in Ealing, which will also include retail, commercial and leisure facilities



The University of Bath is **seeking a contractor to deliver its £60m Institute for Advanced Automotive Propulsion Systems** at Bristol and Bath Science Park, designed by Stride Treglown and DKA



Kier has won a **£36m deal to convert two disused buildings into a new cardiac unit and outpatients' department** for private patients at St Bartholomew's Nuffield Health Hospital in central London



Permasteelisa has won a **£62m contract** to carry out work on **Phase 3A of the Battersea Power Station** redevelopment to design, supply and install more than 27,000m² of cladding



Galliford Try has won a **£31.7m contract to build a new £3bn sports park and refurb existing facilities at Durham University**, which will include an indoor cricket hall, a 12 court multi-use sports hall, a martial arts gym, a fitness suite and a high-performance weights room



Countryside Properties will partner housing association Home Group to deliver a residentially-led mixed-use development in Brent, which will also include a health centre, commercial and retail space, as well as public realm improvements

Economic Overview

Gleeds' Economic Report reviews factors affecting UK construction, taking into account inflation, construction output, orders and employment. It also assesses wider social, political and economic matters which could impact on the economic environment and general confidence in the market.

LOOKING BACK TO Q1 2018

Construction output

According to revised data from the Office of National Statistics (ONS), construction output decreased by 0.8% in Q1 2018 compared to Q4 2017

Over the previous 12-month period construction output decreased by 4.9%

Q2 2018 – THE LATEST FIGURES

Construction output increased by 0.9% in Q2 2018 when compared to the previous quarter (Q1 2018)

Over the previous 12-month period (June 2017 to June 2018), construction output has increased by 2.2%

Pay and employment

In Q1 2018, the unemployment rate fell to 4.2%

ONS predicted that average weekly earnings (total pay) in the construction industry rose by 4.5% in the year to Q1 2018

Unemployment falls to 4.0%

Average weekly earnings for construction workers rose by 5.3% in Q2 2018 compared to a year earlier



The impact of the lack of an agreed Brexit deal is being seen in the markets; with uncertainty increasing, the rate of construction inflation has slowed. The next six months will be key - what happens in London is bound to then spread to the regions."

PAUL SWEENEY, DIRECTOR, GLEEDS

Gleeds' regional inflation forecast

ANNUAL % CHANGE	3Q18 to 3Q19	3Q19 to 3Q20	3Q20 to 3Q21	3Q21 to 3Q22
EASTERN	3.00	3.00	4.00	5.00
GREATER LONDON	2.50	2.50	4.00	5.00
NORTH EAST	3.00	3.00	3.00	3.00
YORKSHIRE & HUMBERSIDE	4.00	5.00	5.00	5.00
NORTHERN IRELAND	2.00	4.00	5.00	6.00
MIDLANDS	3.50	3.50	4.00	4.00
NORTH WEST	3.00	3.00	3.50	3.50
SCOTLAND	2.00	2.00	3.00	3.00
SOUTH EAST (EXCLUDING LONDON)	3.50	4.00	5.00	5.00
SOUTH WEST	3.00	3.50	4.50	4.50
WALES	3.00	4.00	4.50	4.50
UK AVERAGE (ROUNDED)	3.00	3.40	4.10	4.40

Note: these are average regional forecasts based on activity and market awareness within Gleeds' regional offices. Actual inflation will be determined by a combination of macroeconomics and micro project situations. Forecast inflation at a project level needs to be carefully considered based on the project's characteristics and prevailing local conditions. All published statistics can be misleading and subject to later revision and should be used with caution.

Background to Economic Outlook

UK Economics

In their August Inflation Report, the Bank of England's (BoE) Monetary Policy Committee (MPC) voted unanimously to increase the Bank Rate to 0.75%. The MPC also voted to maintain the stock of non-financial investment-grade corporate bond purchases at £10bn and the stock of UK government bond purchases at £435bn.

The decision to raise the Bank Rate to its highest level since March 2009 was based on four key factors:

1. Inflation is above the 2% target
2. The easing of the squeeze on pay
3. The current level of growth is around its 'speed limit', which the MPC judges to be GDP growth of around 1.5% per annum
4. The Bank's belief that interest rate rises should be gradual and limited.

GDP is expected to grow at around 1.75% per annum over the forecast period. Although modest by historical standards, this projection exceeds the diminished rate of supply growth, or 'speed limit', which averages around 1.5%. According to the MPC, the UK economy still possesses a very limited degree of slack and, as unemployment is low, this is expected to create a small margin of excess demand by the end of 2019.

Consumer price inflation (CPI) remains above target, due to the effects of sterling's past depreciation and rising energy prices. Since the release of the BoE's May inflation report, sterling has depreciated by a further 2.5%. However, CPI is expected to fall throughout the second half of 2018 as the contribution from fuels diminishes.

Bank Rate is projected to reach 1.1% by the end of 2021 and thereafter, reach a peak of between 2% and 3%. Previously, we have been used to a rate of 5%. Slower population growth, longer life expectancies, greater costs of financial remediation, and decreasing productivity growth mean that this is unlikely to happen.

Global Economics

Global growth remained broadly stable in Q2 2018; while growth in the US was stronger than expected, activity was somewhat weaker in other markets. Growth in global trade and capital goods orders also declined.

The outlook for global growth remains robust and this is expected to push up inflation generally. Higher oil prices and wage growth will also continue to generate additional inflationary pressure.

GDP growth in the euro area averaged 0.4% in the first half of the year, considerably lower than the 0.7% expected in May. However, GDP growth is expected to recover to 0.5% in the second half of the year. US GDP growth rebounded strongly from a dip in Q1 2018 to 1% in Q2 2018, although this is expected to fall back in Q3. GDP growth in China picked up to 1.8% in Q2, even more strongly than expected.

