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G&T Main Contractor Survey

October

2021

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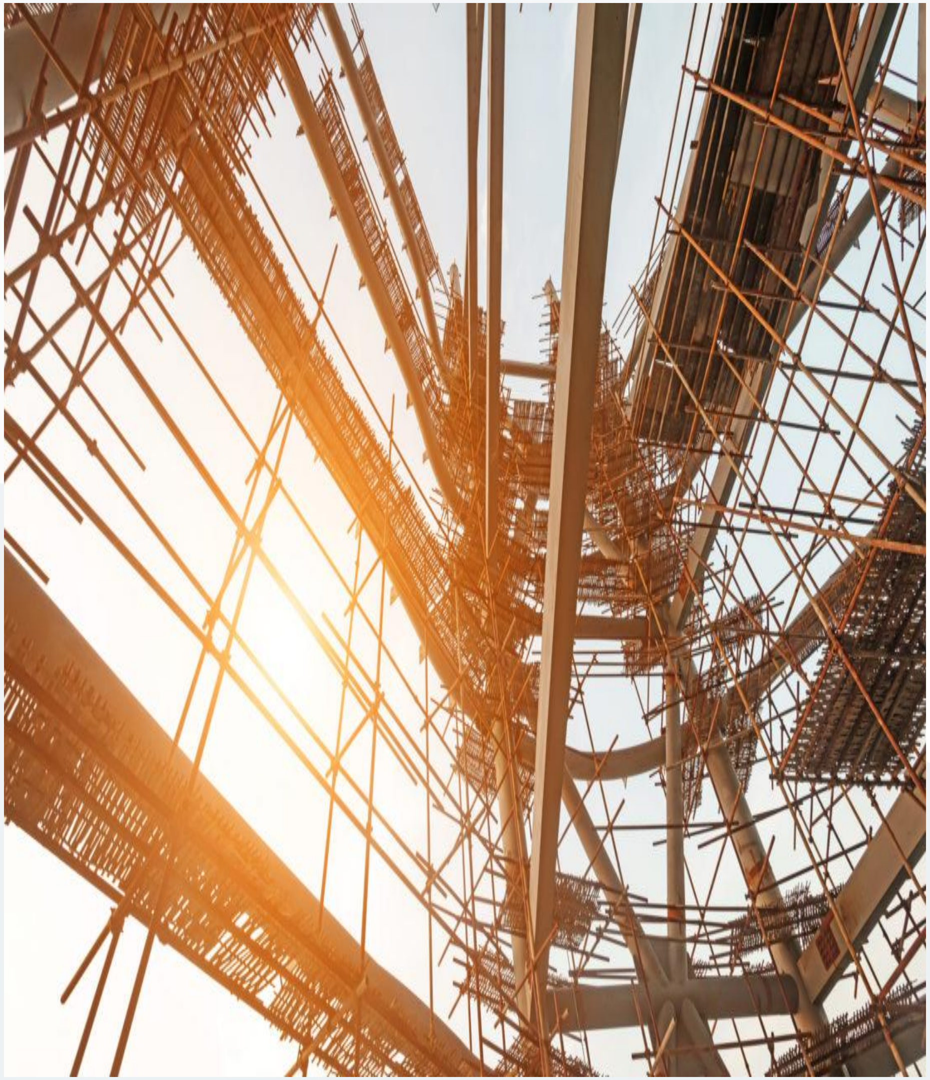
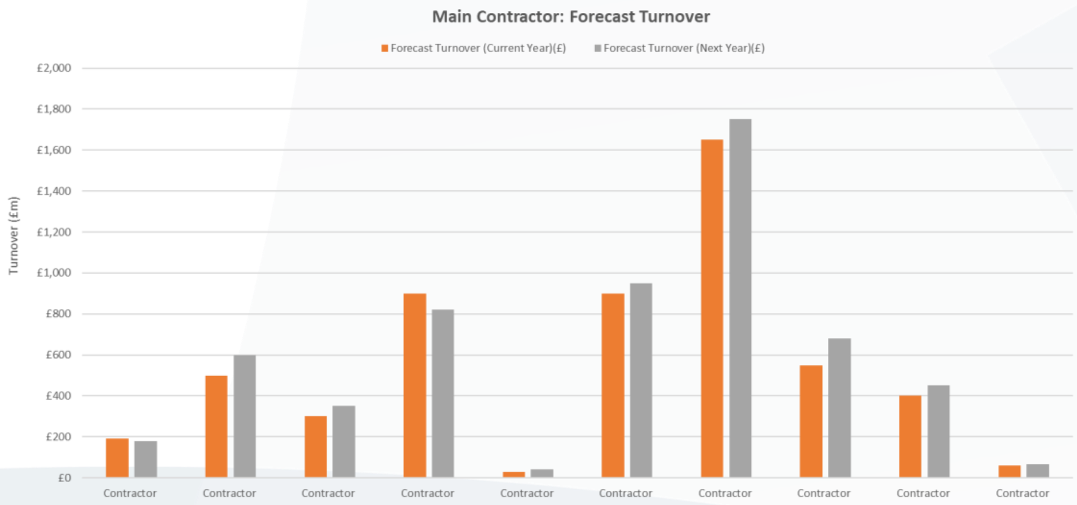
G&T's Main Contractor Survey report for October 2021 summarises some of the key trends and themes generated from the responses to our most recent Main Contractor survey.

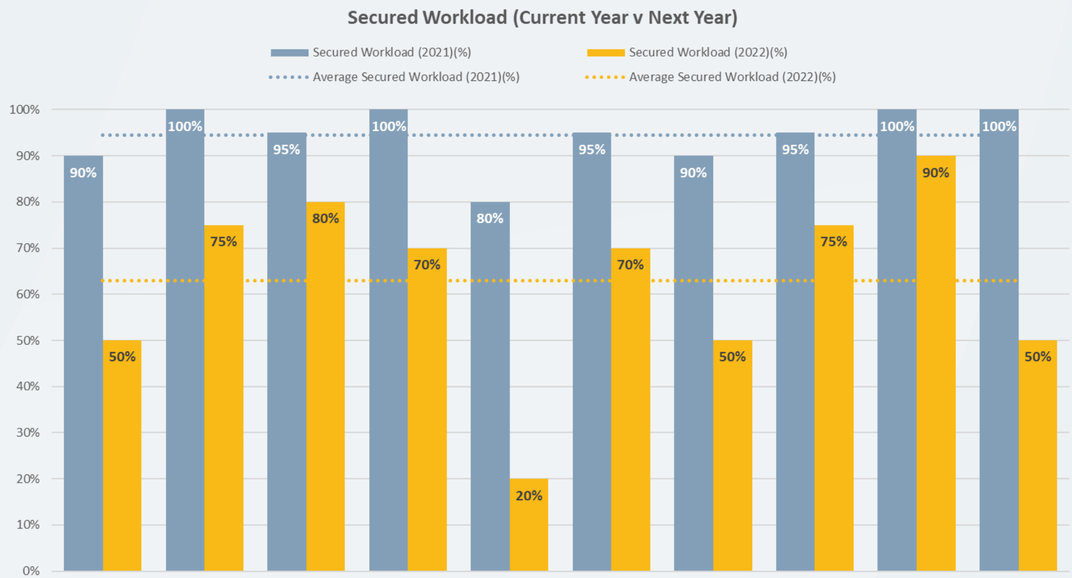
Please note: *For confidentiality reasons, the names of the individual contractors that responded to the survey have not been disclosed in this report.*

