Southern Construction Framework

Market Intelligence

Q2 2024

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Introduction

As part of SCF's commitment to collaboration and transparency, every quarter, SCF main contractors gather market intelligence from the construction industry directly through their trade supply chains. Our intelligence analyses data across 11 key trade packages from across the south of the UK, identifying regional market trends and forecasts for the following year.

Professional consultants from the SCF Consult framework also share their valuable monitoring of the construction market and provide supporting commentary on the returned data.
Data for this report has been formed from over 150 subcontractors from across the south of the UK, providing a real-time indication of market trends from those directly involved with construction. We share this information with our clients to highlight key areas of risk that may impact on project delivery.

SCF Main Contractors, Consultants, and Clients can use this information to predict pressures and opportunities in the market, to make decisions about material specification, construction methodology, off-site or automated construction techniques and project planning and programming, ensuring the best possible decision making to deliver maximum value.

Foreword

In the face of ongoing challenges driven by fluctuating outputs and evolving market dynamics, M&E packages are playing a critical role. Despite a 1.4% decline in overall construction output in April 2024 compared to the previous year, driven by reductions in new work and maintenance activities, there has been a notable 3.02% increase in tender workload for trade subcontractors in Q2 2024. This highlights a significant disparity between tendering activities and actual construction output.

M&E packages, which account for a substantial portion of construction costs, continue to face challenges such as high-profile insolvencies, a shortage of skilled labour, rising copper prices, and increasingly complex specifications. Mace suggest that changes in typical specifications, driven by stringent environmental and quality requirements, are adding to the complexity of M&E solutions, in addition to increased use of PV, air source heat pumps, ground source heat pumps, and mechanical ventilation.

Feedback from main contractors also indicates that insolvencies within certain packages have led to a reliance on trusted suppliers for pricing works. This has resulted in individual suppliers, especially those working with multiple main contractors, being asked to tender for more projects than they might have in a more stable market.

As the industry moves forward, it is crucial for project teams to engage early with specialist supply chains to incorporate their input on buildability, value engineering, and specialist design work. By agreeing on design fees, and committing to partners, project teams can enhance cost certainty and overall buildability.

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Tender Workload

Data from the ONS indicates that in April 2024, Great Britain's construction output fell by 1.4% when compared with the previous year, driven by declines in new work and repair and maintenance. This has been further observed throughout Q2 (April-June), with construction output falling by 0.1%, this was driven by a decrease in new work (-0.5%).

However, trade subcontractors reported tender workload to be 3.02% greater in Q2 when compared with the same time last year, showcasing a deficit between the rate of tendering and construction output.