Source: Bank of England, Quarterly Inflation Report, August 2018



Summary

- The Bank Rate has been maintained at 0.75%
- CPI is expected to return to the 2% target by the end of 2018
- Global growth remains stable in Q2 2018

Statistics & Figures

Outlook for Gross Domestic Product (GDP) and Inflation



Sources:

Office for National Statistics (ONS), UK
GDP monthly estimate: June 2018;

ONS, UK consumer price inflation: July 2018

Quarterly GDP is estimated to have increased by 0.4% in Q2 2018, up from 0.2% in the previous quarter. However, the underlying trend is one of slowing growth; GDP increased by just 0.6% in the first half of the year.

Following a lull in demand in the consumer-facing industries, **Services** growth picked up to 0.5% in Q2, in line with expectations. Some of this can be attributed to the warmer weather, Bank Holidays and World Cup, all of which had a positive effect on food and drink, summer clothing and garden furniture sales. Growth in business services and finance slowed in Q2, driven partly by a fall in architectural and engineering activities.

Output in the **Construction** industry increased by 0.9% in Q2 2018, following a decline of 0.8% in the previous quarter. Anecdotal evidence suggests that the improved weather conditions may have driven a surge of activity in house building and the commercial and civil engineering sectors. However, growth remains below the quarterly average for 2017 (1.1%).

Production decreased by 0.8% in Q2 2018. The warmer weather conditions saw energy supply fall by 2.7%, while manufacturing fell by 0.9%. The weakness in manufacturing reflects an easing in export growth, suggesting a drop in global demand for UK-produced vehicles and materials for processing destined for China. Mining/quarrying and waste management production both increased by 0.7% and 1.9% respectively.

CPI in the year to July 2018 was 2.5%, up from 2.4% in June 2018. This slight increase can be attributed to the rising cost of transport and computer games which were partially offset by falling clothes prices. This is the first increase to CPI since last November although is in line with forecasts.

The Retail Prices Index (RPI) fell to 3.2%, further narrowing the gap to CPI.

The CPI including owner occupiers' housing costs (CPIH) inflation rate was 2.3% in July 2018, unchanged from June 2018.

Note: CPIH is the most comprehensive measure of inflation as it includes a measure of the costs associated with owning, maintaining and living your own home as well as Council Tax, which are not included in CPI.



Summary

- GDP grows 0.4% in Q2 2018
- CPI creeps up to 2.5% in the year to July 2018
- CPIH remains at 2.3% for third consecutive month

GDP, CPI & RPI Movement Predictions

	2018	MOVEMENT	2019	MOVEMENT	2020	MOVEMENT	2021	MOVEMENT	2022
GDP growth (%)	1.3	↑	1.6	↑	1.7	↑	1.8	↑	1.9
CPI (%)	2.4	↓	2.1	↓	2.0	↔	2.0	↑	2.1
RPI (%)	3.4	↓	3.1	↓	3.0	↑	3.1	↑	3.2

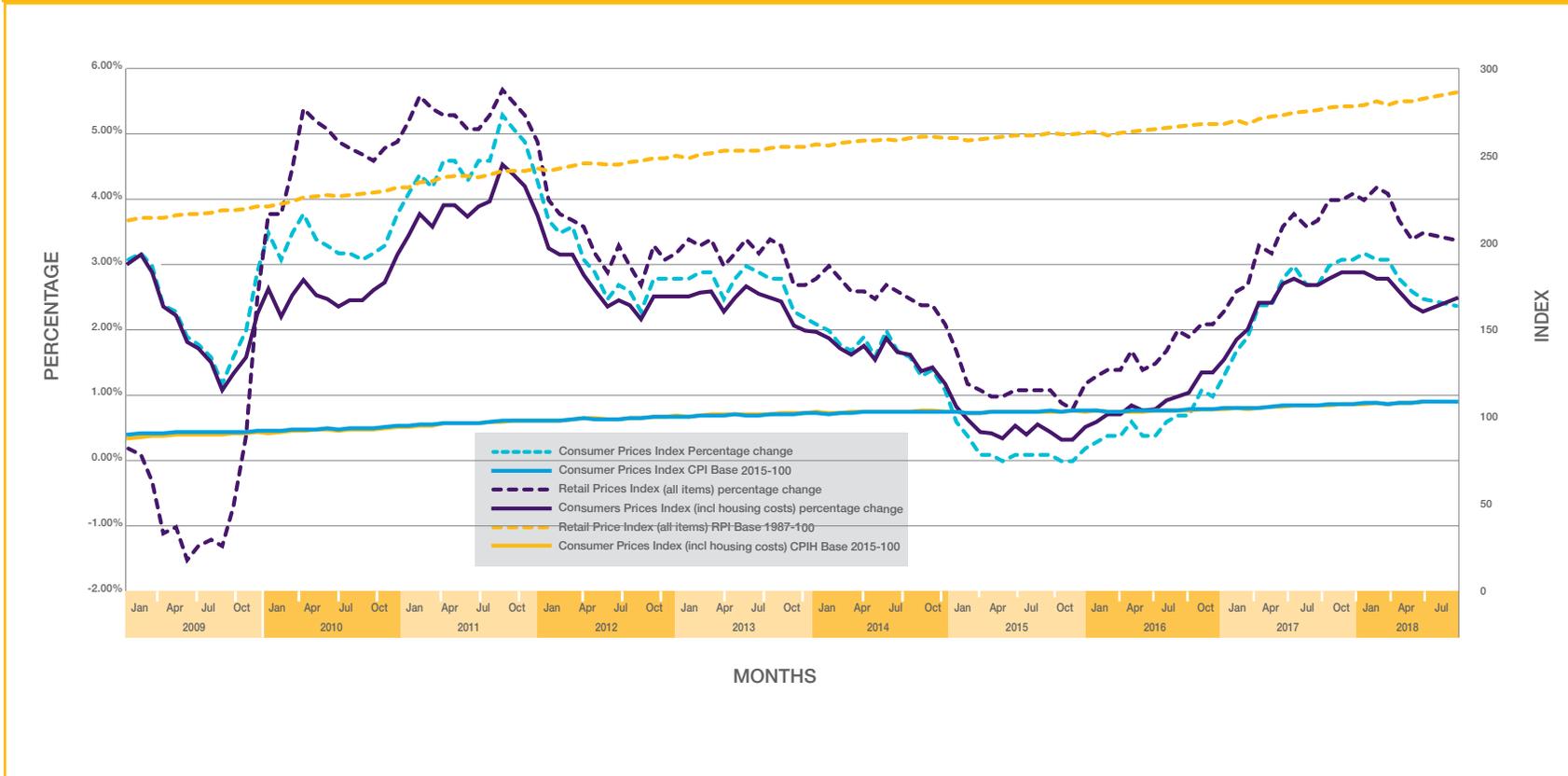
Source: HM Treasury Forecasts for the UK Economy, August 2018

