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RIDER LEVETT BUCKNALL TENDER PRICE FORECAST UK

Q3 2018

Q3

Rider Levett Bucknall

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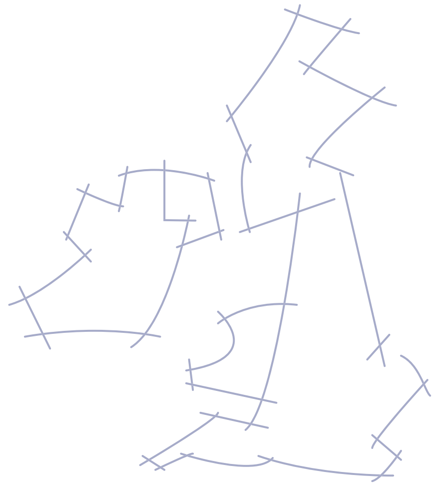
The RLB Tender Price Forecast looks at the movement of tender prices across the UK, reflecting on how construction markets are developing and providing insights on where they are going.



ECONOMIC OVERVIEW

Overall, UK GDP rose by 0.4% in the quarter to June 2018, after a fairly flat first quarter.

Growth was driven predominantly by services, mostly retail, due to the good weather. Meanwhile, the national Consumer Price Index recorded an uplift of 0.86% in the first half of the year, against a 5.6% uplift in labour costs in 2017.

The recent 0.25% rise in the interest rate reflects the surge in labour costs, together with rising costs of imports due to the weakened pound, and increases in energy and fuel costs. Moreover, there may be more in the way of interest rate rises to come, as the Bank of England recognises the fact of unemployment being at a 40-year low and wages increases largely defining the trajectory of inflation.

In construction, ONS is reporting 2.5% labour cost increases in their latest half year figures, with 8.5% on the whole year, far outstripping the general economy and demonstrating the labour issues faced by construction. Over the whole economy, wages growth has slowed in the second quarter, yet has still remained in positive territory.

After a weak first quarter, construction output returned to growth of 0.9% in Q2, against the fall of 0.8% in Q1, likely due in part to the contrast between the poor weather of the earlier part of the year and the later conditions. Although this is encouraging, the bulk of the gain was due to increase in maintenance work, with new work output being relatively flat. At the time of writing, CPA is forecasting an overall fall of 0.6% in construction output in 2018, with a rebound of 2.3% growth in 2019. BCIS meanwhile is showing an upside forecast of +5.5% new work in 2018, set against the other end of their range, a downside forecast of -9.9%. Given the overall situation as at the mid-year point, the actual performance level may be set to be more central, perhaps biased toward the upside BCIS forecast.

In common with labour costs, construction materials prices showed above-CPI increases of around 3% for the first half of the year. Headline movers were imported plywood (up 17%) and timber generally (up 5-7%).

If you'd like to find out more, please get in touch:

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LONDON

TENDER PRICE FORECAST UPLIFT PERCENTAGES

		%					
SOURCE	REPORTED	2017	2018	2019	2020	2021	2022
RLB (London)	**Q3 2018**	**2.00**	**1.25**	**1.00**	**1.50**	**2.00**	**2.75**
Others - Upper range (London)	Q1 2018 - 2Q 2018	2.75	2.30	2.60	5.00	4.00	4.00
Others - Lower range (London)	Q1 2018 - 2Q 2018	1.50	1.00	0.50	1.00	1.50	2.00
BCIS (National)	Q3 2018	14.89	-2.78	3.81	3.98	5.88	5.83

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Despite reported levels of weakening confidence as a result of Brexit, it remains our view that the long-heralded "Market Reset" is, to some degree, being counter-balanced by issues such as the risk of a reduced labour supply, a weakened pound and the on-going requirement for residential development in London and the South East.