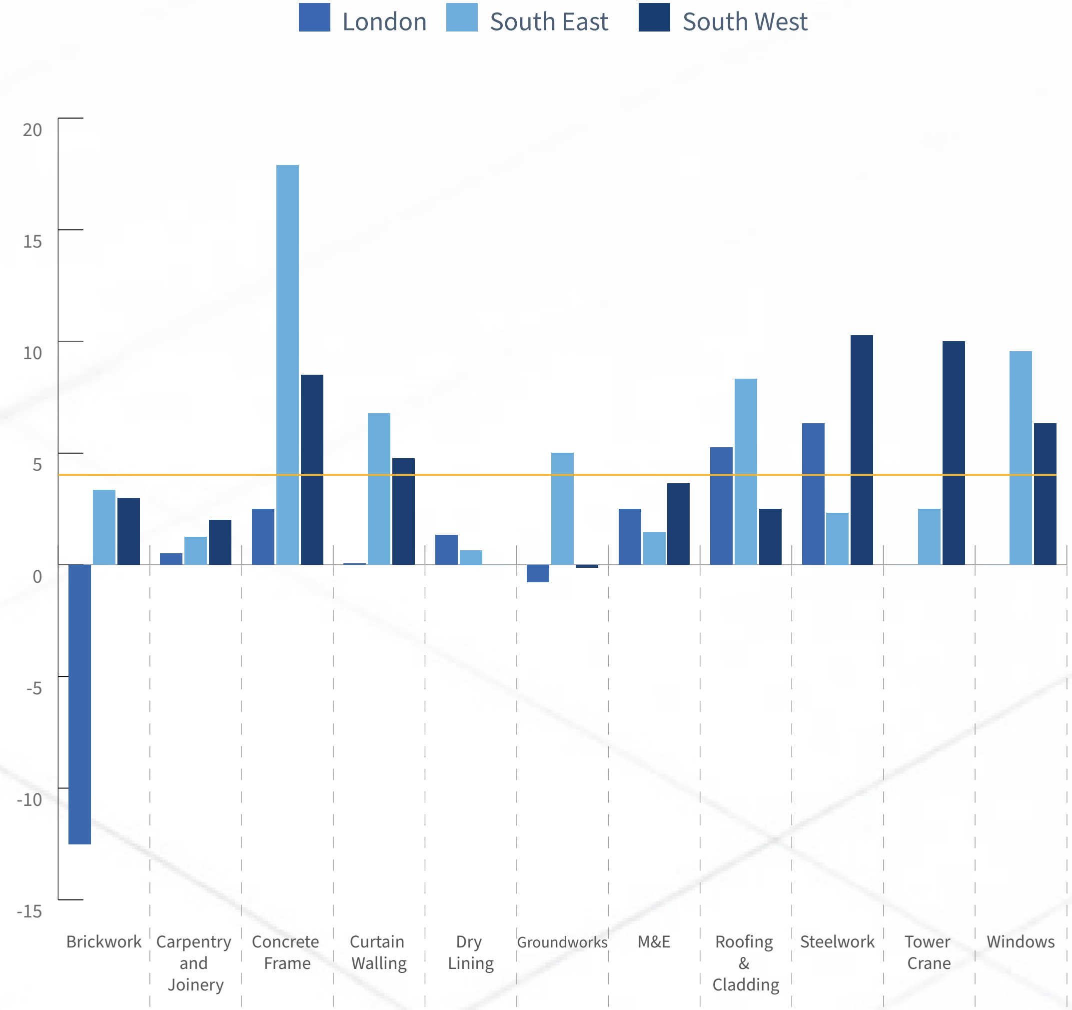
Anecdotal evidence from main contractors and their trade suppliers suggests that subcontractors are being asked to revisit previous tenders in the search of cost savings and specification adjustments as past hyperinflation has led to outdated budgets. As a result, this may be driving tender workload across the industry but not necessarily resulting in an improvement in output.

In addition, feedback from main contractors indicates that in some packages, insolvencies have meant that trusted suppliers are being relied upon heavily for pricing works, and therefore individual suppliers, particularly those that work with multiple main contractors, are being asked to tender for more projects than they might have been in a more stable insolvency market.

Throughout Q2, tender workload increased by 3.78% when compared to the previous quarter (Q1). The trades with the largest increases were:

- Concrete Frame (11.67%)
- Windows (6.81%)
- Steelwork (6.71%)