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

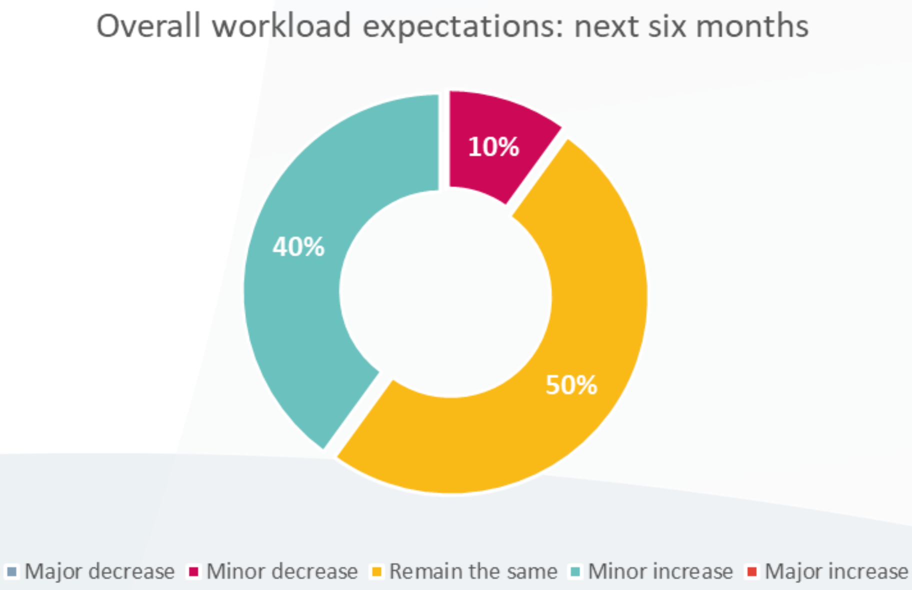


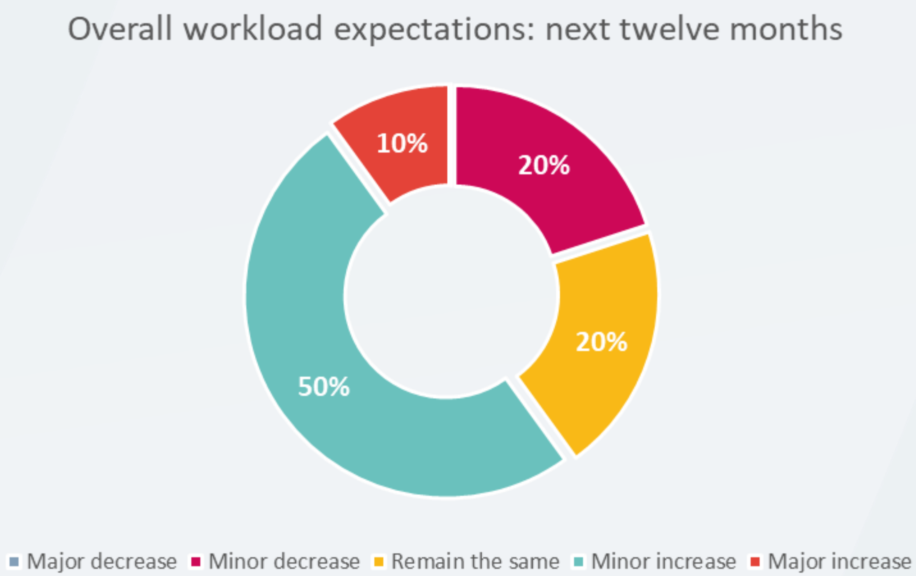


- The majority of respondents (***80%***) anticipate that turnover next year (2022) will be higher than their 2021 turnover
- On average, main contractors forecast that turnover will increase by ***11.2%*** in 2022 compared to their 2021 turnover levels
- A number of contractors said they are planning for growth in 2022 and noted that while they have built in provision for some market uncertainty, they do not expect to have to chase turnover
- Some contractors also indicated that they are being more selective with their bidding activities and are focusing on identifying the right projects with the right clients to suit their risk profile

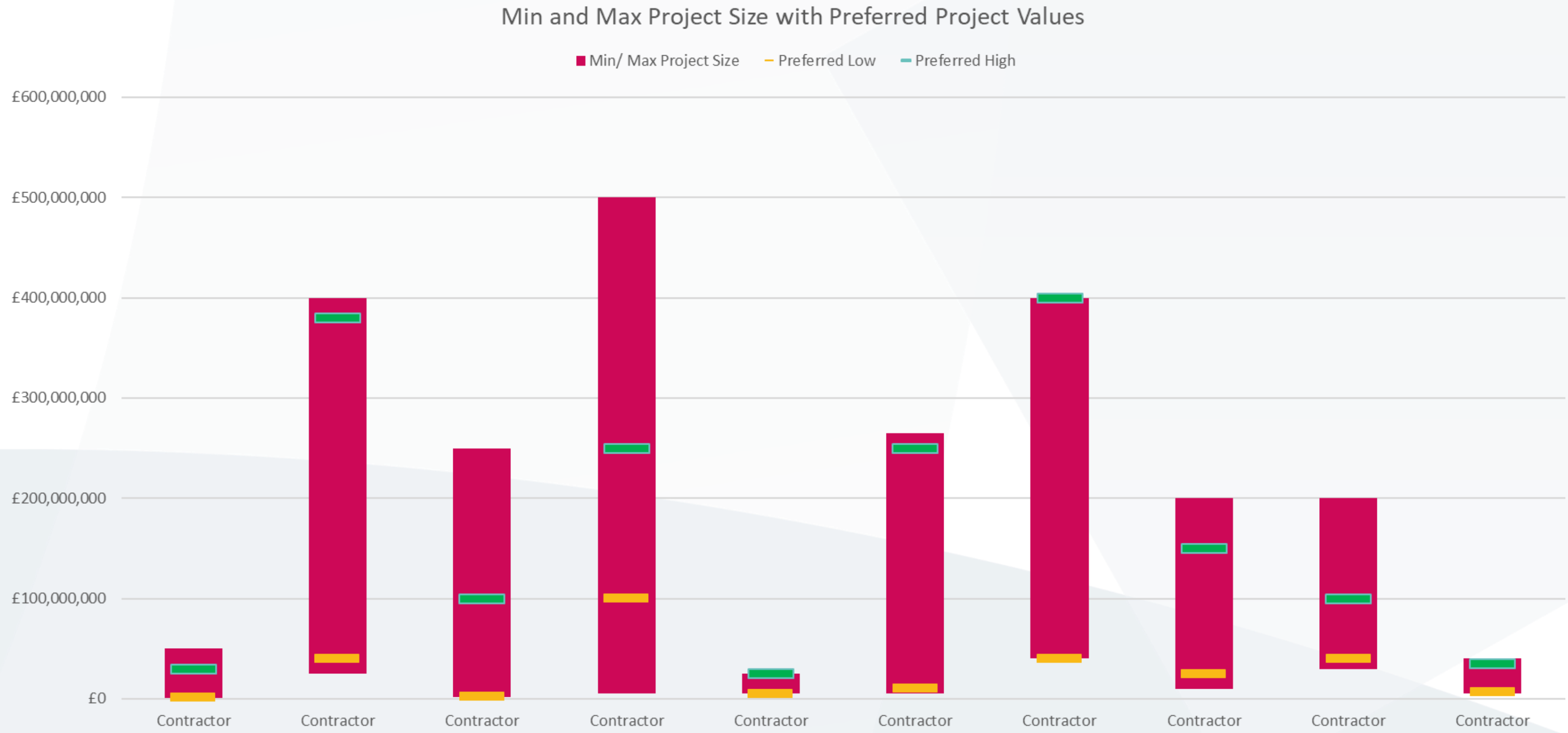


- On average, contractors have secured ***95%*** of their workloads for 2021 but only ***63%*** for 2022
- Excluding the contractor with the lowest secured workload value for 2022 (***20%***), the average secured workload value increases to ***68%***. However, this is still lower than what would normally be expected for the time of year (ie typically ***70-75%***)
- Main contractors have an average unsecured workload capacity of ***37%*** for 2022. However, the latest Construction PMI survey points to rapidly rising workloads and stretched business capacity, suggesting that 2022 workload capacity will fill quickly
- One respondent noted that workloads in central London may decline but anticipated that strong regional construction activity growth will more than make up for this

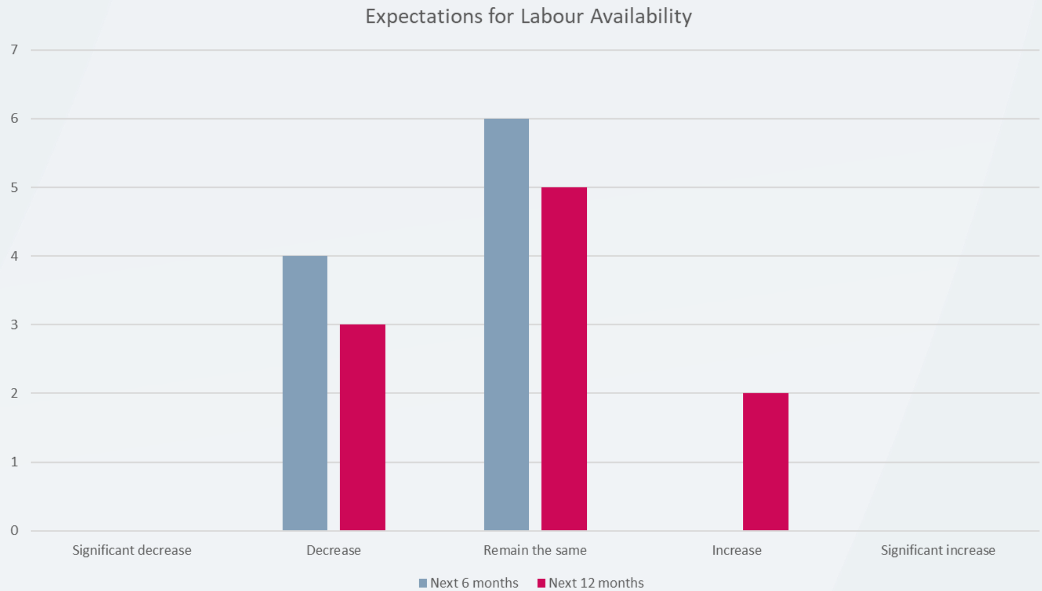




- Workload expectations for the next six months are split between those who anticipate no change (***50%***) and those who expect either a 'minor increase' (***40%***) or 'major increase' (***10%***)
- Over the longer 12-month period, workload expectations become more polarised
- Encouragingly, the majority (***60%***) expect workloads to increase to some degree over the next 12 months while a further ***20%*** said that workloads will remain at the same level. However, the number of contractors expecting workloads to see a 'minor decrease' rose slightly from ***10%*** to ***20%***
- **Generally, construction companies are highly optimistic about their growth prospects for the year ahead however, some are clearly less confident in light of supply chain disruption and signs of softer demand**

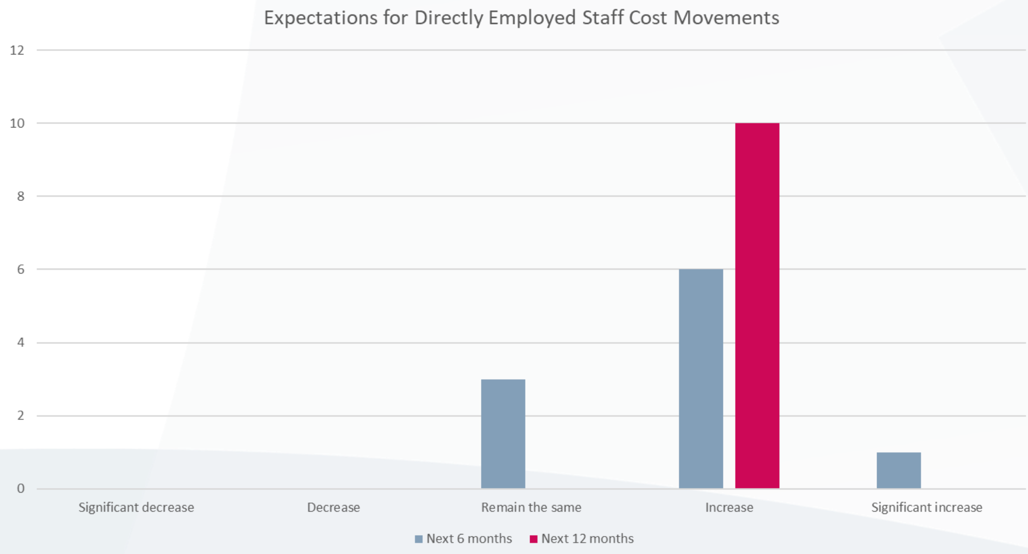


- Across all surveyed contractors, the average minimum project size was just over **£12.7m** while the average maximum size of project was **£233m**
- The minimum and maximum project values ranged from **£100k** all they way up to **£500m**, but some contractors noted that there was no real upper limit and that the maximum value was dependant on the contract arrangement
- The 'preferred' maximum project size for all contractors was, on average, nearly ***25%*** lower than their absolute maximum project size
- There was a significant difference between the absolute minimum project size that contractors were willing to get involved in and their 'preferred' minimum. On average, the preferred minimum project size was ***318%*** higher than the absolute minimum project size
- Some noted that they had no real preference regarding project size and were able to take on higher value projects in certain regions (eg London)

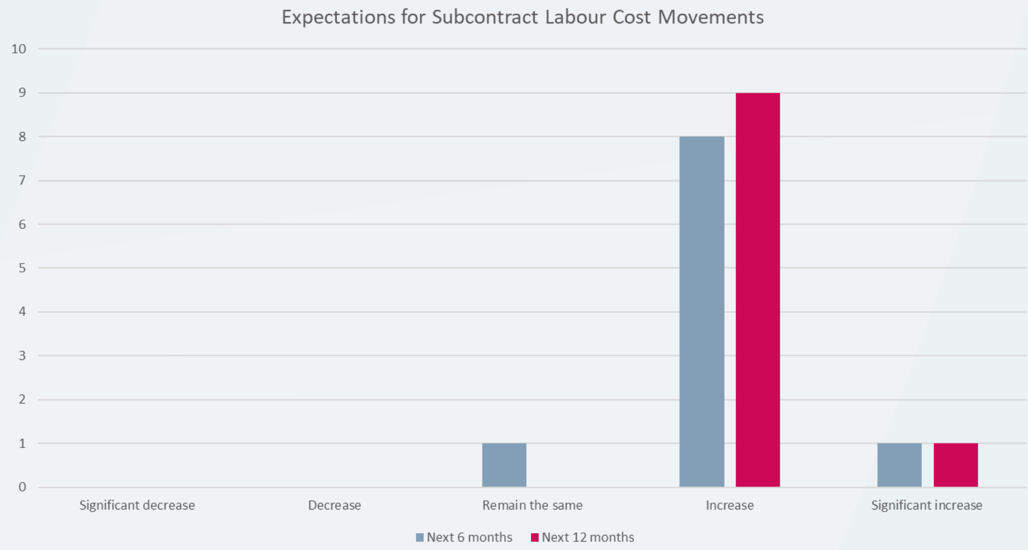


- Main contractors reported lower levels of availability for project labour resource than staff resource
- While ***70%*** of contractors said that staff resource was currently 'available', the same proportion of respondents said that project labour resource availability was either 'low' or 'very low'
- Although a handful of contractors explained that the current lack of labour availability was becoming a major business and industry issue, most have been able to match resources with their project workload and planned growth
- Reduced availability of operatives has put pressure on certain key trades (eg brick and blockwork), prompting some to demand unrealistic and unsustainable rates
- One contractor added that while general salaried staff were indeed available, there has been a significant increase in churn and that staff have raised salary expectations

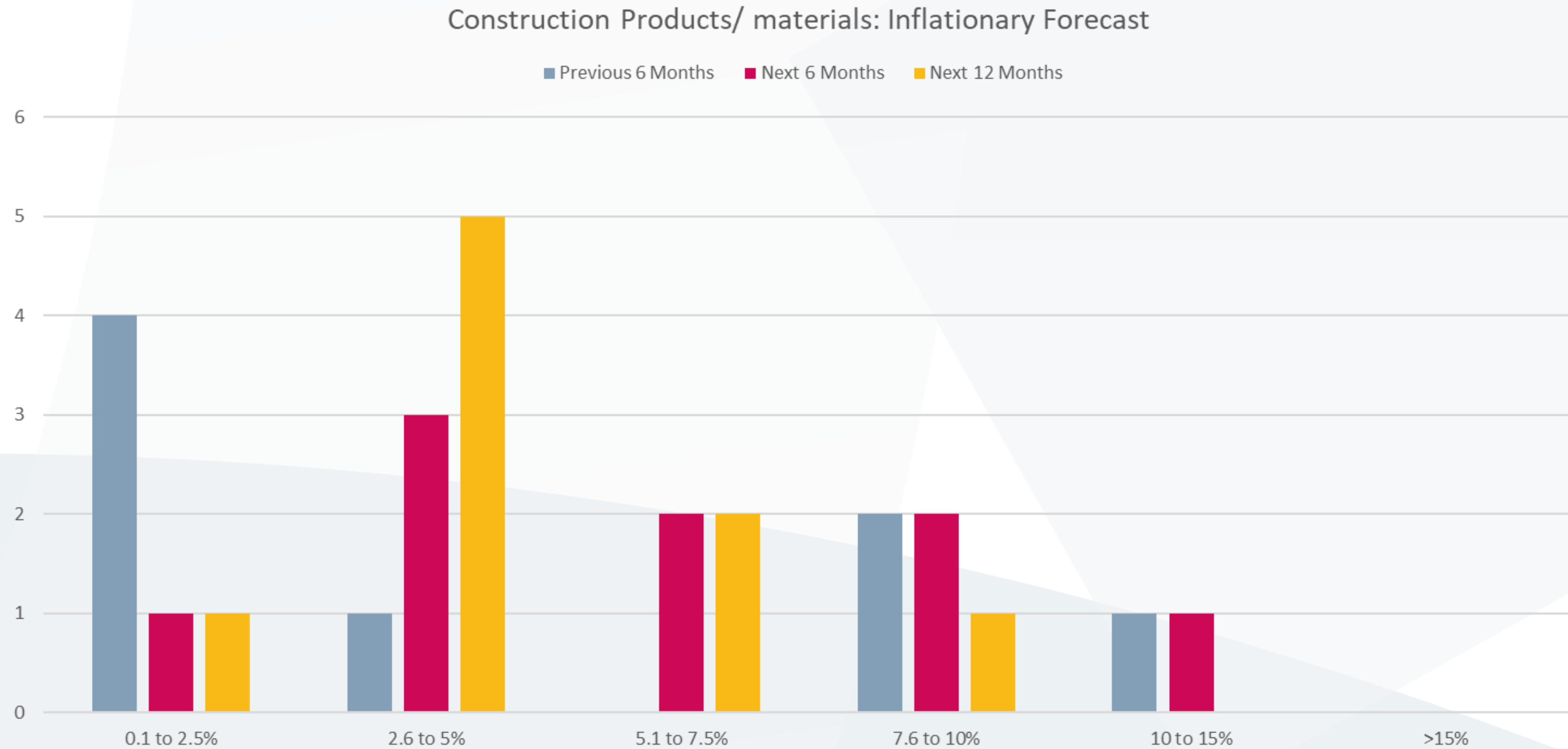
- According to most contractors (***60%***), labour availability will 'remain the same' over the next six months while ***40%*** anticipate that availability will 'decrease'
- However, the data points to a gradually improving situation over the longer 12-month period, with ***20%*** indicating that labour availability will 'increase' and ***10%*** fewer respondents expecting availability to either 'decrease' or 'remain the same'
- Staff and labour availability will continue to be impacted by demands from major infrastructure projects (eg HS2 and Hinckley Point)



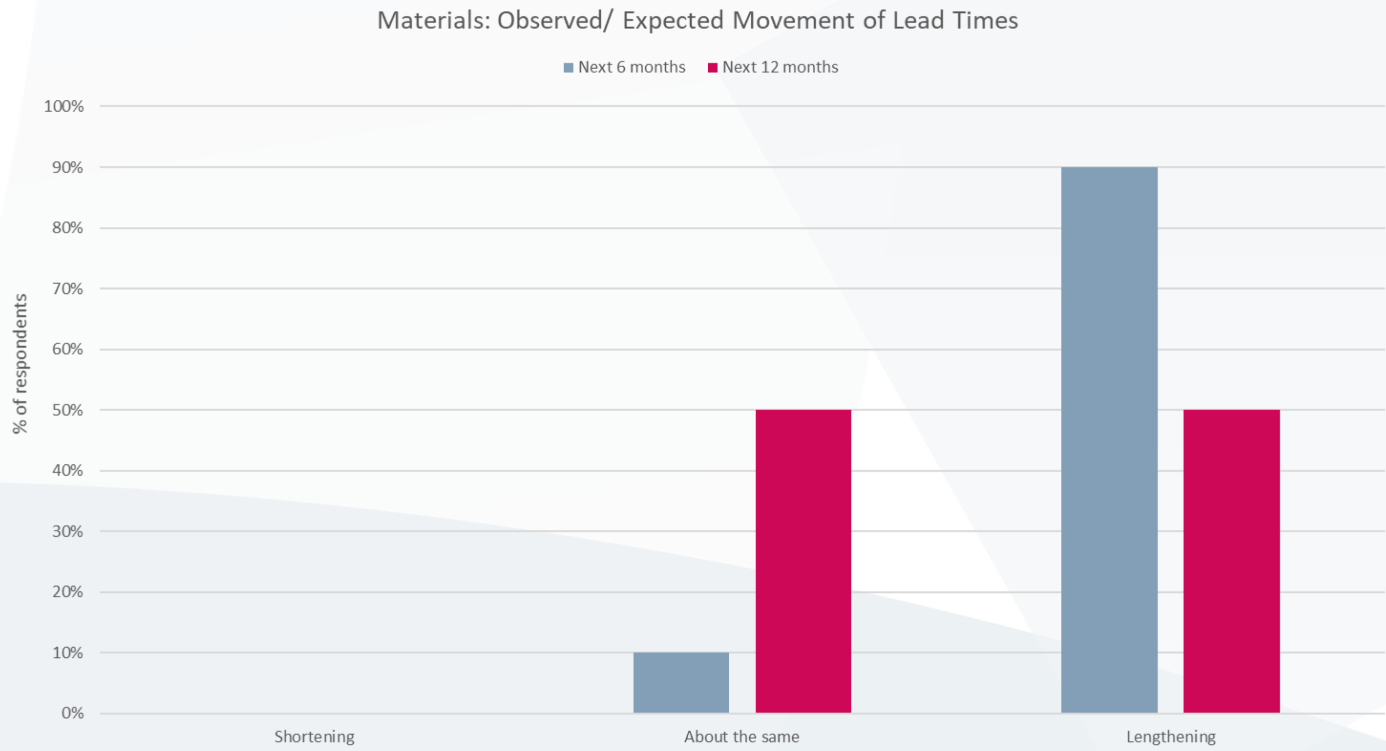
- Expectations for directly employed staff cost movements over the next six months ranged from 'remaining the same' (***30%***) to a 'significant increase' (***10%***), but the majority (***60%)*** expect that staff costs will 'increase'
- Over the longer 12-month period all contractors said that costs for directly employed staff would 'increase'



- Expectations for subcontract labour cost movements follow a similar pattern, with the majority expecting costs to increase over the next six months (***80%***) and the next 12 months (***90%***)
- Prices are being driven by labour capacity and a number of specialist sub-contractors (eg cladding and MEP sub-contractors) having capacity constraints ranging from preconstruction, design and installation
- Sub-contract labour shortages are putting a real strain on costs and are combining with the supply chain crisis to disrupt activity on site

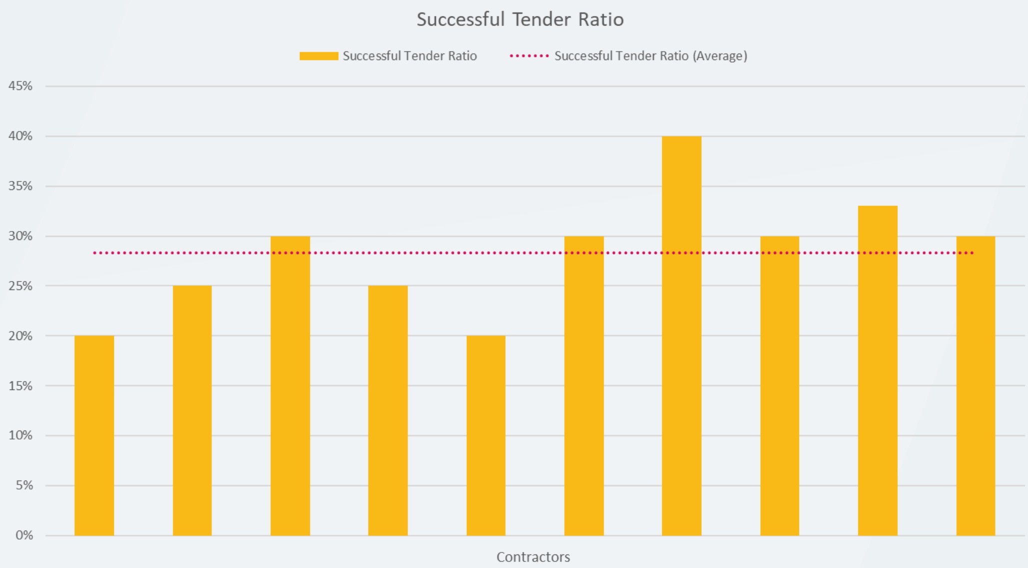


- All respondents, without exception, confirmed they were currently experiencing supply issues with regards to construction products and materials
- Over the past six months ***40%*** of contractors said that construction product/material prices had risen by ***'0.1 to 2.5%'*** while others said that inflation has been much higher. For example, ***20%*** of respondents reported inflation in the ***'7.6 to 10%'*** range while one contractor said that material prices had risen by ***'10 to 15%'*** over the last six months
- Interestingly, material price inflation expectations for the next six months are even higher. The most common inflationary forecast was ***'2.6 to 5%'*** with ***30%*** of respondents expecting material prices to fall within this range. However, half of all respondents expect inflation to surpass this level and fall within one of the three ranges spanning from ***5.1% to 15%***.
- Over the longer 12-month period, ***50%*** of surveyed contractors expect inflation will be within the ***'2.6 to 5%'*** range, suggesting a greater degree of confidence than the rapid inflationary growth rate seen in 2021 will subside



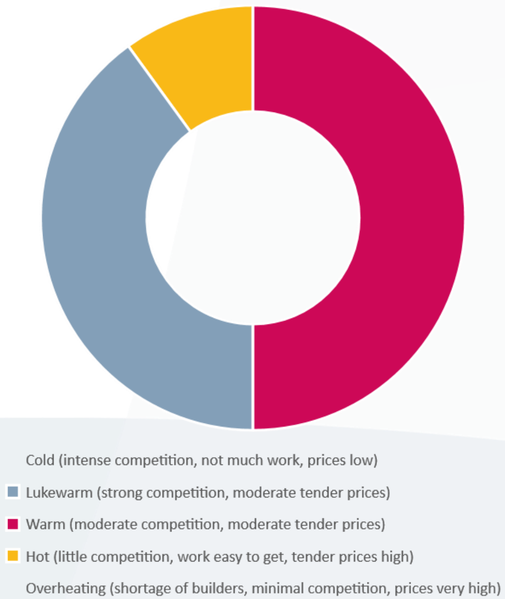
- On the whole, lead times are expected to lengthen over the next six months but then plateau and begin to ease over the longer 12-month period
- Contractors reported big increases in lead times for certain materials which, in some cases, have doubled over the last six months. This was a result of deepening supply issues amid a rapid recovery in demand
- With no obvious quick-fix solution to current global supply issues, many expect that upward pressure on lead times will be maintained. Timber and metals (inc steel) were cited as having some of the longest lead times but some suggested that the materials affected may change over time as supply increases
- Recent increases in wholesale gas prices are expected to impact the production of materials that require high energy manufacturing processes (eg cement) and further extend lead times in the short-term
- However, one contactor noted that lead times have started to show some early signs of improvement and was hopeful that by the start of 2022, lead times should begin to return to more normal (ie pre-pandemic) levels

- In the current market conditions, two-thirds of contractors indicated they were only holding tendered prices for one to two months, but some are still holding prices for longer periods (ie three to six months)
- Most said that the length of time prices were being held was dependant on the scheme and what was being fixed. Some are fixing staff and preliminaries costs for longer periods but prices on certain packages/materials will only be held for relatively short durations (ie 0-4 weeks) due to the current price volatility

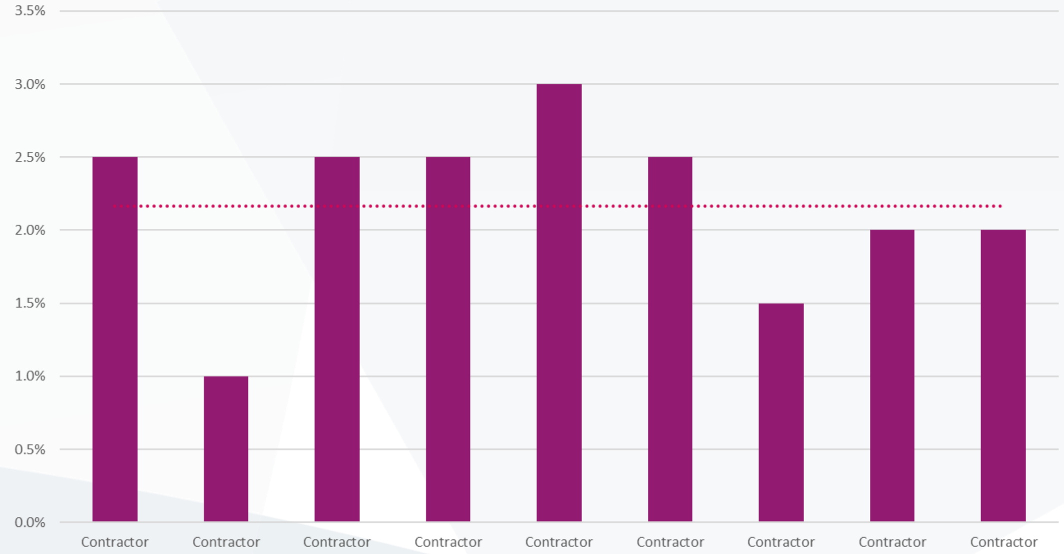


- The ratio of successful tenders (or the 'Bid-Hit' ratio) averaged at ***28%*** but ranged between ***20%*** to ***40%***
- This ratio is typical in a healthy tendering market and indicates there is a good volume of new bidding opportunities coming through the pipeline

Description of Market Tendering Conditions

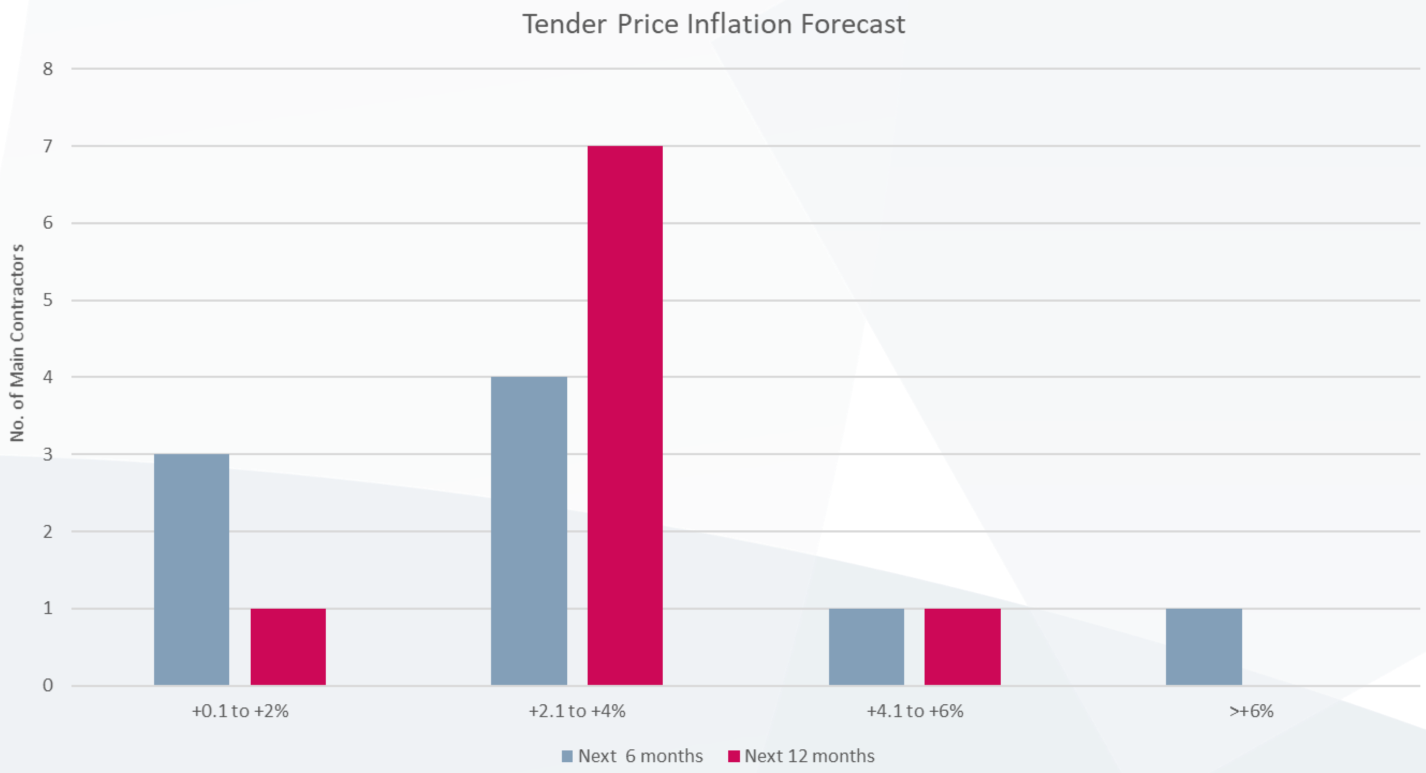


Typical Project Risk Allowance

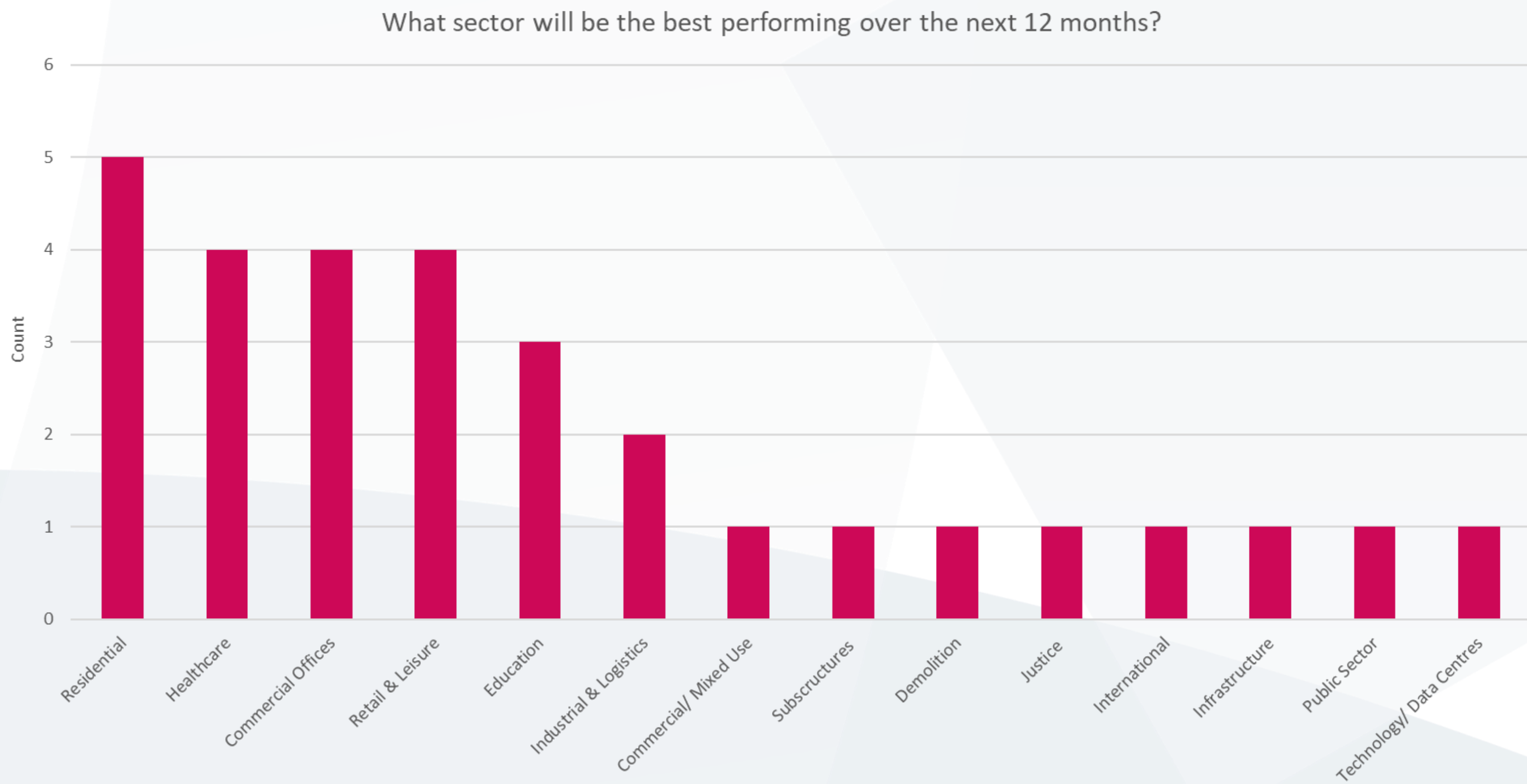


- Market tendering conditions were described as 'Warm' by half of the surveyed contractors (ie moderate competition producing moderate tendering prices)
- However, a significant proportion (***40%***) thought that although tender prices were moderate, competition was relatively strong and said conditions were better described as 'Lukewarm'
- Only ***10%*** of contractors thought that market conditions were 'Hot' – ie little competition, work easy to get and tender prices high

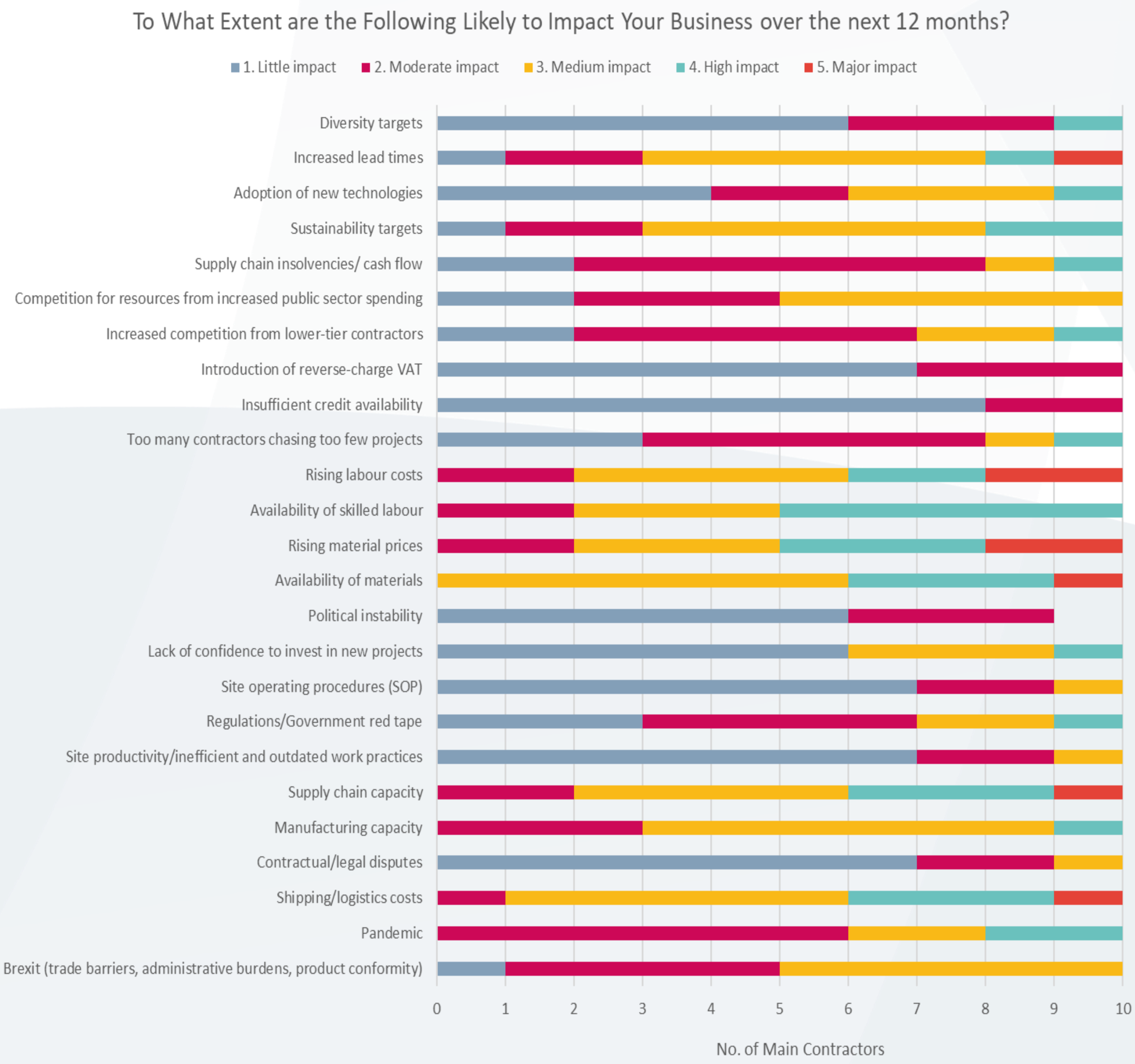
- Average project risk allowances currently stand at ***2.17%*** but allowances ranged between ***1%*** and ***3%***
- On some projects in certain sectors, the risk allowance can be much higher. One commented that in a competitive tender the risk allowance can be ***0%*** but in a negotiated position they suggest that clients hold for ***5%***
- The supply chain is understandably nervous about cost movements and is therefore adding significant premiums through higher risk allowances to fix prices for projects starting in 2022 and beyond
- In the current market, where work is fairly abundant and material prices movements are uncertain, risk allowances are expected to remain above average



- All contractors forecast tender price inflation growth over the next 6-12 months but most indicated this would be in the ***'+0.1 to 4%'*** range
- There is a greater spread of inflationary forecasts over the shorter, six-month period with one respondent even suggesting that TPI would exceed ***6%***. Over the longer 12-month period, inflationary estimates tighten and fall within a narrower range with ***70%*** forecasting TPI growth of ***'+2.1 to 4%'***
- While there are early signs that the rate of material price inflation is beginning to ease, a tighter labour market is expected to drive input costs higher. A shortage of HGV drivers also needs to be factored in which will impact not just input costs, but delivery timescales and construction output growth
- Contractors reported that confidence has grown with rising workloads and strong project pipelines. With a plentiful supply of work, contractors are reluctant to absorb sustained input costs rises and are being more risk averse and selective in the projects they choose to tender



- Contractors were asked what they thought would be the best performing sectors (in terms of activity growth) over the next year and the residential sector received the highest number of votes of all the sectors
- One contractor explained that because of recent societal shifts, they were looking to explore new and emerging markets - one of these being repurposing a glut of retail space to residential development as retailers reduce their footprints
- Other sectors that look poised for growth include the healthcare sector (due to the Government's ambitious hospital programme), commercial office sector (which is benefitting from a surge in refurbishment and fit-out projects) and also the retail and leisure sectors (which are adapting in light of changes to post-pandemic shopping and leisure habits)
- Education is another sector expected to see strong growth as university estates consolidate. The industrial & logistics sector (which has been the best-performing sector in terms of new order growth over the last year) also looks set to benefit from the e-commerce boom and the current undersupply of space



- Surveyed main contractors said that ‘rising labour costs’ and ‘material prices’ were likely to be the two biggest issues over the next 12 months

- Both issues stem from availability/supply issues which were therefore also expected to have a significant impact on main contractors’ business activities

- These factors were followed closely by concerns over ‘shipping/logistics costs’ and ‘supply chain capacity’

- Concerns over sub-contractor capacity have emerged in recent months. A surge in activity has created short-term capacity constraints and contractors are feeling increasingly stretched

- According to the Freightos Baltic Index (**FBX**), shipping costs have risen by ***358%*** in the year to 22nd October. With logistics experts suggesting that costs will not begin to fall until 2022 (once the record number of containers ordered this year come on stream and begin to address the capacity shortfall), this will remain a key issue in the short-term

- Manufacturing capacity is also expected to have a moderate impact on businesses. Rapid demand shifts have meant that a lot rests on how quickly and effectively supply capacity is rebuilt and ramped up

What market pressures are currently driving construction prices?

- Labour resource availability
- Materials shortages and uncertainty of supply (eg certain products being on allocation)
- Commodity price pressures
- High plant, fuel and haulage costs
- Competitor behaviour
- Unwillingness of the supply chain to fix prices
- Macroeconomic factors (eg COVID-19/ Brexit impacting supply)
- The attractiveness of projects and confidence around timescales (ie is it likely to happen in the short-term?)
- Uncertainty/ lack of confidence with regard to investment in the mid to long-term
- Main contractor capacity and appetite for risk
- Legislative change requiring further project resource in response to Building Safety Bill
- Further sustainability and environmental legislative compliance such as the GLA's revised Energy Assessment Guidance (SAP 10) and Part L enhancements with focus on impact on residential sector

Is your business model/strategy likely to change over the next six months?

- Depending on workloads, potentially less emphasis on work in Central London
- Exploration of new/ emerging markets and sectors (eg life sciences, public sector work)
- Building in extra provision for uncertainty but still planning for growth through early identification of the right projects with the right clients
- Not expected to chase turnover
- Greater focus on off site manufacture for construction

"We strongly believe the lack of free movement due to Brexit is hindering the construction sector as a lot of the labour force came from Europe."

" The main market trend is the investment in developing buildings that will support a reduction in carbon emissions and become net zero carbon by 2050."

" The market is busy. We have seen a trend in clients entering PCSAs to develop the price, methodology etc., rather than issuing traditional tenders."

Are you currently seeing any interesting market trends or themes emerging?

- Net Zero: investment in developing buildings that will support a reduction in carbon emissions
- Greater investment in green technology/ materials (eg 'green concrete')
- Increased demand from clients for air source heat pumps or exhaust air heat pump solutions
- Greater focus on Environmental, Social and Corporate Governance (**ESG**) and the 'Ten Point Plan for a Green Industrial Revolution'
- Digital technology, modern methods of construction, design for manufacture and assembly and offsite manufacture
- Early contractor engagement and certainty of construction team
- