

G&T M&E Contractor Survey
July 2023

 @gt_llp

 gardiner.com

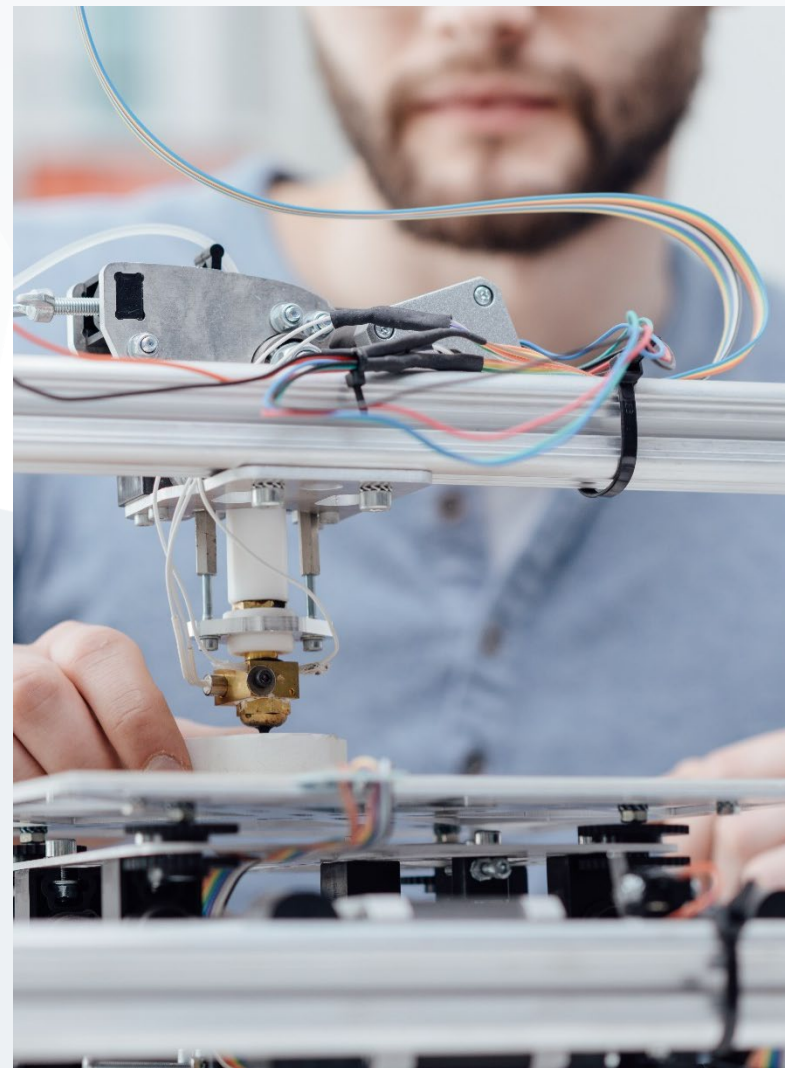
 marketintel.gardiner.com



G&T's M&E Contractor Survey summary for July 2023 analyses some of the key trends and themes generated from the responses of our most recent M&E contractor survey.

Financials	3
Secured Work and Lead Times	4
Typical Project OH&P and Preliminaries	5
MEP Tender Price Inflation Forecast	6
Market Pressures and Risks	7
Labour Rates and Resource Availability	8
Preferred Project Size	9
Successful Tender Ratio	10
MEP Products & Materials: Supply Issues and Lead Times	11
Inflation: MEP Products and Materials	12-13
Sector Split (Average and by Contractor)	14-15
General Market Feedback	16-17

Please note: Although survey respondents operate across all geographical regions of the UK, the majority tend to operate in Greater London and the South East.



G&T's latest survey of M&E contractors has provided valuable insights into the current state of the UK MEP market. While there has been some alleviation of price pressures since our previous report in November 2022, shortages of specific electrical components, labour availability pressures, and a busy MEP market all continue to weigh on pricing.

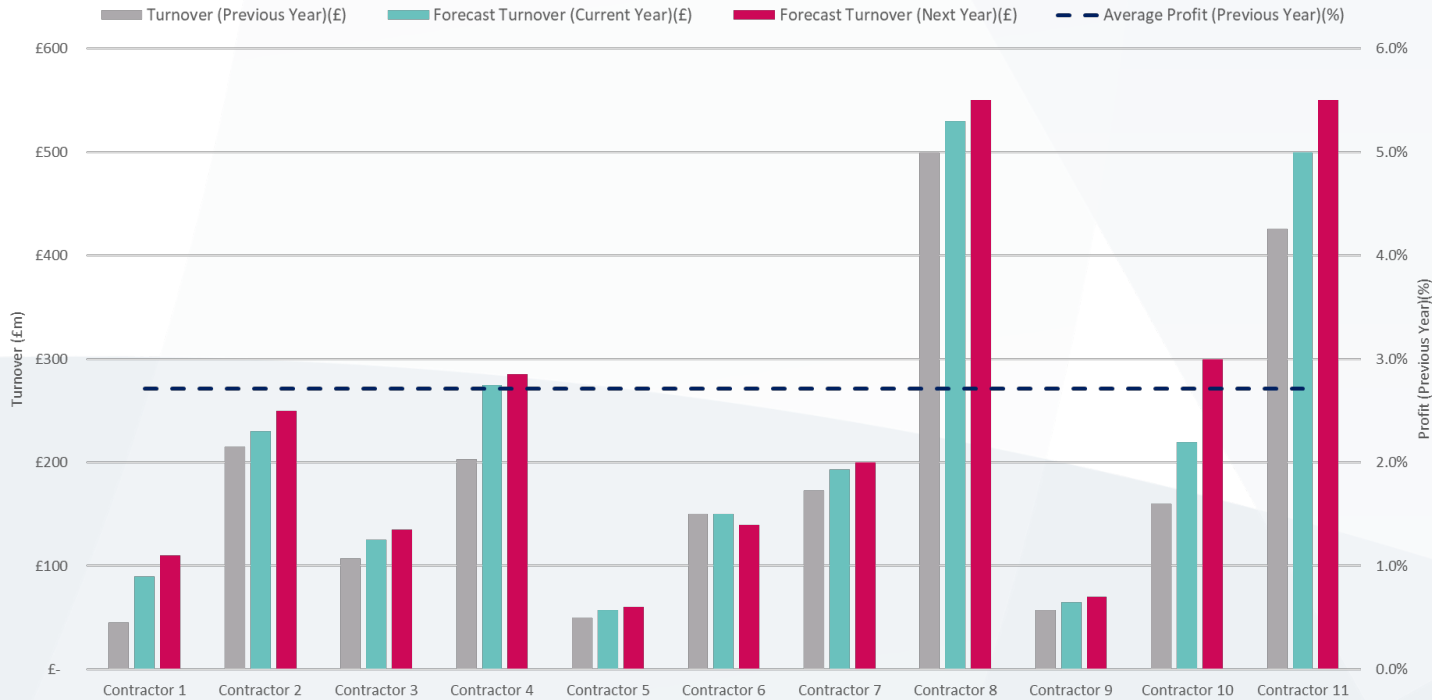
According to surveyed contractors, short to medium-term order books remain strong, but slowing new order growth may impact longer-term pipelines, creating more spare capacity. Delayed decision making due to stakeholders reassessing their requirements and seeking cost reductions in schemes has created some uncertainty in recent months. Many anticipate the rising cost of borrowing will impact client investment plans and hence future contractor workloads, but for now, the market is being sustained by strong new order growth from the past two years. The culmination of strong workloads and ongoing input cost pressures, meant contractors expect MEP tender price inflation to be 6.3% this year (2023), before easing further in 2024 to 5.4%.