Tender Workload % Change since Q1 2024



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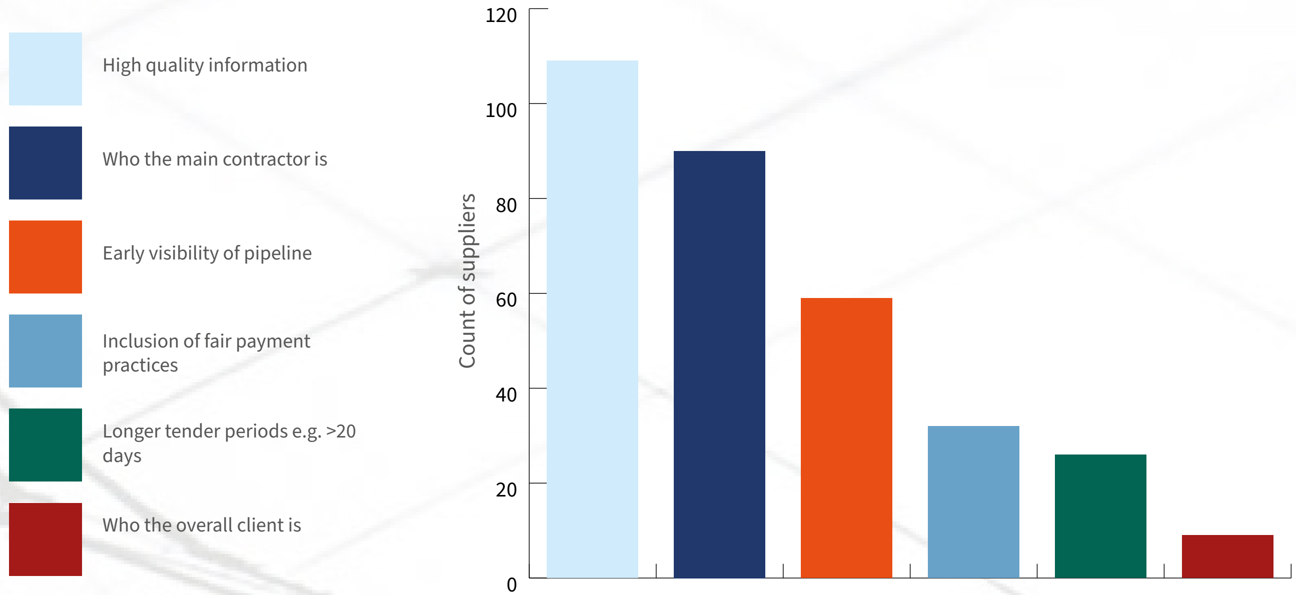
Supply Chain Health

As of May 2024, the ONS reported 4,287 construction firms faced insolvency, a 1.9% increase compared with the previous year (May 2023). Main contractors have responded by diligently investigating business histories through accreditation services. To enhance risk management, contractors also maintain close relationships with suppliers and monitor on-site indicators, such as shifting labour patterns, which serve as early warnings.

Last quarter, feedback from SCF's Supply Chain Survey highlighted an adversity to risk amongst subcontractors, with a reluctance to grow their businesses, but rather looking to prioritise stability through selective tendering and certainty of profit margins. This raises the question - what can project teams do to attract high quality supply chain?

Driving Factors for Tendering



In Q1, we observed that the quality of information provided at tender was the most frequent factor in dictating a subcontractor's choice to bid. To overcome this, project teams should look to benefit from early engagement with specialist supply chain, this way their input on buildability, value engineering, and specialist design work can be incorporated.

However, with elongating preconstruction programmes and with some projects not progressing to site at all, as of late some supply chain partners are hesitant to commit resource to extensive early engagement and multiple iterations of pricing. A potential solution lies in undertaking mini competitions for key supply chain partners during the earlier project stages, agreeing supply chain design fees and committing to partners to improve cost certainty, buildability and support with VE solutions where required.

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Building Cost

The rise in building cost has slowed, with Q1 marking the smallest quarterly fluctuation seen in the past four years (1.47%), suggesting a return to pre-pandemic stability. Similarly, national inflation (CPHI) reduced from 4.2% in January to 2.8% in June. This slowing in cost is helped by the cooling of material prices, data from the Department for Business and Trade reported average material prices for All Work to decline by 2% in the 12 months to May 2024. This decline is particularly evident in steelwork, most notably in the South East Region whereby structural steel and rebar have experienced a significant drop.