Forecasts for the UK Economy is a summary of published material reflecting the views of a selection of forecasting organisations which are subject to review. This edition contains 25 forecasts, all of which were received between August 1st and August 10th 2018. The table above summarises the average of May's forecasts.



Annual Inflation Rates

ANNUAL INFLATION RATES OFFICE OF NATIONAL STATISTICS Q3 2018



Tender Price Forecasts

Gleeds considers that tender prices, on average, grew by 2.3% between 3Q 2017 and 3Q 2018. For the same period, the **Building Cost Information Service (BCIS)** has forecasted a 1.6% rise in prices.

BCIS predicts that tender prices will increase over the four-year forecast period as follows.

Forecasts of Tender Prices:

Year on Year	Current BCIS Forecast (17/08/2018)	Gleeds Average Forecasts
3Q2018 to 3Q2019	+3.2%	+2.9%
3Q2019 to 3Q2020	+4.0%	+3.4%
3Q2020 to 3Q2021	+6.0%	+4.1%
3Q2021 to 3Q2022	+5.9%	+4.4%

Volume of Construction Output

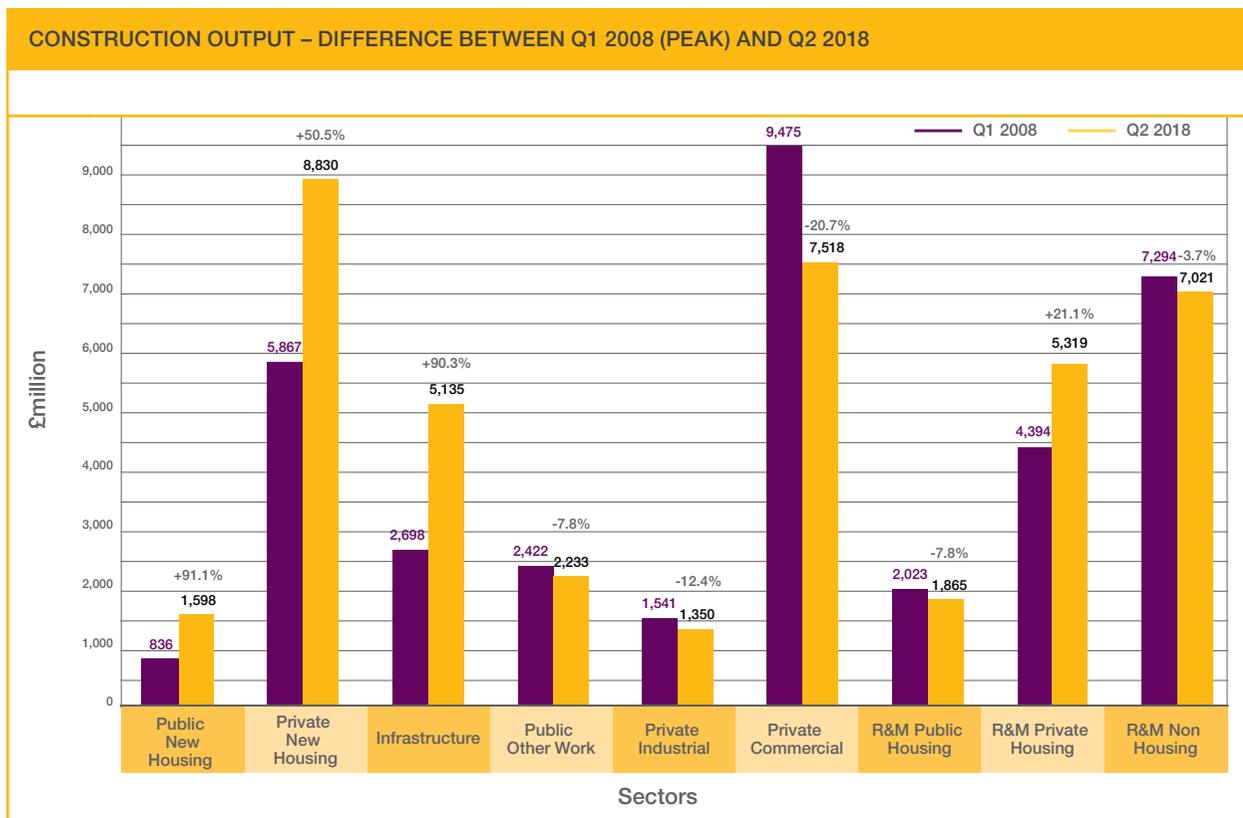
Looking at the volume of construction output, the ONS reports that:

In Q2 2018, **total construction output** increased by 0.9%, recovering from a fall of 0.8% in Q1 2018, following three consecutive periods of decline. This was due to a 2.7% increase in **all repair and maintenance (R&M)** output while **all new work** remained flat over the quarter. Construction output has now returned to the levels seen at the end of 2017.

Following a weak start to 2018, R&M made the biggest positive contribution to growth in Q2 2018. New public housing and infrastructure also made a strong contribution, growing 10.4% and 2.6% respectively.

Only two sectors – new private housing and public other new work – provided downward pressure on the volume of construction output in Q2 2018. Public other new work, which is made up of publicly funded projects in the health, offices, schools, colleges and university sub-sectors, fell by 8.4% in Q2 2018, representing the 15th consecutive decline in output.