There are large numbers of sizeable long term construction projects ongoing across multiple sectors throughout the London market, with a cumulative construction cost in excess of £20 billion. Examples include Crossrail, the multiple phases of Battersea, commercial towers in the City, One Lansdowne Road, HS2 and the Thames Tideway Tunnel. These projects, together with the underlying development activity, are weighing and will continue to weigh heavily on supply chains. As a result, workload in the capital remains solid.

Across the sectors, in London the move to online shopping is noticeably shrinking the retail industry. As a downstream effect, RICS surveyors are predicting a consistent increase in retail vacancy rates over the next year. Conversely, demand is consistently high for office space, with vacancy rates at a low, 1-2%.

In the Industrial sector, construction activity continues to grow, from the small "starter/ trade counter" size projects right up to the larger 1 million ft^2 plus units. This is in response to a combination of speculative and end-user-driven demand, with on-line/logistics clients to the fore.

An increase in available capacity in the Tier 1 contractors' order books will bring competitive pressure to bear on their peers as well as those in Tier 2.

Materials price increases in steel, concrete and aggregates are starting to filter through to tenders, however contractors are offsetting these increases where possible, to remain competitive and to retain market/client share.

Despite this elevated level of competition, strong demand for specialist sub-contractors e.g. cladding and steel frame, is resulting in elongated lead-times and the need to reserve fabrication slots earlier in order to meet programmes.

The London construction sector's continued reliance on EU workers remains a concern, the effect of which will only really be known when the deal to exit Europe crystallises.

BIRMINGHAM

TENDER PRICE FORECAST UPLIFT PERCENTAGES

		%					
SOURCE	REPORTED	2017	2018	2019	2020	2021	2022
RLB (Birmingham)	**Q3 2018**	**2.80**	**2.50**	**2.25**	**3.25**	**4.00**	**4.00**
Others - Upper range (Birmingham)	Q1 2018 - Q2 2018	2.50	2.50	4.00	4.00	5.00	2.00
Others - Lower range (Birmingham)	Q1 2018 - Q2 2018	2.50	1.00	1.50	1.50	2.00	2.00
BCIS (National)	Q3 2018	14.89	-2.78	3.81	3.98	5.88	5.83

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There is much construction activity on site in Birmingham and some exciting and significant pipeline. Set against this is a cautious outlook, with the fear of short term uncertainty slowing projects down.

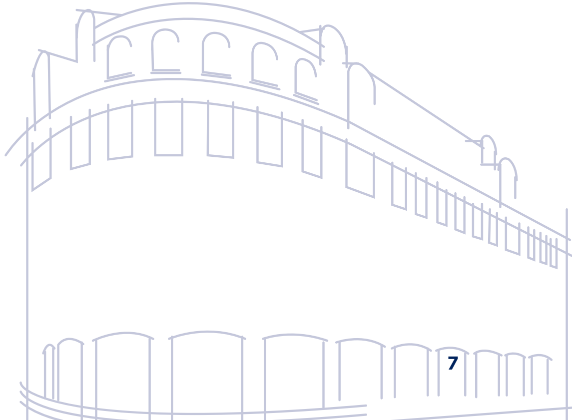
Naturally, the major talking points are the effects of Brexit; whether and if they will impact upon construction in the Midlands. Impacts are being felt in some sectors, with economic uncertainty affecting confidence. This is particularly the case in the automotive sector, which is doubly affected, feeling also the strain of uncertainty over future policy outcomes in relation to use and/or design of diesel engines.

At another level, Brexit discussions are stifling development of other areas of government policy. With not much legislative time for major policy advancements, works in the health, custodial and residential sectors are progressing with the preservation of the status quo. On the ground, retail remains a fragile sector, with recent and ongoing casualties on the high street. However, set against all this turbulence, there are large commercial schemes underway at Arena Central, Paradise and Snowhill, in addition to similarly significant values of large residential projects.

While uncertainty is expected to continue into next year, reduced output may be the end upshot, even though input costs are rising. The inevitable outcome is margin compression on the part of both contractors and sub-contractors, with the attendant necessity of recovering expended-cost.