Quarterly Change in Building Cost (%)			
Q3 23	Q4 23	Q1 24	Q2 24
2.5	2.3	2.3	1.47

While the rate of increase has slowed the trades with the largest increase this quarter include:

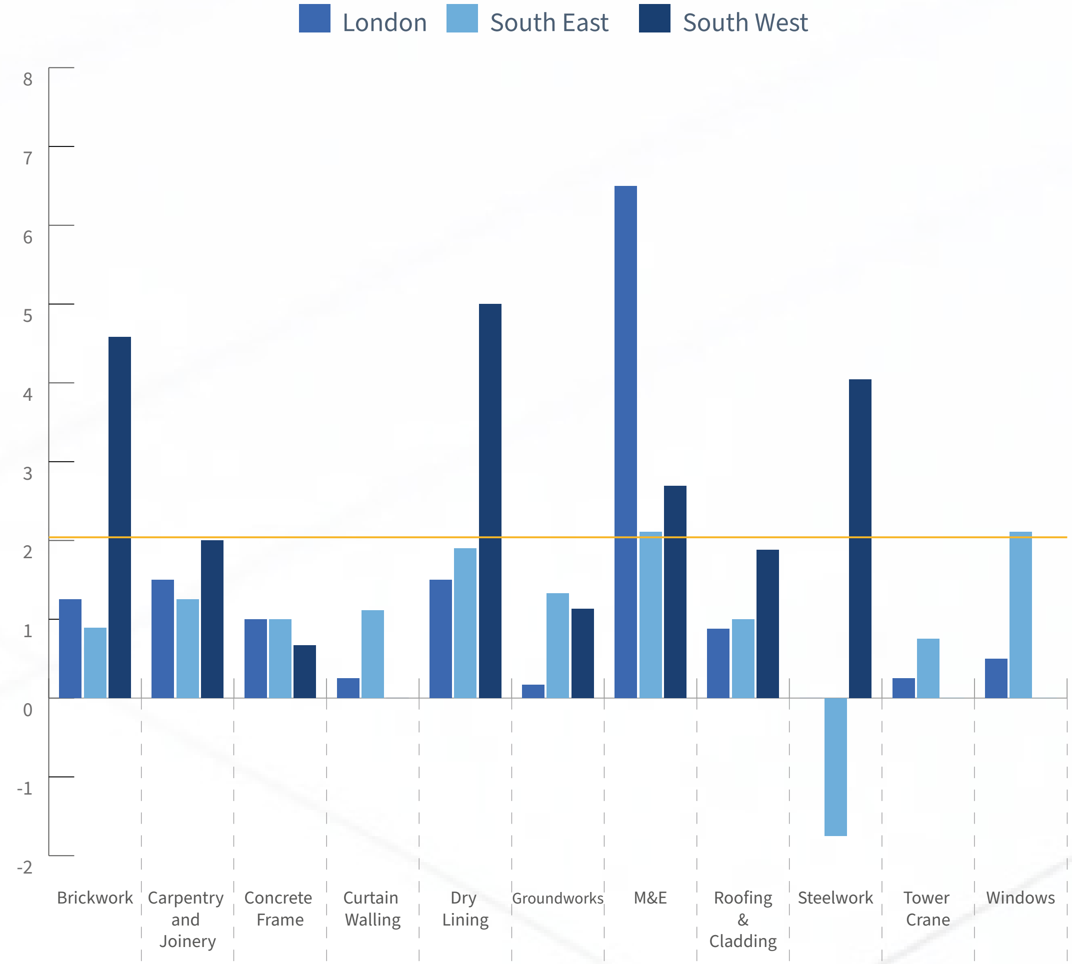
- Drylining: 3.02%
- M&E: 2.95%
- Brickwork: 2.37%

In addition, average building cost was still 3.79% greater when compared with the same time last year. Trades with the largest increase throughout the year include the following:

- M&E: 7.01%
- Brickwork 6.32%
- Roofing & Cladding: 6.20%

With some trades reporting a rise in build cost that exceeds inflation (2.8%), suggests that some trade packages may still be impacted by material prices and labour pressures.

Building Cost % Change since Q1 2024



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M&E

M&E is often a critical package for projects, responsible for a high proportion of the construction cost (average of 19.6% of contract sum). As a result, any unexpected escalations can often place significant pressure on project affordability. It is of utmost importance that cost escalations are well understood and predicted. In examining the escalation costs for M&E this year, several factors appear to play a significant role.