In stark contrast to adverse colder weather effects earlier in the year, anecdotal evidence suggests that the more recent warmer conditions have had a positive impact on construction output.



Value of Construction Output

Sector	Q1 2018 – Q2 2018	Q1 2008 – Q2 2018
All Work	3.0%	30.0%
All New Work	2.7%	31.9%
New Public Housing	11.9%	90.9%
New Private Housing	2.8%	80.7%
New Private Commercial	1.9%	-11.3%
New Private Industrial	7.2%	-4.4%
New Public Non-housing	-6.9%	3.3%
New Infrastructure	4.8%	123.2%

Sector	Q1 2018 – Q2 2018	Q1 2008 – Q2 2018
All R&M	3.6%	26.5%
Public Housing R&M	2.9%	10.7%
Private Housing R&M	2.4%	60.0%
Infrastructure R&M	6.5%	N/A
Public Non-housing R&M	6.4%	-42.1%
Private Non-housing R&M	3.2%	-18.9%

Source: ONS, *Construction output in Great Britain: June 2018*

Employment

During Q2 2018, the UK-wide unemployment rate fell to 4.0%, down from 4.2% in Q1. The number of people classed as 'unemployed' decreased by 65,000 and the number in employment increased by 42,000 to a rate of 75.6%, unchanged from Q1 2018. The proportion of people classed as 'economically inactive' – those not seeking or available to work – has risen slightly to 21.2%, up from 21.0% in Q1 2018.

The employment rate for women aged 16-64 has fallen slightly, from 71.2% in Q1 to 71.0% in Q2 2018. The employment rate of women has been steadily increasing over the last few years due to ongoing changes to the State Pension age for women, meaning that fewer women retiring between the ages of 60 and 65 years.

The number of EU nationals working in the UK has fallen by 86,000 over the past year. This is the largest decline since comparable records began and can be attributed to status concerns post-Brexit.

Workers' earnings excluding bonuses (regular pay), rose 2.7% in Q2 2018 compared to a year earlier, falling from 2.9% in Q1. Total pay increased by 2.4% in the same timeframe. In real terms, adjusted for consumer price inflation at 2.5%, regular pay increased by 0.2% and total pay by 0.1%.

In the construction industry, average weekly earnings (total pay) rose by 5.3% in Q2 2018 compared with a year earlier, while regular pay (excluding bonuses) rose by 5.6% over the same timeframe.

Source: ONS, UK labour market: August 2018

Market Reports



The results of the Q2 2018 **RICS Construction & Infrastructure Market Survey** show a broad deceleration in the pace of growth. Only 15% of this quarter's respondents reported an increase in total workloads, down from 23% in the previous quarter.

The strongest slowdown happened in the private industrial and housing sectors. Anecdotal evidence indicates that investment decisions are being impacted by the housing market slowdown and ongoing ambiguity with the Brexit negotiations. The private commercial and infrastructure sectors also saw a decline in activity while the rail, roads and energy subsectors are expected to experience strong growth over the coming year. Public sector workloads were mixed with surveyors reporting a modest acceleration to growth in housing (12%) but slowdown in non-housing (-5%).

54% of respondents expect tender prices to increase over the next 12 months, down from 63% in Q1 2018, and this is projected to signal rising input costs and shrinking profit margins. Financial constraints are reported by 80% of surveyors as the most significant impediment to growth, up from 76% in Q1. Planning delays and labour shortages continue to pose a challenge. The lack of sufficiently skilled workers is particularly acute for professional services such as quantity surveying.

Workloads in all geographic regions are now reported to be decreasing, and particularly so in the Midlands and East Anglia. However, workloads remain resilient in the North and South West, supported by solid activity in private housing.

Source: RICS, UK Construction and Infrastructure Survey, Q2 2018

“ The Q2 2018 **RICS Construction & Infrastructure Market Survey** results show the downturn across the retail sector intensifying, with stores in secondary locations displaying particularly negative rental and capital value projections. This remains in contrast with the performance of the industrial sector, which continues to attract solid demand from both occupiers and investors.”

Source: RICS, UK Commercial Property Market Survey, Q2 2018

Construction Output Summary of Forecasts

SECTOR	YEAR	EXPERIAN	CONSTRUCTION PRODUCTS ASSOCIATION
TOTAL CONSTRUCTION OUTPUT	2018	-2.1%	0.1%
	2019	1.7%	2.7%
	2020	3.1%	1.9%
TOTAL NEW WORK	2018	-2.6%	0.3%
	2019	1.6%	3.4%
	2020	3.5%	2.3%
REPAIR AND MAINTENANCE	2018	-1.3%	-0.2%
	2019	2.0%	1.4%
	2020	2.5%	1.3%
PUBLIC HOUSING	2018	0.0%	3.0%
	2019	3.0%	3.0%
	2020	6.0%	0.0%
PRIVATE HOUSING	2018	3.0%	5.0%
	2019	3.0%	2.0%
	2020	4.0%	1.0%
INFRASTRUCTURE	2018	0.0%	6.4%
	2019	10.0%	13.1%
	2020	9.0%	7.0%
PUBLIC NON-HOUSING	2018	-9.0%	-4.8%
	2019	-1.0%	0.9%
	2020	-1.0%	1.5%
PRIVATE INDUSTRIAL	2018	1.0%	2.3%
	2019	0.0%	1.4%
	2020	1.0%	2.5%
PRIVATE COMMERCIAL	2018	-9.0%	-7.8%
	2019	-5.0%	-0.8%
	2020	0.0%	0.7%

The Glenigan Index

Glenigan's August Index reflects a subdued market. The value of project starts in the three months to July 2018 was down 15% on a year ago and 1% down on the preceding three-month period. This is primarily due to a general decline in both residential and non-residential building projects, most notably in social housing, commercial, education and community projects.

Private residential and social housing starts were 11% and 40% lower than a year ago respectively. Overall non-residential projects were 18% lower than a year ago owing to sharp declines in commercial, retail and education starts. Health projects saw a 50% rise in starts compared to a year ago while civil engineering also increased, up 35% over the same timeframe. This was driven by a 12% increase in infrastructure starts and an 80% jump in utilities work.

London experienced the sharpest decline in starts, down 45% on a year ago. The South East, East of England, Yorkshire & the Humber, Northern Ireland and Scotland also saw significant falls of 16%, 18%, 30%, 37% and 11% respectively. In the East Midlands, however, the value of project starts was 41% up on a year ago and starts were also up 14% in both the West Midlands and North East.

Source: *The Glenigan Index, August 2018*

Construction Output Summary of Forecasts

BCIS considers that there remains a great deal of uncertainty over the terms that will be agreed when the UK leaves the EU. On this basis, they continue to produce forecasts based on three different scenarios reflecting a range of potential outcomes from the EU exit negotiations. These are:

 **Upside scenario** – the UK will remain a member of the EU (but with no voting rights) and retains access to European construction operatives after cessation of the two year transitional period

 **Downside scenario** – the UK will experience a 'hard Brexit' (i.e. no transitional period) with less favourable trade agreements with the EU and restricted movement of labour

 **Central scenario** – the UK will remain a member of the EU (but with no voting rights) but there will be some restrictions to the movement of labour and less favourable trade agreements

All scenarios are equally likely and assume that there will be no change of UK government over the forecast period and that there is political stability in the rest of the world.

Year on year	Upside Scenario	Central Scenario	Downside Scenario
2018	5.5%	-0.3%	-9.9%
2019	6.3%	1.6%	-5.9%
2020	6.4%	3.7%	6.3%
2021	5.5%	4.9%	9.7%
2022	5.3%	4.5%	6.2%

Spotlight on the Energy sector - Gary Mills

Gleeds' Gloucester office is predominantly occupied by their two big energy sector clients – EDF and Horizon Nuclear Power. At present, both EDF's Hinkley Point C and Horizon Nuclear Power's Wylfa Newydd projects are demanding high resource requirements.

Hinkley Point C has now moved significantly into the marine works phase, both on-site (both reactor bases) and off-site (Temporary workers accommodation phase 1 completion, phase 2 due to commence shortly). At Horizon, some site preparation activities have commenced, together with significant work to help demonstrate procedures adopted for supplier engagement as well as spent costs in readiness for the Department for Business, Energy & Industrial Strategy review. Reviews of the cost estimate are now taking place as well as preparations for the examination phase of the Development Consent Order (DCO) process.

The energy sector is vulnerable to the same external factors as much of the rest of the industry, such as the insolvency of Carillion and the subsequent labour redeployment, uncertainty created by other contractor restructuring (such as Interserve) and the likely loss of skilled European labour post-Brexit. Of particular concern to the sector are discussions between Hitachi and the Japanese government discussions and the UK government and investors, the Chinese nuclear involvement in Hinkley and Bradwell, and Trade and Union Pay Agreements and/or disputes at Hinkley Point C. The uncertainty around what impact a hard or soft Brexit will have on imported goods, trade, migrant workers, ex-pat overseas workers and currency variation can and should not be under estimated.



Regional Reports

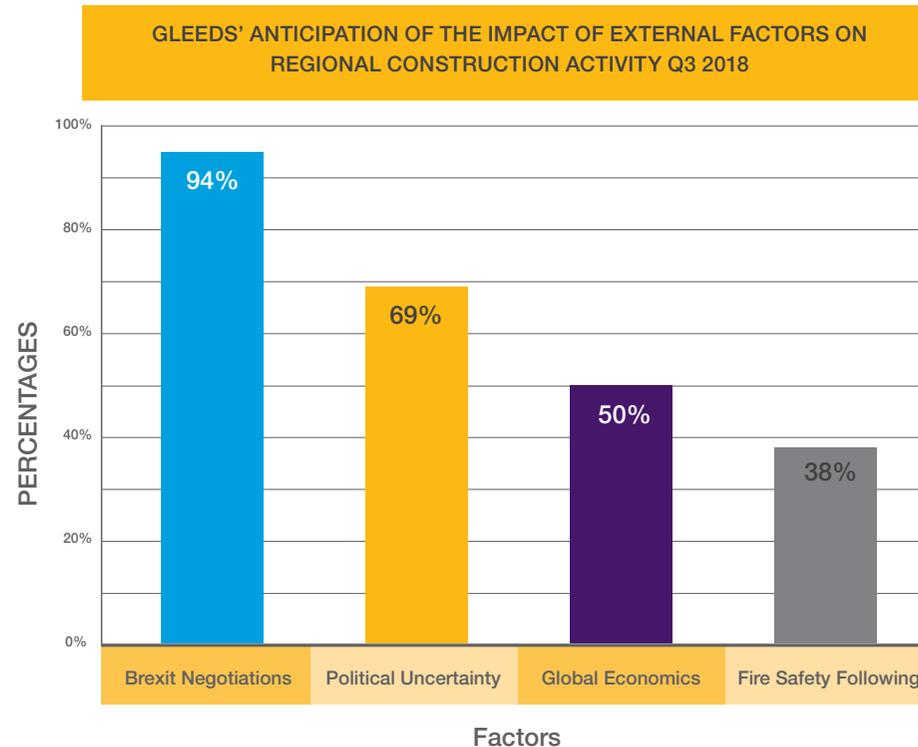
Gleeds monitors construction activity and confidence in each UK region.

As well as activity analysis, we directly engage with local contractors and industry contacts to understand their experiences. As feedback contains a degree of opinion and anecdotal evidence, it is not completely scientific, but should provide a useful insight into the views of those at the core of industry.

While it may not be possible to predict future trends or pre-empt potential stressors, careful monitoring of regional activity can provide us with the ability to adapt to adverse conditions more rapidly and effectively.

External factors

Brexit negotiations continue to be the dominant source of concern, with 94% of Gleeds' staff expressing uncertainty in this regard. Political uncertainty in the UK is having an impact on confidence over much of the UK (69%) and global economic conditions remain a significant concern (50%) despite relatively robust forecasts. Issues surrounding fire safety post-Grenfell appear to be having less of an impact on the industry, falling from 56% in last quarter's report to 38% in Q3 2018. Our contributors also highlight insufficient funding arrangements and a lack of government support as potential pit falls, and this can be evidenced by the government's decision to withdraw funding from the Swansea Bay Tidal Lagoon project (see Wales regional commentary below for more information). Interest rate rises and potential contractor liquidation are also playing on people's minds.



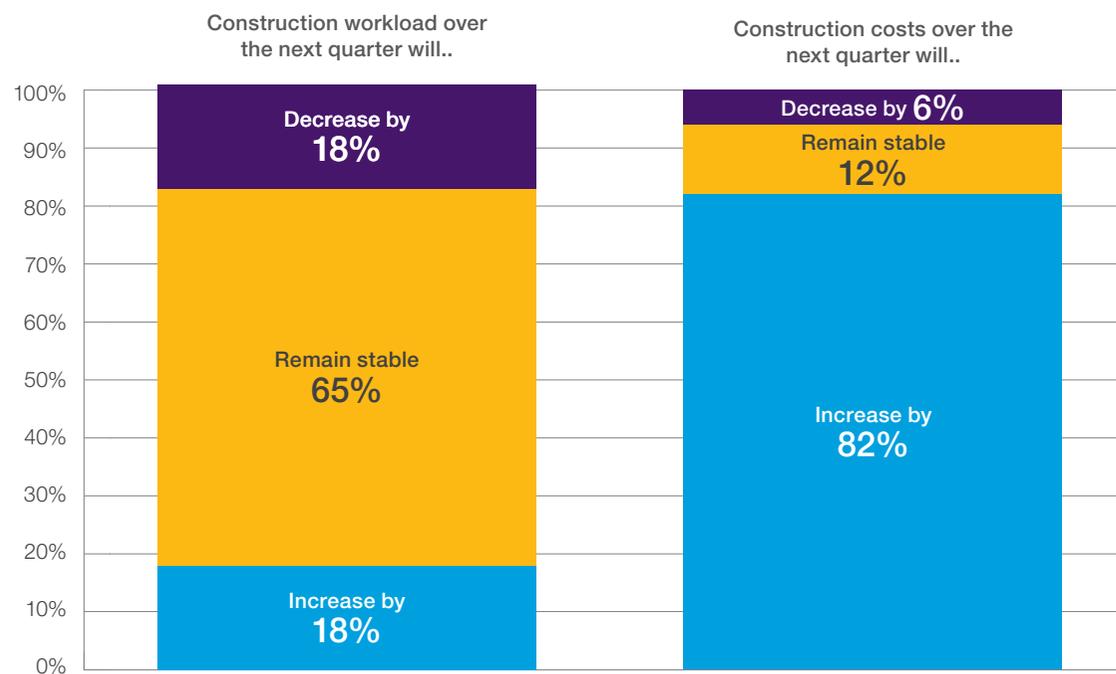
Regional Reports

According to our contacts, the East, North West and Northern Ireland are seeing the migrant population moving out of the local area. This is thought to be as a direct result of concerns about a more hostile living and working environment following Brexit as well as uncertainty over the security of their status in the UK after we leave the EU.

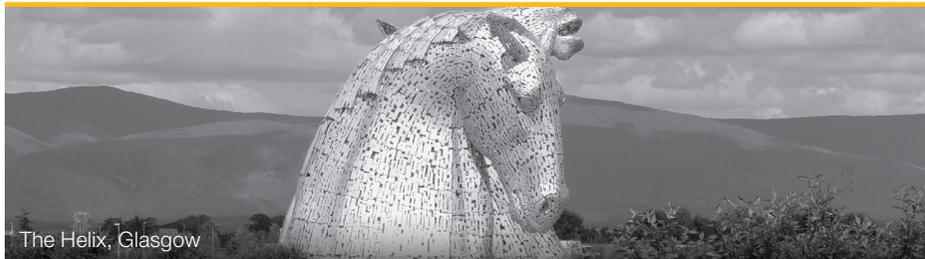
More than 40% of our contacts believe that bankruptcies in the industry are on the increase compared with 12 months ago. This is a concern for capacity moving forward especially in those regions already reporting labour shortages (North East, North West, Northern Ireland).

Construction workloads are projected to remain stable over the next quarter while costs are expected to increase.

PREDICTION FOR CONSTRUCTION WORKLOADS AND COSTS OVER THE NEXT QUARTER



Regional Reports



The Helix, Glasgow

Nigel Watkins

Reporting on Wales

Discussions with local businesses confirm that current levels of activity in the region remain good with a healthy amount of new opportunities in the pipeline - student accommodation, education, house building and commercial projects lead the way in South Wales.

Unfortunately bad news hit the proposed Swansea Bay Tidal Lagoon following the granting of planning permission in 2015, with the notification that the UK Government felt the project too expensive to subsidise. There is renewed hope however, following an independent review in July, that the project could be funded independently and with private finance. If the project proves successful, this could kick-start similar projects at Newport, Cardiff and Colwyn Bay.

Student accommodation schemes remain a strong sector locally, with commercial offices and education projects making up the bulk of the remaining workload. The local supply chain is able to support this activity although there are not enough specialists/large sub-contractors; this expertise has to be brought in from further afield.

The number of new homes being built by the private sector in Wales grew firmly in

the second quarter of the year, but overall activity in the construction sector was flat, according to figures from the RICS Construction & Infrastructure Market Survey.

The development of Central Quay, a joint venture between SA Brain and Rightacres, on the former SA Brains Brewery site in Cardiff could see up to 3m ft² of new leisure, residential and office space over a 14 acre site South of Central Station. A public/private joint venture has been established locally to deliver public transport projects within the capital (Metro Delivery Partnership) - the Interchange Project has also been given the green light to progress and a new planning application is to be submitted shortly.

The aftermath of Grenfell has generated a hesitancy to utilise ACM cladding products on a number of projects, with developers needing to look for alternatives; the uncertainty over future legislation in this regard does impact material selection and could increase costs.

🚩 In our previous quarterly report, levels of construction activity in Wales were strong, driven by the student accommodation, commercial and education sectors.

Brian Stevenson

Reporting on Scotland

The retail, education, residential and infrastructure sectors are the main drivers of growth in Scotland at present. Retail clients, in particular, are looking to refurbish their current assets alongside the construction of new assets in order to increase customer footfall and draw in high-end tenants. Universities are also undertaking a mixture of refurbishment and new build works in anticipation of increasing student applications. The volume of infrastructure projects continues to increase, with developments outside of Aberdeen and Edinburgh underway, which could pave the way to addressing Scotland's housing shortage. There are also encouraging signs for the commercial sector within the region.

Current planned works include:

- Two Ministry of Defence projects in Faslane (£400m) and Loussiemouth (£350m)
- A £70m infrastructure project outside of Edinburgh to create a new town (Blindwells)
- A £68m student accommodation project for the University of St Andrews
- A £47m new Government offices project in Edinburgh
- A £11m infrastructure project at Countesswells, Aberdeen
- A £70m new Regional Distribution Centre for Lidl
- Sutherland Vertical Launch Facility
- Glasgow Harbour Lifestyle Outlet
- Barclays campus, Buchanan Wharf

The Scottish construction industry is, however, beginning to experience difficulties with resourcing, in particular with bricklayers, joiners, and painters as demand is exceeding supply. Another key issue is that tier one contractors are becoming more risk-averse when it comes to project tendering and are less inclined to tender for high risk, high value (£50m+) projects. It is anticipated this will have a negative impact on high value major projects in the region and is likely to drive tender costs up. In addition, material prices continue to rise - this has been encountered in steel, insulation, bricks, and timber.

Brexit remains the most immediate and complex of the challenges the economy faces and has created uncertainty among investors.

🚩 Last quarter, we reported that workloads in Scotland were stable, with the bulk of activity in the retail, residential and infrastructure sectors. Much of these works were refurbishments rather than new builds reflecting uncertainty in the wider economy.

Regional Reports



Geoff Warke

Reporting on Northern Ireland

The Northern Ireland economy is expected to grow by 1% during 2018 and 1.2% during 2019, taking into consideration Brexit-related uncertainty and political considerations going forward.

The total volume of construction output in Q1 2018 decreased by 6.5% compared with Q4 2017 and was 6.1% lower compared to the same quarter in 2017. The latest decrease followed four quarters in which the level of construction output has been broadly consistent.

However, Northern Ireland's construction sector remains relatively buoyant despite the ongoing Brexit and political uncertainties. Most of the activity has come from infrastructure works, commercial offices, hotels and the residential market. Following the post-election deal between the Conservatives and the DUP, £1b of new money is now being spent on infrastructure projects such as the Belfast Transport Hub and the York Street road interchange project. This is a timely boost to the local construction market.

The local political parties are currently meeting with the Secretary of State to progress agreement of a lasting deal; if this does not materialise, the possibility of direct rule from Westminster might be instigated which may lead to more political instability.

In last quarter's report, we reported that Northern Ireland construction activity was growing due to infrastructure works, new Grade A offices, hotels and residential dwellings.

Galvin Tarling

Reporting on the Eastern Region

Within the last quarter, a market contraction, particularly within the commercial, retail and industrial sectors, has led to a further hardening of competitive tenders in the Eastern region. This is evidenced by a reduction in main contractor overhead and profit levels together with a smaller spread of competitive tenders. Main and sub-contractors seeking to bolster their order books for 2019/20 has also fuelled keener pricing.

Within the central Cambridge commercial office market, rents have broken £40/ft² during the preceding quarter. Investor and occupier demand remains buoyant.

The continuing economic uncertainty of Brexit has seen regular clients within the industry unwilling to commit to schemes in the short to medium term. There are instances of the migrant population returning home but labour availability remains adequate at present.

In our previous report, the construction market in the Eastern region remained relatively buoyant but an uncertain economic outlook was impacting on the competitiveness of tenders.

Regional Reports



St Pancras Renaissance, London

Paul Sweeney

Reporting on the Greater London Region

Brexit uncertainty continues to be reflected in the London and is impacting foreign investment. In particular, the demand for large new build commercial office schemes remains subdued, as it has for some time. Despite a general decrease in the volume of tenders, refurbishment and fit out activity remains strong.

The residential sector continues to slow and this, coupled with waning sales, is resulting in projects stalling.

An increase in contractor availability is anticipated towards the end of the year which in turn will lead to greater competition in the market place and keener tender returns as a result.

In our previous quarterly report, London was experiencing a slowdown in foreign investment which was impacting on workloads, particularly in the commercial and residential sector.

Phil Wright

Reporting on the Midlands Region

Construction activity across the Midlands remains buoyant. In particular, the residential sector in the West Midlands is strong owing to high demand for multi-room schemes. Large commercial and mixed use schemes are ongoing with the likes of Snowhill, Arena Central and Paradise under construction. The infrastructure to complement these developments and the Birmingham city plan is in progress.

Consultants and contractors continue to remain very busy across the Midlands. Contractors are becoming more selective on projects they tender for and are less prepared to engage in the competitive tendering process favouring two stage or negotiation instead. Material prices continue to rise and this is expected to generate increases in tender prices.

The construction industry is still greatly affected by external factors with the uncertainty of Brexit and associated impact on the UK economy continuing to have a detrimental impact. The increasing risk of a no-deal Brexit would further impact on the construction industry. Contractors continue to report issues of material and labour price increases and difficulties of availability.

However, the opportunity provided by HS2, the Big City Plan, and the Commonwealth Games all coming to Birmingham and major regeneration projects in Nottingham are providing a factor of insulation from the effects of Brexit and political uncertainty for the region.

In our previous quarterly report, we reported strong activity levels in the Midlands, driven by the residential, commercial and infrastructure sectors.

Regional Reports



Hiscox Insurance Building, York

Peter Burns

Reporting on the North East Region

Whilst construction activity in the North East region remains good, there have been signs of a slight slowdown over the past few months which is to be attributed to the uncertainty over Brexit. The Brexit factor is an ongoing concern although no-one is really sure what effect this will have on investor confidence, imported materials or the labour market, so it is not having a significant impact on prices as yet.

The residential sector across the North East continues to thrive but mainly in the affordable sub-sector. In Newcastle, a number of high profile apartment/residential schemes are coming forward. Developments such as the L&G project at Newcastle Helix and Central Square in Middlesbrough represent a bid to overcome the historic lack of investment in Grade A office accommodation throughout the region, particularly in the main city centres. The development at Vaux is also re-starting, having been retendered following the demise of Carillion.

A number of contractors report capacity to take on additional tender opportunities and tender levels remain competitive. However, they continue to be wary of complex projects with inappropriate risk transfer.

As highlighted on the news recently, there are longer supply periods for bricks due to an increased volume of new house building and a lack of stockpiling. This, coupled with the shortage of available bricklayers, may lead to reconsideration of materials on some projects. The cost of securing and retaining bricklayers is becoming an issue for many housebuilders, with a number of major sub-contractors only considering work of a simple nature and at inflated costs.

🚩 In the previous quarter, we reported on a busy construction market in the North East, driven by new build residential housing and student accommodation schemes.

Alex Halliday

Reporting on the North West Region

Construction activity in the North West remains strong. The tower crane count particularly in Manchester is high with significant activity in the residential sector. It is anticipated that this sector will continue to remain strong with numerous schemes in the planning pipeline and pre-planning appraisal stage at the current time.

The education sector also remains busy with John Moores, Manchester Metropolitan University and the University of Manchester all having significant schemes in the pipeline and on site.

There are a considerable number of opportunities arising post-Grenfell, with building owners/landlords considering re-cladding schemes to irradiate ACM cladding panels.

The £1bn St John's development in Manchester is due to start construction later in the year. It is highly likely that labour shortages will increase and subcontractor tender pricing will be less competitive once construction begins in earnest.

🚩 In our previous quarterly report, a declining pool of subcontractors (due to increased bankruptcies) were driving up costs and the volume of work was limited.

Steve Green

Reporting on the Yorkshire & Humberside Region

The construction industry in the Yorkshire and Humber region remains buoyant, particularly with regards to higher education projects. There is also a marked interest in the hotel sector with the emergence of both refurbishment and new build schemes. A range of healthcare projects are progressing under the P22 procurement route.

Clients remain risk averse and continue to focus their attention on diligence undertaken in contractor procurement and selection. Contractors are becoming more selective in their interest and their focus remains on working in local regions where they are supported by a strong supply chain of key sub-contractors.

Brexit uncertainty weighs heavily on some construction sectors with projects being cancelled in some cases. Furthermore, it is anticipated that the increase in the Bank Rate will affect investment decisions based on borrowing and interest calculations.

Looking forward, HS2 represents a catalyst for long term decision making, highlighting opportunities for key areas of development in local planning policy.

🚩 In the previous quarter, the construction industry in the Yorkshire and Humberside region was reported as being buoyant, driven by education and health sector works.

Regional Reports



30 Old Bailey & 60 Ludgate Hill, London

Richard Hine

Reporting on the South East Region

Construction activity within the South East region has seen a slight slowdown in general housing activity. A more concentrated effort is being placed on the private house building sector as house builders recognise the bigger returns on revenue in the short term. Residential is still the busiest sector in terms of construction activity within the South East in the last quarter.

Private commercial and infrastructure projects still experience a modest pace of growth and activity. The impact of the London market is continuing to have an impact on tender prices which is reflected in the general level of number of tender returns. It is being reported that there is a slight stalling in activity due to planning and other red tape issues.

The demand on house building is leading to material and labour shortages in some trades which have high domestic demand. It is noticeable that commercial-only trades are not affected by this and prices for those trades remain competitive.

Brexit and the resulting political uncertainty remain an influence on the larger private sector projects whilst public sector and smaller private sector projects are progressing. This uncertainty weighs heavily on investors who are choosing to defer decisions at this time. Those projects affected by the Brexit vote remain on hold with little sign of any change in the near future.

In our previous quarterly report, a busy house building sector in the South East region was driving growth, although a lack of confidence was impacting on larger longer-term projects.

Matthew Quirk

Reporting on the South West Region

Within the last decade the economic profile Bristol has outpaced many other UK cities. Growth continues to be driven by demand from the city's large student population, its diverse economy, and a strong programme of city centre regeneration.

The delivery of housing continues to rise and is now at its highest level in the last seven years. Even so, demand still significantly outstrips supply, which is impacting housing affordability.

A positive relationship between the councils in the West of England Combined Authority is fundamental in driving continued growth. This is particularly the case in their support of edge of settlement development. Whilst the city centre remains a key focus for housing delivery, competition from other sectors (notably student accommodation) will inevitably require an increased density of dwellings if schemes are to be commercially viable.

High demand and the loss of stock through change of use is putting pressure on the city's office supply. At the end of Q1 2018 there was less than 500,000ft² available to let (less than 5% of the total stock). As a result, record rents are under offer.

Bristol is still waiting to hear whether it has been selected as a hub city for Channel 4 and a positive decision could spark another wave of businesses basing themselves within the city, providing an extra lever for growth.

There appears to be a generally held opinion that the construction and property sector will be negatively impacted by the Brexit process.

In our previous quarterly report, the South West region was enjoying a surge in student accommodation projects, although increasing material prices were becoming a concern.

Acknowledgements

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BCIS All-in Tender Price Indices
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Inflation Report, Bank of England
Labour Market Statistics, Office for National Statistics
Output in the Construction Industry, Office for National Statistics
RICS UK Commercial Property Market Survey
RICS UK Construction & Infrastructure Market Survey
The Glenigan Construction Index

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Key

ONS: Office for National Statistics

HM Treasury: Her Majesty's Treasury

BCIS: Building Cost Information Service

RICS: Royal Institution of Chartered Surveyors



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