MEP contractors will need to adapt to challenges such as skills shortages and the imperative of achieving net-zero carbon emissions. They will also need to redirect their focus towards high-growth sectors like Life Sciences, Data Centres, Pharmaceuticals, and Healthcare in the coming years. These changes will inevitably require adjustments to the business models of many MEP contractors, but the survey reveals that a significant number of respondents are already taking steps to meet these challenges.



Shortages of specific electrical components, labour availability pressures, and a busy MEP market all continue to weigh on pricing

MEP CONTRACTOR TURNOVER v. PROFIT



2024 Turnover forecast to increase by...

+8.8%

(on average, compared to forecast turnover for current year)

Average Profit previous financial year...

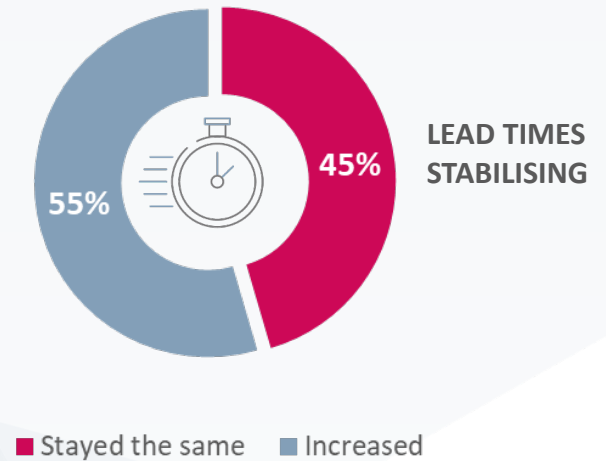
2.7%

(compared to **2.4%** in 2021)

- The average forecast turnover of surveyed MEP contractors for 2023 was £221 million – **16%** higher than the average figure in 2022 (£189 million)
- Contractors expect turnover will continue to rise but at a slower pace, **increasing by 8.8%** on average in 2024 compared to the current financial year
- An overwhelming majority of contractors (**91%**) anticipate that their turnover for 2024 will surpass their 2023 figures, underscoring the robust health of their order books
- Average profit in the previous financial year (2022) was **2.7%** - up from **2.4%** in 2021 but still down on 2019 average profits (**3.9%**)



MEP PRODUCTS/MATERIALS LEAD TIMES: PAST SIX MONTHS



*On average, contractors have secured **89%** of 2023 workloads and **58%** of 2024 workloads*

- All contractors have secured **80% or more of their 2023 workloads** but there is **greater slack/capacity in 2024**
- Short to medium-term **order books remain strong** but **slowing new order growth may impact longer-term pipelines**, creating more spare capacity

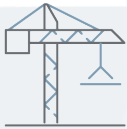
In contrast to many other construction materials, lead times for MEP products are still extended

- Items with **solid state chips** are experiencing long lead-in times, as are **ASHPs, switchgear** and **generators**

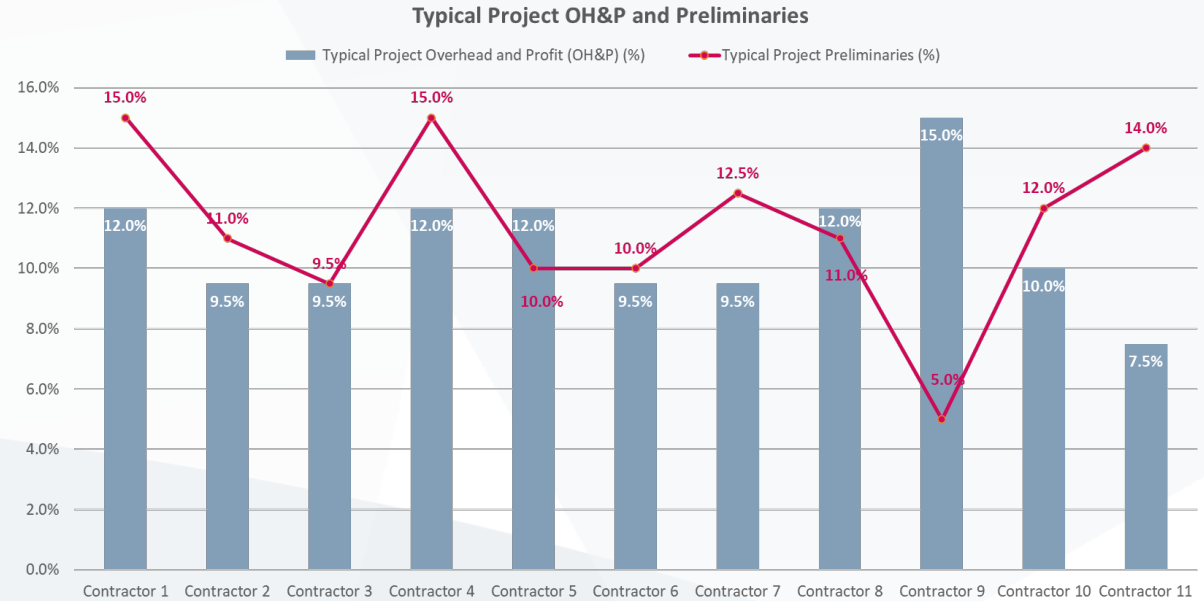
“Supply chains are not keen on issuing lead-in times as they are very much governed by their supply chain and the availability of necessary materials.”