More positively, the work towards the 2022 Commonwealth Games is proceeding, as is the work in support of the higher education sector. The works surrounding HS2 are now getting underway, with ongoing design and early implementation works.

The overall result of this mixed bag of risks and uncertainties is that tender price inflation will continue to undercut general inflation, with input cost inflation likely to outpace them both.



BRISTOL

TENDER PRICE FORECAST UPLIFT PERCENTAGES

		%					
SOURCE	REPORTED	2017	2018	2019	2020	2021	2022
RLB (Bristol)	**Q3 2018**	**2.50**	**3.00**	**3.00**	**3.00**	**3.00**	**NP**
Others - Upper range (Bristol)	Q1 2018 - Q2 2018	2.60	2.00	2.75	3.75	4.50	2.00
Others - Lower range (Bristol)	Q1 2018 - Q2 2018	2.60	0.50	0.50	1.00	1.50	2.00
BCIS (National)	Q3 2018	14.89	-2.78	3.81	3.98	5.88	5.83

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Bristol's market is continuing along its buoyant route, with a large number of projects on site and a strong pipeline of projects working their way through planning and coming to tender.

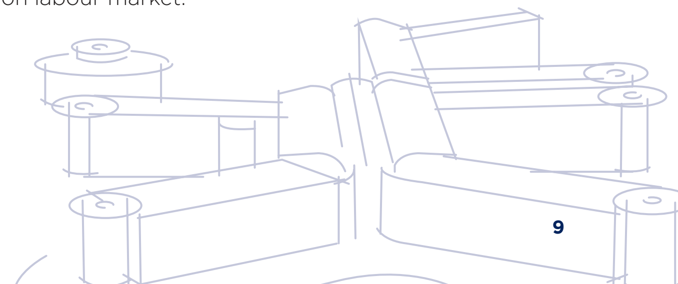
Any "Hinckley effect" is still absent from the Bristol market, in that the advent of the major Hinckley project does not appear to have significantly affected the building market. A part of this may be due to the fact of Hinckley being a large-scale engineering project rather than a building project, and drawing from a labour pool having a different, specialist skills-set applicable more to civils work. However, it is also true that the labour market in building is feeling the strain, as supplies of skilled and unskilled labour have little spare capacity. That shortage is also lapping over into the consulting, architecture and engineering professions, where levels of staff turnover are significantly above norms.

For their part, contractors are generally busy, which is resulting in a selective approach to project tendering, with avoidance of risk, and price risk in particular, prevalent.

Looking at sectors in the market, the residential space is extremely active, with major and heavily labour-intensive projects on-site throughout the region. The residential industry covers everything from small-scale unit construction right through to multi-storey apartment building, and all are active. In particular, the University sector is in the process of providing for the new campus at Temple Quay and the associated accommodation and infrastructure. Inquiries regarding development costings from both the private and quasi-public sectors are at their highest levels in ten years, suggesting a pipeline of work stretching out toward 2020. Even in the commercial office segment, there is some new-build and refurbishment activity in Bristol, where there has not traditionally been a strong office market component.

Beyond Bristol, the motorway corridors continue to attract construction of distribution facilities, down the M5 to Taunton, and on to Exeter and Plymouth, where the University sector is again experiencing abundant workload.

Overall, the market in the South West is nearing its current capacity bounds. The salient issues remain the Brexit outcomes of course, together with the related issue of labour force availability within the region, and in terms of the draw of the London labour market.



MANCHESTER

TENDER PRICE FORECAST UPLIFT PERCENTAGES

		%					
SOURCE	REPORTED	2017	2018	2019	2020	2021	2022
RLB (Manchester)	**Q3 2018**	**2.00**	**1.00**	**1.00**	**2.50**	**3.50**	**NP**
Others - Upper range (Manchester)	Q1 2018 - Q2 2018	2.50	2.50	4.25	4.50	5.00	1.75
Others - Lower range (Manchester)	Q1 2018 - Q2 2018	2.50	2.00	1.80	1.50	1.75	1.75
BCIS (National)	Q3 2018	14.89	-2.78	3.81	3.98	5.88	5.83

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The lively investment and development environment in and around Manchester is continuing to drive a healthy construction market, despite any uncertainties surrounding the wider political situation.

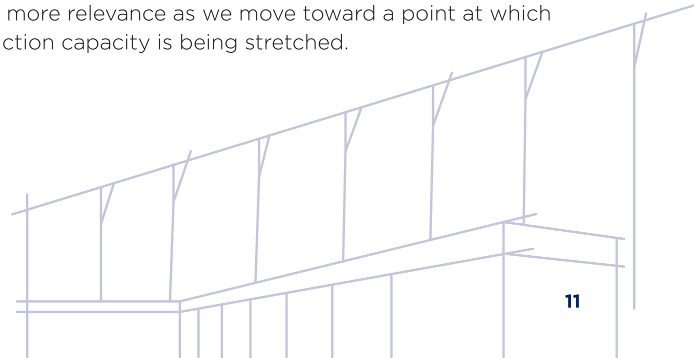
Given the ongoing growth of the higher education sector and the strength of the University-level sector in and around Manchester, there is pent-up demand for student accommodation, which the universities are looking to address over the next five years. The anticipated £2 billion spend suggests a strong pipeline of core major project works, which will form a useful basis on which Tier 1 contractors can frame their bidding strategies.

Set against that background of upcoming work, current major projects on-site remain dominated by the ongoing and upcoming residential projects, which will turn out in excess of 15,000 units over the next three years. This output is backed not only by the existing shortfall, but by strong population growth forecast for Manchester and its surrounds. Development in the residential sector will continue to feature strongly, as Manchester seeks to redress former under-investment in its housing and accommodation stock.

In similar fashion, the hotel and leisure sector continues to deliver new rooms, to support the lively Manchester commercial sector.

Looking to the wider market, the private sector growth mentioned in our last Tender Price Forecast is being enhanced by significant overseas investment from around the world, as well as local financing. The opportunity represented by the slowdown of commercial office development following the Global Financial Crisis is being exploited to some extent by plans for the construction on the former ITV city centre site, as well as NOMA and Salford Central.

An interesting aspect of the forecast strength of future workload is the prospect of a significant upturn in tender pricing, as is indicated in our tender price forecast figures, as multiple new major projects come to market in a fairly brief window of time. Planning of procurement programmes and timing of tendering and commencement on site will become of even more relevance as we move toward a point at which construction capacity is being stretched.



YORKSHIRE AND HUMBER

TENDER PRICE FORECAST UPLIFT PERCENTAGES

		%					
SOURCE	REPORTED	2017	2018	2019	2020	2021	2022
RLB (Sheffield)	**Q3 2018**	**2.00**	**-1.50**	**3.75**	**4.25**	**5.60**	**5.60**
RLB (Leeds)	**Q3 2018**	**2.00**	**-1.00**	**5.15**	**4.70**	**6.15**	**6.05**
Others - Upper range (Sheffield)	Q1 2018 - Q2 2018	2.40	4.00	4.00	4.00	6.00	1.50
Others - Lower range (Sheffield)	Q1 2018 - Q2 2018	2.40	1.00	1.00	1.00	1.50	1.50
BCIS (National)	Q3 2018	14.89	-2.78	3.81	3.98	5.88	5.83

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This edition of the Tender Price Forecast follows hard on the heels of RLB having opened their new office in Leeds in June, targeting further growth in the locality.

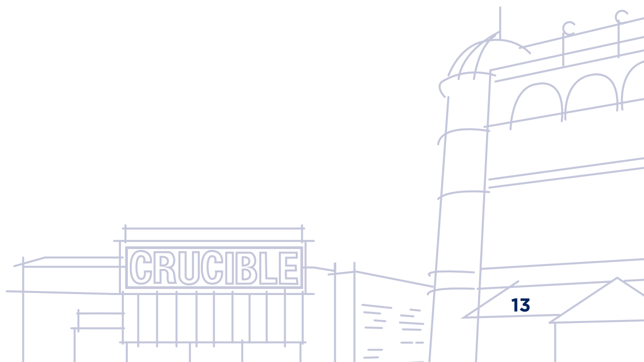
In the Yorkshire and Humber region, the residential and commercial sectors saw a notable upturn in activity during June and the near-term outlook also brightened. New orders are rising in volume at their fastest pace in over a year, while input buying is at its fastest pace for two and a half years.

Locally, materials costs are expected to rise 3-4% this year, through the normal inflationary effects married with the fall in Sterling affecting imports. A number of pinch-points have appeared in certain trades, masonry in particular, which is giving rise to cost spikes and availability concerns in some locations. In terms of labour costs, the principal unknown is the outcome of the Brexit question, which could result in significant labour shortages.

Activity levels are currently high and consistent across the RLB portfolio. Alongside existing workload, RLB is currently aiming to increase market penetration within the healthcare sector. Despite a challenging health economy, we are hopeful that further government investment will be made available to support the investment need, as populations age and medical needs change.

In the logistics sector, demand for space has increased 60% year-on-year, as online retailers look to procure storage and fulfilment developments that are in short supply currently. This demand has resulted in the construction of a number of large scale industrial units in the region, benefitting from the extensive motorway network available.

However, regardless of the above, tender prices are forecast to continue to fall until the third quarter of 2018, due to ongoing lack of confidence surrounding the UK's exit from the European Union. When the terms and timeline of Brexit are finalised, tender prices are expected to increase steadily due to increased construction output in the private residential, industrial, commercial and healthcare sectors, and due also to pent-up pricing pressures.



THAMES VALLEY

TENDER PRICE FORECAST UPLIFT PERCENTAGES

		%					
SOURCE	REPORTED	2017	2018	2019	2020	2021	2022
RLB (Thames Valley)	**Q3 2018**	**NP**	**2.00**	**1.50**	**2.50**	**2.50**	**3.00**
Others - Upper range (Thames Valley)	Q1 2018 - Q2 2018	2.50	2.10	3.25	3.50	4.50	2.50
Others - Lower range (Thames Valley)	Q1 2018 - Q2 2018	2.50	0.50	0.50	1.00	1.50	2.50
BCIS (National)	Q3 2018	14.89	-2.78	3.81	3.98	5.88	5.83

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The Thames Valley construction and property market remains strong despite Brexit-related uncertainty.

Key regional infrastructure schemes, including Crossrail, are affecting the wider construction market, while other transport links continue to create improved movement to both London and Heathrow. Links to and with London are an important component of the Thames Valley construction economy in terms of both the development market and supply chains.

Reading's market in particular, has to some extent already benefitted from the Crossrail stimulus and other related and parallel commercial development that has already occurred. The recent acquisition of the Station Hill scheme is an interesting move that could signal another key development.

In addition, many key regional regeneration and development schemes are already continuing toward fruition in, for example, Slough, Maidenhead and Oxford. This sustained activity level evidences the continuing trend of London-based developers in the residential and commercial sectors looking to more regional locations to find better-value opportunities. The residential sector (particularly regional house building) is currently very strong, with substantial schemes continuing to come through the pipeline now and for the foreseeable future.

Of just as much interest will be how the Heathrow third runway plays out from this point in terms of legal challenges, but if it does go ahead as planned it will further underpin elements of the development market.

In overview, the Thames Valley market continues to thrive, feeding from the live and ongoing infrastructure workloads and, in its own right, the strong development pipeline around the region. Improved transportation options will continue to give rise not only to distribution buildings opportunities, but to related business infrastructure developments and housing development.

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