High Profile Insolvencies & Sustainable Bidding

Pre-Covid, many supply chain worked to unsustainable rates and the market has seen numerous high-profile insolvencies, however, firms report that the competitive nature remains. Nevertheless, insolvencies have strained supply chain, with businesses having to absorb costs lost through administration of tiered supply chain working beneath them. Thus, resulting in a smaller pool of their own specialists to tender works.

Consequently, supply chain partners are being more selective in the type of projects they tender as they can no longer afford to take on schemes with squeezed margins, project uncertainty or poor design. Many M&E companies are now pricing projects in such a way to ensure that their businesses remain sustainable and that they will be here for the foreseeable future.

Alongside fewer market participants, the view from many M&E contractors is there is enough work in the market. Technology and design quality has gone up, commonly requiring larger teams. Meanwhile, the jump in data centres and associated work has also helped firms spread risk by providing a new sector in which they can operate. All of these factors are boosting workloads and confidence, allowing M&E firms to set higher prices if and when they choose to tender.

Shortage of Skilled Labour

A well-documented shortage of skilled labour continues to drive labour costs in M&E packages. Two types of skilled workers where updated qualifications have had an impact on the market are for those involved in sprinklers and ductwork.

Copper Prices

The cost of copper continues to rise at a rate exceeding levels observed prior to the pandemic making predictability a challenge. A global increase in demand for data centres, electric vehicles, solar panels and wind turbines combined with a reduction in exploration, reserves, and new mines as well as a ban on Russian copper has consistently increased its cost. This has been particularly evident around products such as fittings and valves.

Increasingly Complex Specifications

Specialist M&E providers suggest that an increase in build cost may also be derived from a change in typical specification, particularly following stringent environmental and quality requirements.

Supply chains are seeing a rise in the use of PV, air source heat pumps, ground source heat pumps, and mechanical ventilation, all driving the complexity of M&E solutions. Such changes can also have knock-on effects, which are not always immediately clear. As an example, heat pumps typically require larger ductworks than gas boilers which can in turn change other design aspects. Similarly, accurately sizing basements, where many of these services are stored, is important and a source of risk.

In addition, fire regulations and local planning requirements have further tested the viability of schemes, with sprinkler systems, fire / smoke dampers, fire hydrant tanks, and electrical vehicle charging points being increasingly utilised. Changes to regulation are also pushing developers to scrutinise work more carefully, and design more exhaustively. Unsurprisingly, designing for the worst case has higher costs.

SCF Top Tip

The SCF process places emphasis on a mutually agreed procurement strategy and threads this throughout its governance, project teams should look to understand and agree risks and opportunities surrounding package procurement. Utilise supply chain databases, such as the Local Supply Chain portal, these can be used to robustly test the local market ensuring your procurement strategy provides maximum value and factors in supply chain resilience.

Try and de-risk the project so that the supply chain doesn’t pass such potential problems on through higher prices. As well as using a suitable procurement route and ensuring accurate drawings are available, potentially including appropriate indexing mechanisms to adjust for inflation and offering advance payments can help encourage tenders from the supply chain.

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Employment

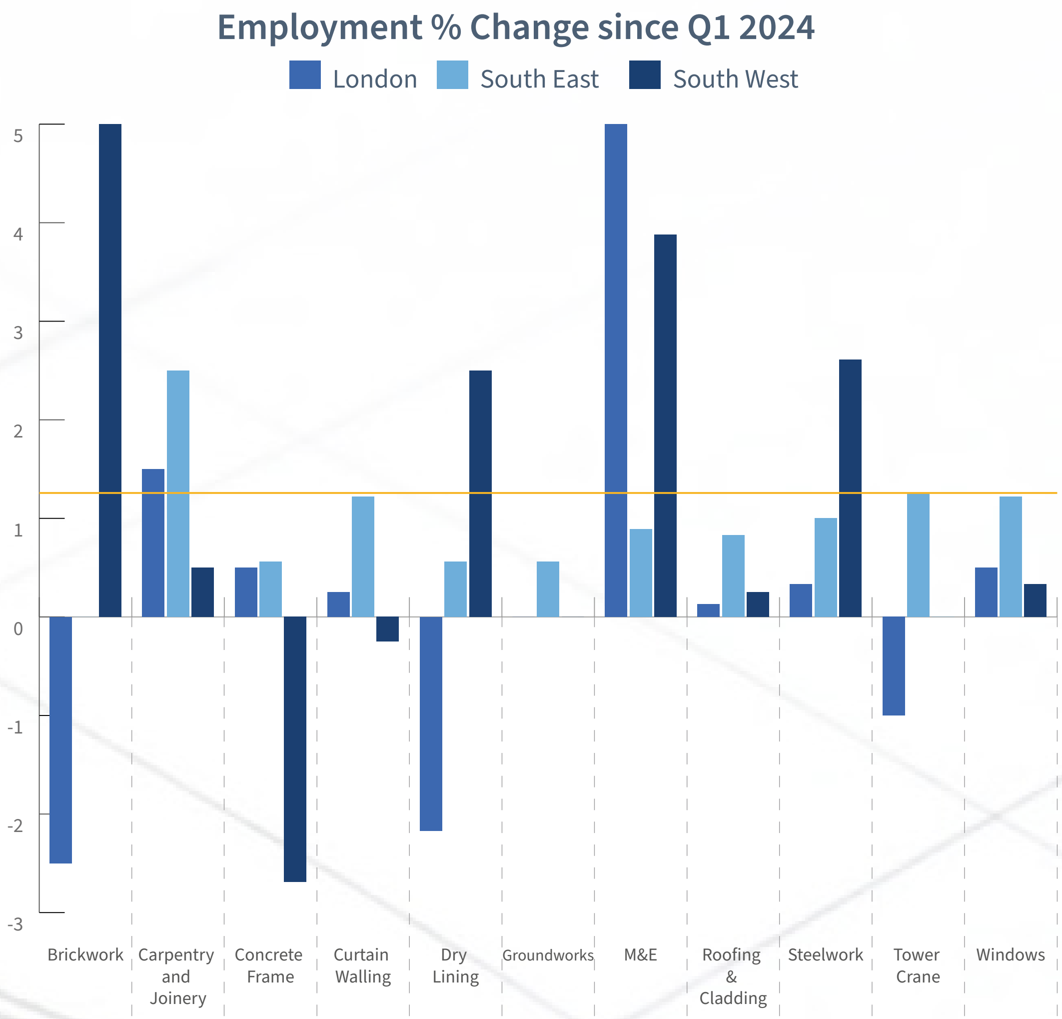
Over this quarter employment increased by an average of 0.7%, including a spike in M&E (2.90%) and Steelwork (1.44%). Similarly, when compared with the same time last year, employment increased by an average of 1.79%. A labour shortage amongst M&E providers is likely driving employment in attempt to improve much needed delivery capacity. In addition, the high number of insolvencies across the industry is resulting in the re-recruitment of workforce across businesses as firms collapse, as a result, our data may not necessarily represent an expanding workforce but rather a redistribution.

SCF Main Contractors have noted a shortage of skilled brick workers, particularly in the London region, with brickwork firms reporting an annual decrease in the number of employees (-1.76%). This could also be driven by a shift from brick facades to brick slips and other off-site solutions as projects attempt to improve their fire strategy.

SCF Top Tip

Forward visibility of pipeline is critical in helping subcontractors and their corresponding supply chain lock in hard to source labour. Clients should look to consider early engagement with suppliers in order to maximise opportunities for forward planning. SCF use a transparent portal, Local Supply Chain, to advertise its pipeline early in the project cycle directly to trade suppliers.

With the purpose of ensuring that the SCF helps contribute to the development of workforce and the promotion of the construction industry, an Employment and Skills plan is mandatory on every project. Take a look at our case studies to see our social legacy achievements.



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Material Availability

Currently, the availability of materials is relatively stable with no issues in predicting lead times at present. However, an upward trend in both M&E (+1.63 weeks) and Steelwork (+0.65 weeks) has been observed.

This increase could be attributed to 'seasonal' fluctuations in demand, influenced by large-scale projects like HS2. Moreover, this trend could potentially indicate that orders are being placed early or materials and plant resources are being secured in advance to mitigate anticipated price increases. For instance, British Steel announced a price increase of £30 per tonne at the end of June. Therefore, many companies may be trying to pre-empt cost fluctuations.

Additionally, it's worth noting that generators are now subject to longer lead-in times. This could have implications for project timelines and should be factored into planning and procurement strategies.

SCF Top Tip

Having a proactive approach can have significant financial benefits, allowing companies to lock in prices at current rates and avoid future cost escalations. However, it also requires careful planning and management due to the greater upfront investment and additional storage capacity requirements. Therefore, understanding and responding to these trends is crucial for maintaining project viability and profitability in the face of a dynamic market environment.

SCF Consult: Look Ahead

Two events over the past month provide some guidance about the short-term dynamics likely to affect the construction industry. While both are significant in their own right, neither suggest an instant change in direction. Firstly, a statement by Chancellor of the Exchequer Rachel Reeves underscored the challenges facing the government's fiscal position. Announcing an overspend of £22bn, she also cancelled several infrastructure projects and put others under review. Although the government is pressing forward with changes to planning, at least initially, there won't be any additional money for construction projects. A Budget is due to take place in October, and a long awaited Spending Review will be put forward next year. Both of these will provide greater detail about how Labour will govern over the next five years, but unfortunately, there is no new money immediately forthcoming.

The second significant event was the Monetary Policy Committee cutting interest rates on August 1st. Lowering them from 5.25% to 5%, this is the first move of what is likely to be a string of cuts. However, while monetary policy should continue to ease over the next 18 months, the Bank of England will take their time and go gradually. For construction, the housing sector is particularly sensitive to the Bank Rate, and it therefore cannot expect a swift recovery. With housing output still more than 20% down on its 2022 high, ongoing challenges facing the sector will persist. That they have started to cut rates is a step in the right direction, but as with the new government, it is too early to say the industry's headwinds are over.

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Looking ahead

Understanding trends and their implications is crucial for navigating the competitive landscape of the construction industry. As the industry evolves, staying informed and adapting to changing dynamics will be key to success.

Glenigan predicts a progressive acceleration in growth towards 2% per annum over the next few years leading into 2025/2026. This growth is expected to be driven by various factors, including political changes and industry adaptations.

The recent political change, which introduced a new Labour government, has brought about significant changes to the construction industry. The government has pledged to deliver 1.5 million homes in England over the next parliament, increasing workload across the industry.

Growth is also forecasted in the private residential sector by mid-2024, increasing the demand for brickwork. Having awareness of this helps construction firms plan supply, workforce, and pricing. Moreover, increased demand could potentially allow for higher prices which is forecast over the next year.

Tender workload

Over the next year, tender workload is expected to increase by an average of 5.82%. The trades with the largest forecasted increase include:

- Brickwork: 8.17%
- Windows: 8.21%
- Curtain walling: 8.61%

The rise in Brickwork can be attributed to the anticipated recovery of the private residential sector.

Employment

Trade subcontractors forecast a 3.24% increase in the number of their employees over the next year, with the following largest increases including:

- Groundworks: 5.28%
- Tower Crane: 4.17%
- Brickwork: 4.03%

Building Cost

SCF Main Contractors and their trade supply chain forecast an increase in building costs of 3.78% by Q2 25. The trades anticipated to be most impacted by this increase include:

- Steelwork: 6.06%
- Brickwork: 5.46%
- Carpentry and Joinery: 4.73%

Material Availability

Over the next year, the availability of materials is set to increase by 0.55 weeks The biggest areas of increase are likely to be seen across the following trades:

- M&E: +1.50 weeks
- Carpentry and Joinery: +1.21 weeks
- Tower Crane: +1.00 weeks