TYPICAL OVERHEADS AND PROFIT (OH&P) RANGED BETWEEN **7.5-15%**, WITH AN AVERAGE OH&P FIGURE OF **10.8%**

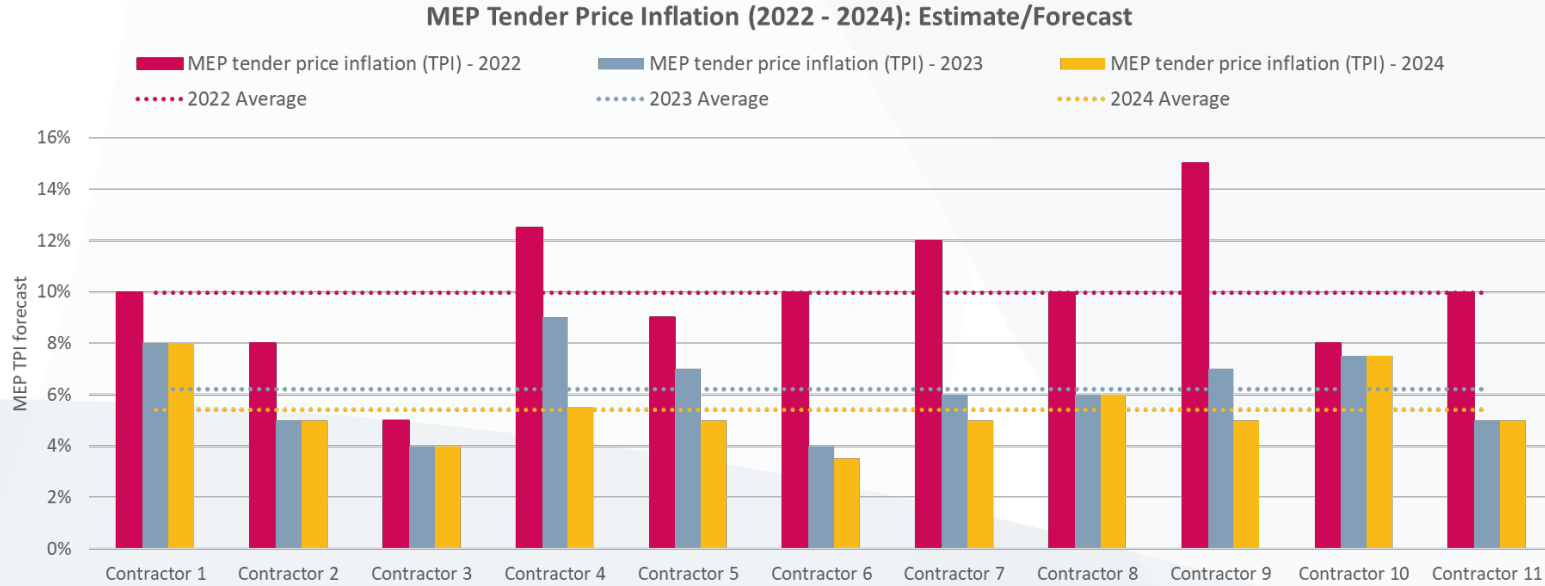
TYPICAL PROJECT PRELIMINARIES COSTS RANGED BETWEEN **5-15%**, WITH AN AVERAGE OF **11.4%**



Other pressures acting to increase OH&P and preliminaries costs include rising borrowing costs, higher insurance costs, sustainability measures and onerous Local Authority requirements. Contractors will naturally look to cover these additional costs by raising their preliminaries levels and OH&P.



- Average OH&P edged higher compared to [November 2022 M&E report](#) (from **10.4%** to **10.8%**) while Preliminaries costs rose from **10.6%** to **11.4%**
- Fixed energy-related factors/consumption on site, as well as staff wage increases continued to push preliminaries costs higher
- OH&P has remained more stable. With sustained workloads, contractors aren't yet being squeezed to reduce OH&P. However, easing new orders may create stiffer tendering competition and put some downward pressure on OH&P
- Many anticipate construction firms will have to compete harder for labour resource, potentially pushing preliminaries costs higher unless cooled by lower demand



Average MEP Contractor Forecast (2022)

10%

Average MEP Contractor Forecast (2023)

6.2%

Average MEP Contractor Forecast (2024)

5.4%

“Labour shortages are a real challenge and will become even more difficult...Certain trade packages with limited Tier 1 availability are also driving pricing. For example, sprinkler sub-contractors are extremely busy, forcing costs to rise”

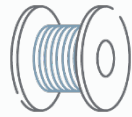
*This compares to a G&T MEP inflationary forecast range of **3-5%** over the next 12 months.

**Note: M&E tender price inflation forecasts/estimates can be influenced by a variety of factors, such as size of the contractor, its purchasing power and the type/size/value of projects the firm typically works on. The forecasts provided are solely those of the survey respondents and do not necessarily reflect the views or opinions of Gardiner & Theobald.*

Market pressures currently driving M&E prices...



Labour Shortages



Material Availability



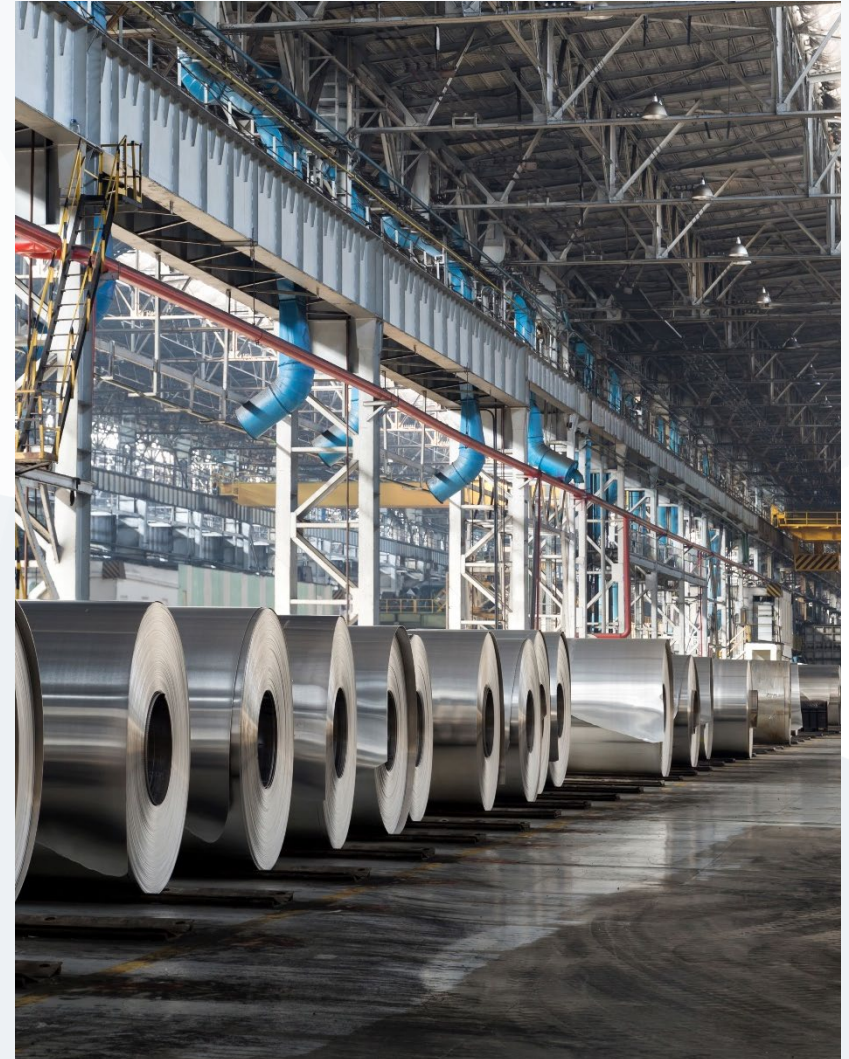
Volatile Market
Conditions



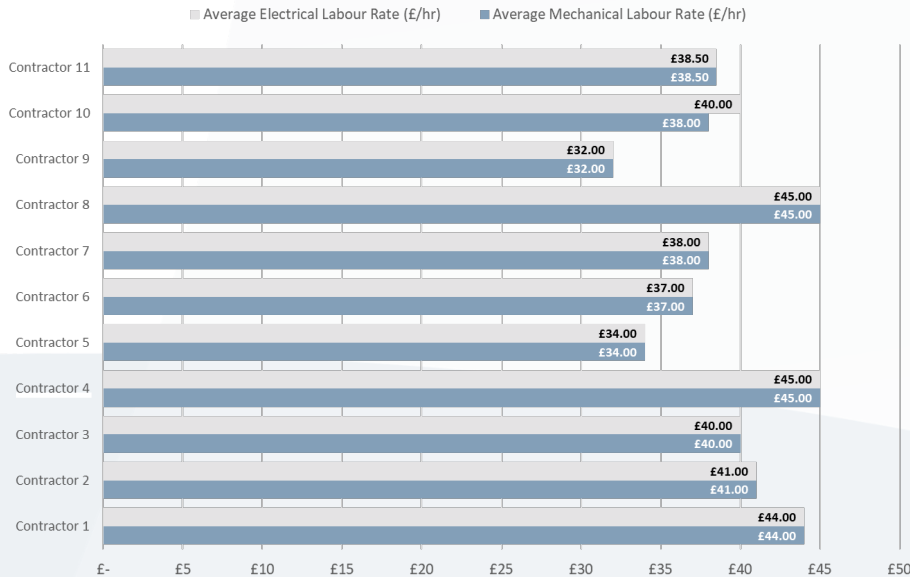
Trade Package/Sub-
Contractor Availability

Market risks for 2023/24...

- Fixing prices on packages with **limited numbers of contractors**
- **Lack of capacity** due to full short-term order books
- Pressure on rates due to **shrinking labour pool**
- Further inflation and **long lead times** on specific materials
- Cost of **borrowing** and **insolvency** of sub-sub contractors



Mechanical & Electrical Labour Rates (£/hr)



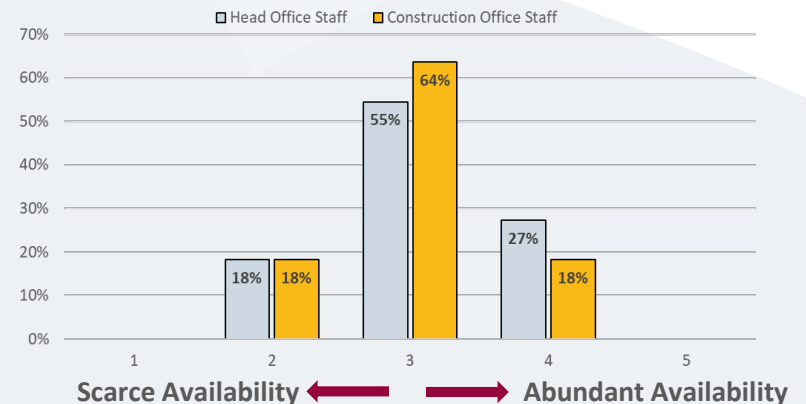
Jul 2023 M&E Survey:

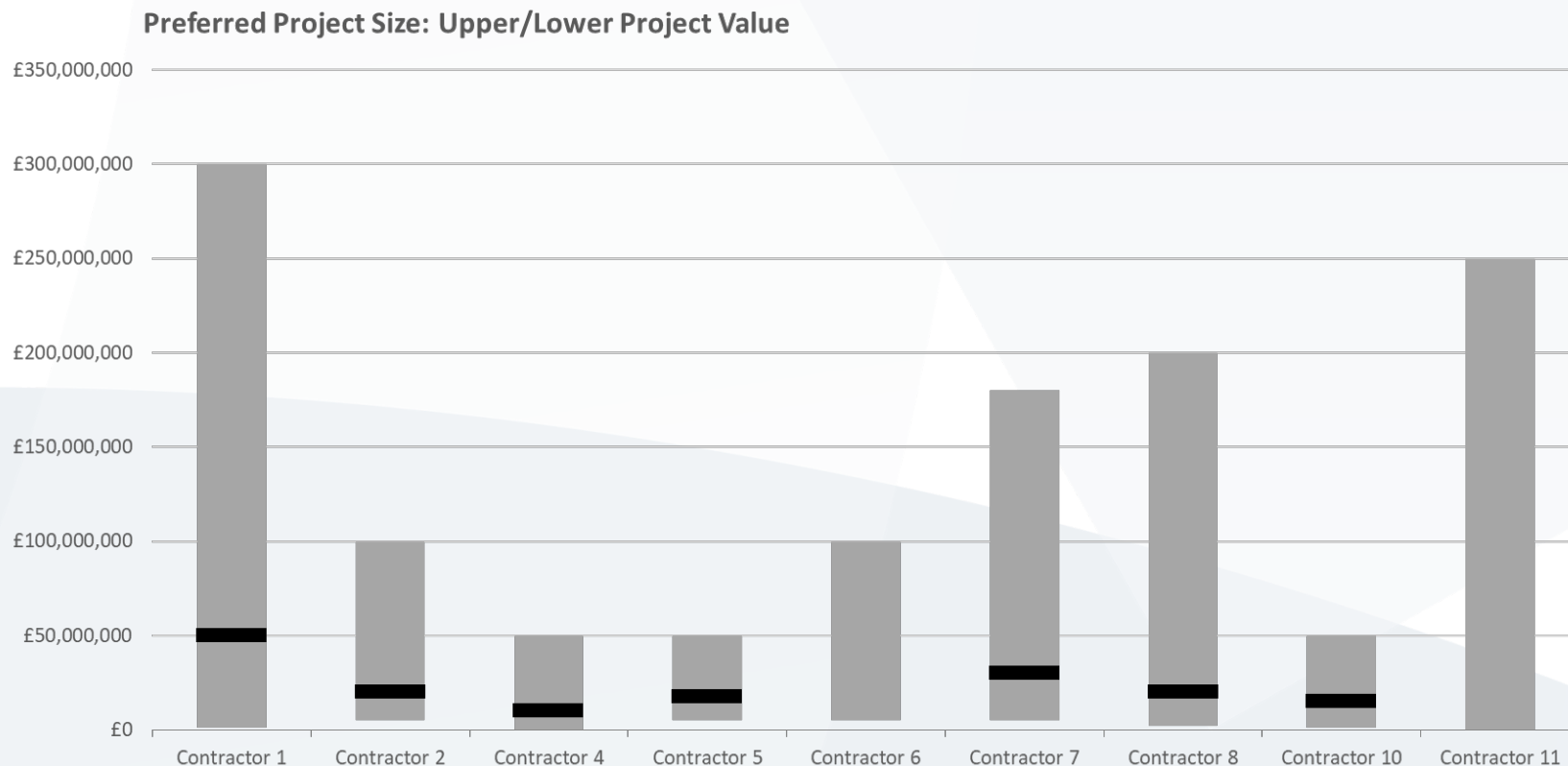
- **Average Electrical Labour Rate: £39.50 p/h**
- **Average Mechanical Labour Rate: £39.32 p/h**
- Compared to [G&T's Nov 2022 survey](#), average electrical labour rates have risen by **3%** while mechanical labour rates have increased by **4%**
- **Difficulty filling vacancies** and **high salary expectations** from skilled/experienced labour continue to drive average rates higher
- A **shrinking labour pool** (due to Brexit, an aging workforce, low apprenticeship uptake) and the **cost-of-living issues** are also putting upward pressure on rates

Most M&E firms reported little difference between head office and construction staff availability but indicated that overall, resource availability had improved compared to the Nov 2023 survey. Respondents noted:

- Firms that directly employ and train operatives/staff from the ground are experiencing **fewer resource issues** and have **better retention levels**
- Strong work volumes causing demand for staff to increase but **some teams are starting to come free** as projects complete
- While **recruitment remains difficult** (particularly for firms with no apprenticeship programmes), job vacancies are falling due to **questions over longer-term order books**. This has helped ease availability issues.

Resource Availability: Head Office & Construction Staff

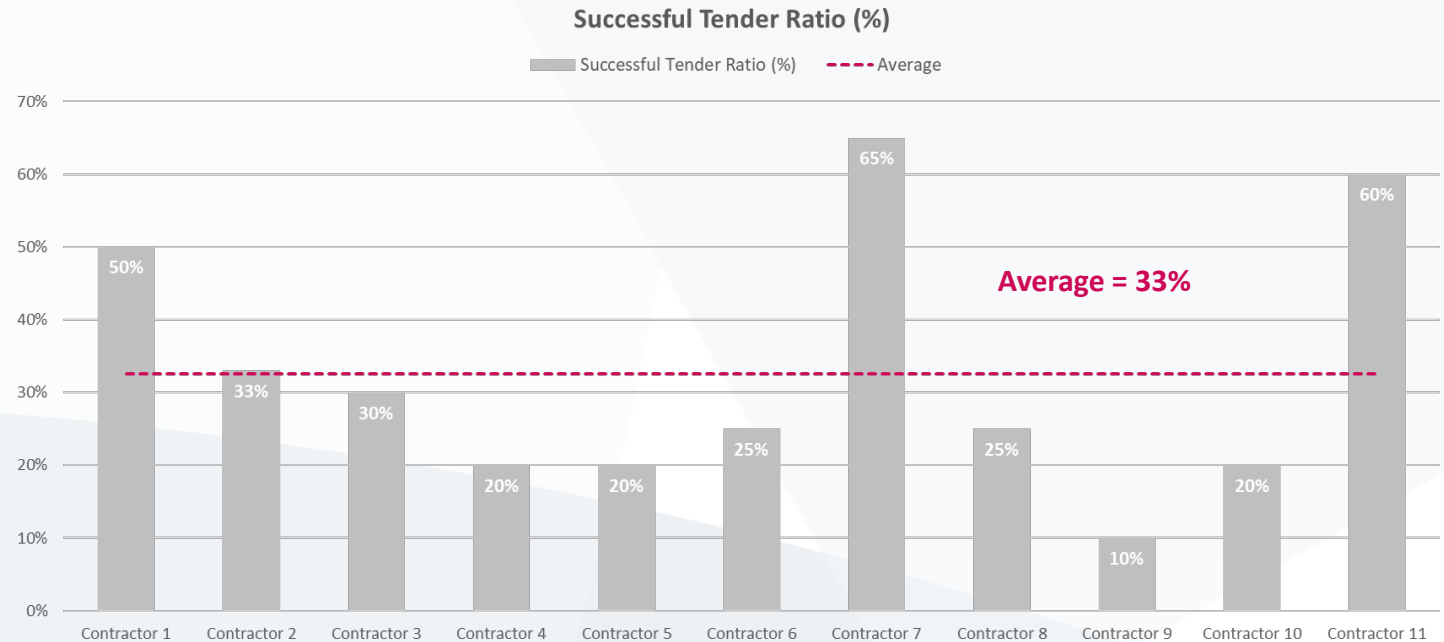




- Across all surveyed MEP contractors, the average minimum project value remained at **£2.7m** while the average maximum value rose **21%** compared to our Nov 22 survey, from **£116.9m** to **£142.2m**
- The lowest stated project value any contractor would consider was **£100,000**. One contractor indicated its ability to get involved in projects with values up to **£300m**
- The 'preferred' project value for all contractors was significantly lower than their maximum project size, averaging around **£20.3m**
- Some contractors noted they had no real preference regarding value and were able to take on higher value projects in certain regions (eg London) and on an exceptional basis

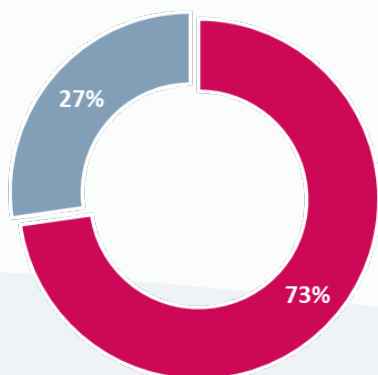


“The market remains busy, and the current lack of capacity due to full short-term order books has helped improve our successful tender ratios”



- The average successful tender ratio was **33%** but ratios ranged between **10-65%** across all respondents
- The successful tender ratio has increased significantly since our Nov 2022 survey, where the average was **28.8%**
- A higher average tender ratio is reflective of strong workloads, full short-term order books, and a current lack of tendering capacity
- Having sufficient resource to deliver workload is a key concern among surveyed MEP contractors
- High growth sectors such as data centres, life sciences, commercial office fit-out and low carbon projects are keeping MEP contractors busy
- MEP contractors are reluctant to bid on projects with unrealistic programmes/cost plans, as well as those with unknown inflation risks. Many will not tender on schemes unless they are engaged early in the procurement process

Are you currently experiencing any supply issues with regards to any MEP products/materials?



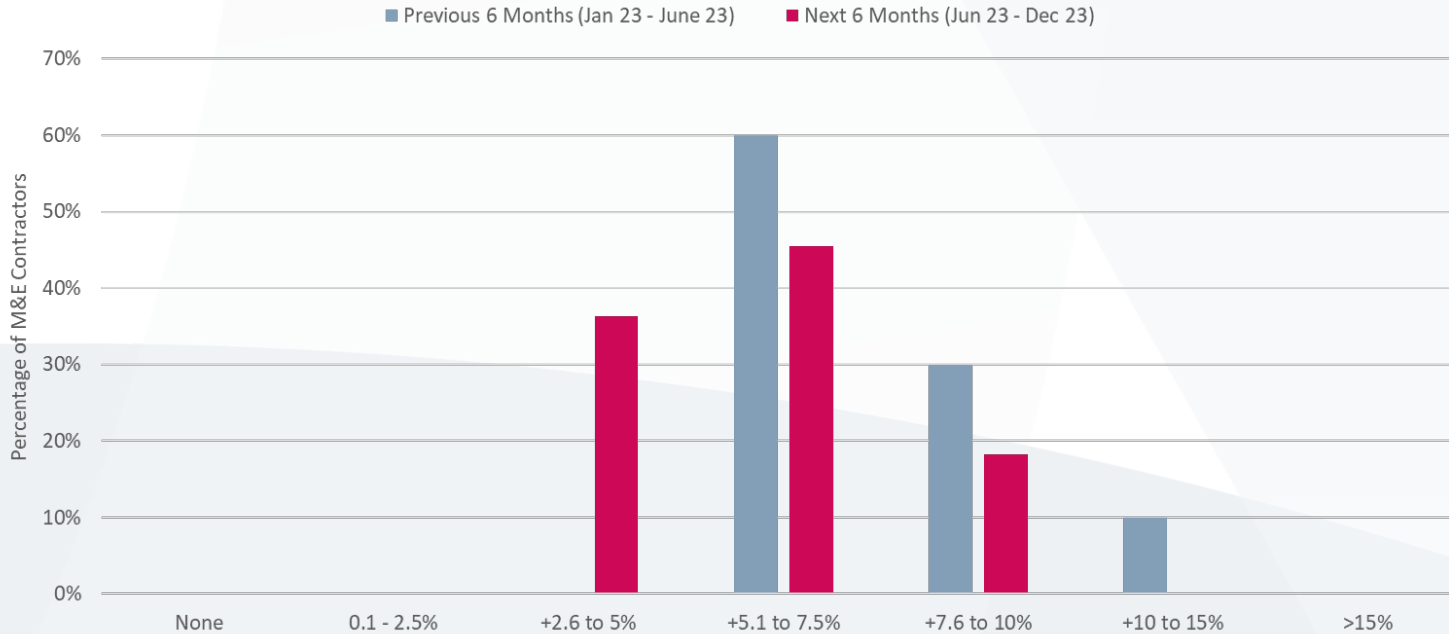
■ Yes ■ No

- **73%** of contractors are currently experiencing supply issues with certain MEP products/materials – an improvement from our Nov 2022 survey when all contractors reported issues
- Procurement periods have increased for major plant and any items with a solid-state chip in them
- Electrical needs need to be determined quickly and orders on products such as switchgear need to be placed early in the design phase
- Some contractors noted ongoing supply chain pressures were resulting in part orders being received
- Some key suppliers are unable to fix prices or provide indicative lead times, resulting in further risk allowances being added to projects

MEP Products/Materials Affected by Long Lead Times

- Most products with Microchips
- Large plant (**ASHP, AHUs**)
- Electrical Transformers
- Switchgear/Switchboards and Circuit Breakers
- Generators
- Cooling Equipment
- Computer Room Air Conditioning (**CRAC**) Units

MEP Products and Material Prices: Inflationary Estimate/Forecast



MEP products/materials price inflation expected to soften over the next six months

Price pressures are easing, but most still expect an inflationary rise of **'+5.1 to 7.5%'** over the next six months

Multiple suppliers (eg Schneider Electric) plan to add mid-year price increases of around **5-10%**

General availability of electrical components is improving, but strong demand for MEP products such as switchgear continues to drive pricing

Look **back** at Inflation:

- Over the past six months (Jan-Jun 23), contractors' estimated inflation for MEP products/materials fell within a range of **+5.1 to 15%**.
- The majority (**60%**) indicated MEP product inflation was within a narrower range of **+5.1 to 7.5%**, surpassing the rate of inflation provided by the BEIS 'All Work' material price index (**2.1%** over the past six months). MEP products and materials have evidently experienced stronger inflationary pressure than many other construction materials

Six Month Inflation Forecast for MEP products/materials...

45% of contractors

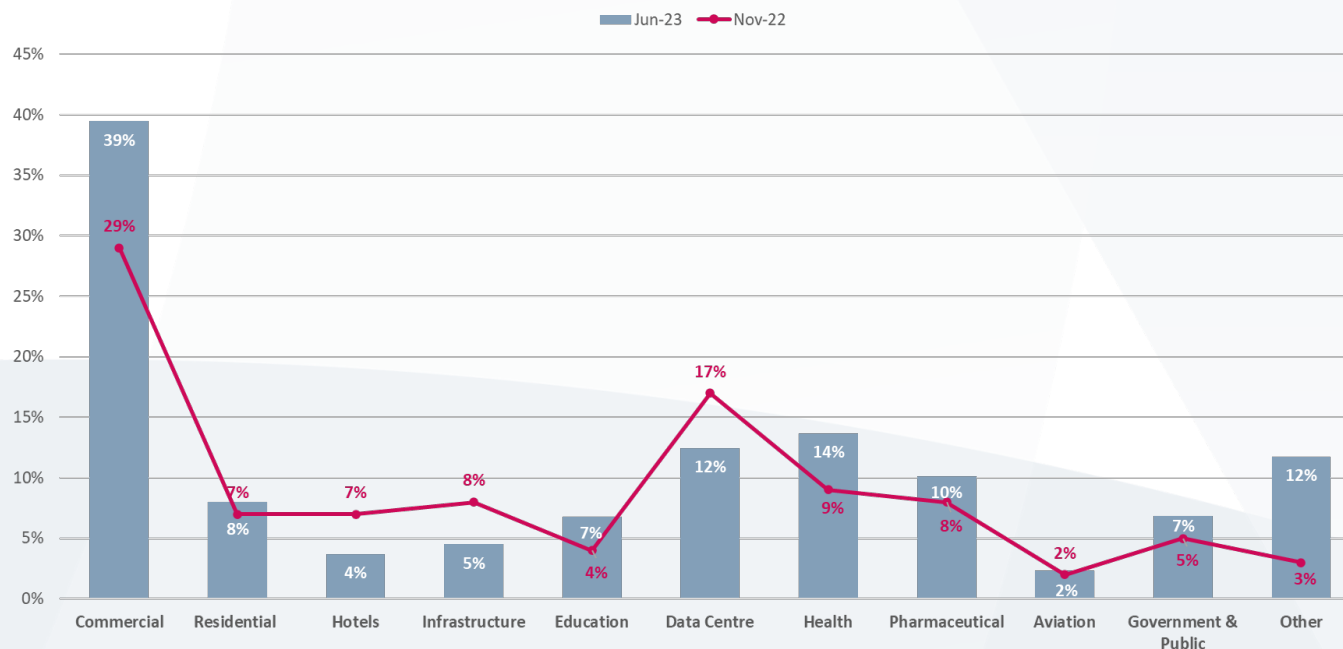
Expect inflation to sit within a range of:

+5.1 to 7.5%

Look **ahead** at Inflation:

- The outlook for the next six months indicates a shift to the left in contractors' expectations regarding inflation. Although most still anticipate relatively high inflation rates for MEP products/materials, ranging from **+5.1% to 7.5%**, none anticipate inflationary increases exceeding **10%**. Moreover, more than one-third of contractors expect inflation to be significantly lower, within the narrower range of **+2.6% to 5%**
- In recent years, the electronics market has had to contend with a global chip shortage, rising prices, and supply chain disruptions. A post-pandemic surge in demand exacerbated the situation, pushing MEP prices higher
- However, in recent months, improvements in component inventories and easing demand has softened price inflation. Although improvements vary wildly by component, the general pricing outlook has improved compared to 2022
- **Although materials availability and pricing remain key concerns for many surveyed MEP contractors over the next 12 months, there are some positive indicators that price pressures and supply shortages are easing for some MEP products and materials**

Average Sector Split (%) - Nov 2022 v. Jun 2023

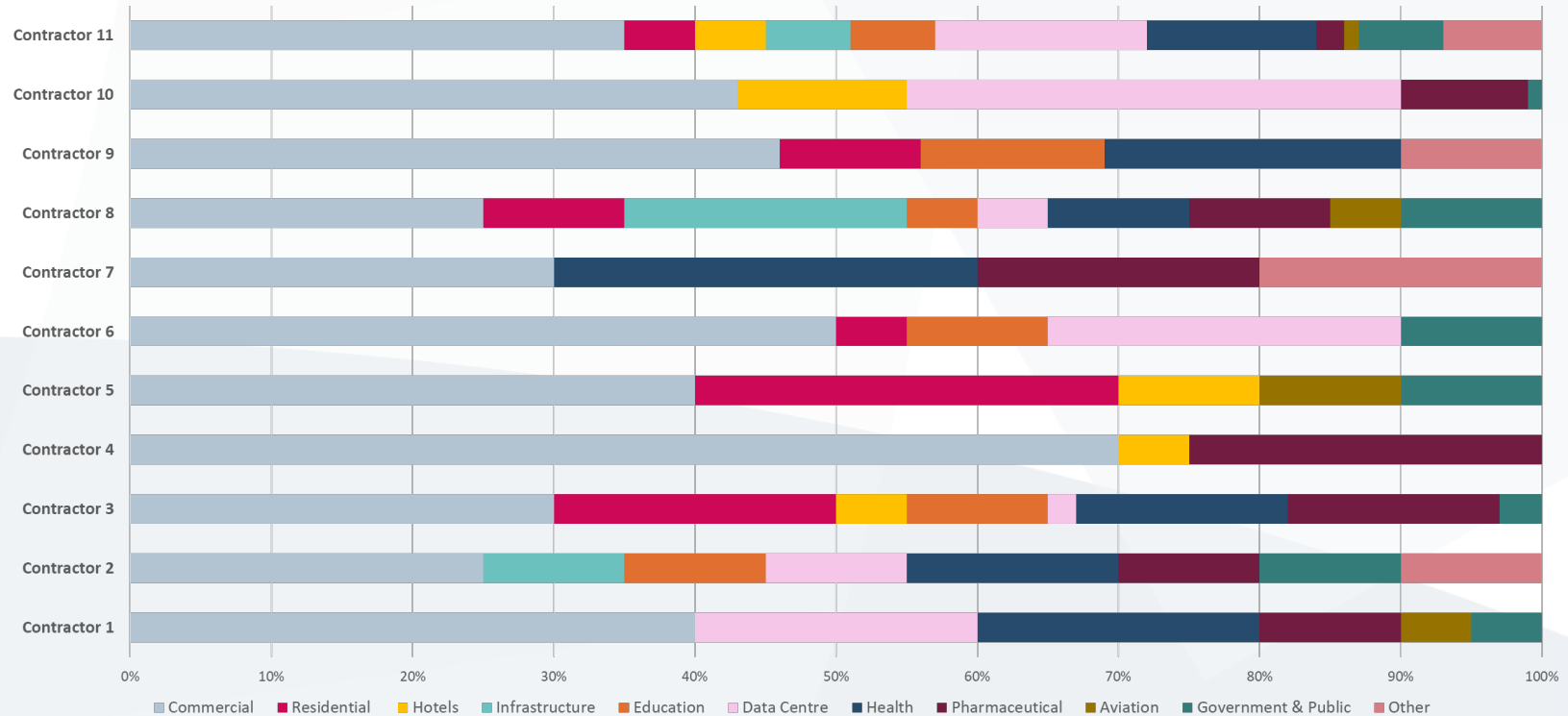


“The [new build]’ commercial sector is a concern for us, and we see this sector slowing down over the next three years”

“We plan to focus on more resilient sectors where we can add technical value, ie health, life sciences, and data centres, while focusing less on residential and hotels”

- MEP contractors reported a notable increase in the proportion of work within the commercial sector. In June 2023, an average of **39%** of survey respondents' projects were in the commercial sector, which is a significant rise compared to **29%** in our previous survey and slightly surpasses the pre-pandemic (2019) average of **38%**
- Health (**14%**), Pharmaceutical (**10%**) and Education (**7%**), all accounted for a higher average proportion of work compared to our previous (Nov 2023) survey, as did Government & Public, Residential and Other
- Increased commercial activity has been driven by demand for office fit-out work rather than new build activity. Tenants demand greener/more sustainable space that can meet their net zero carbon strategies and are focused on meeting WELL and NABERS standards. Health and Lab enabled life sciences projects are also providing a steady flow of new tendering opportunities

Sector Split by MEP Contractor



Commercial continues to account for a significant source of workload for all contractors

Contractors continue to branch out into new sub-sectors to make up for falling residential activity

More MEP contractors are targeting work in growth sectors, ie pharmaceutical and health

Main Risks Facing UK Market:

- Limited number of large sprinkler contractors in London making fixing prices difficult
- Current lack of capacity due to full short-term order books
- Pressure on labour rates due to shrinking labour pool, reduced access to migrant labour and the cost-of-living crisis
- Long lead times for specific materials (ie generators and transformers)
- Further material price inflation
- Rising cost of borrowing and its impact on investment in long-term projects
- Sub-contractor insolvencies
- Reduced workloads and resources to deliver workload

“Fixing prices on some packages (ie sprinklers) is becoming very difficult, resulting in further risk percentages being added to projects.”

Factors Currently Influencing Successful Project Procurement

- Early engagement with the supply chain (CDP packages in particular)
- Better scoped PSCA periods allowing design issues to be resolved early and priced into the project (reducing risk)
- Key team (workforce/operative) availability
- Realistic programme (design & construction) and cost plans
- Unknown inflation risk
- Delivery periods
- Fixed price commitments
- Quality of design
- Right resources to support pre-construction
- Release of design information in a timely manner in order to assist packages to be procured at costs that reflect the tendered prices

What Market Pressures Are Driving Pricing?

- Skilled labour shortages
- Fire regulations stopping building sign off
- Brexit and the war in Ukraine
- Limited capacity of sub-contractors is forcing costs to rise
- Materials shortages
- Previous fuel/energy price increases



Interesting MEP Market Trends



Net zero carbon, greener space and sustainability



Clients adopting early contractor involvement with PCSAs



MMC/pre-fabrication still being pushed on projects



Shift away from residential to growth sectors

Strategic/business model changes planned...



Higher selectivity and enhanced risk profiling



Exploring new sectors and workstreams



Reviewing and limiting the amount of lengthy pre-construction periods



Greater focus on resilient growth sectors



Management reshuffles and changes in regional focus

For further information, please contact:

Jonathan Wilson (*Partner*): j.wilson@gardiner.com

Lee Moore (*Partner*): l.moore@gardiner.com

Michael Urie (*Senior Market Analyst*): m.urie@gardiner.com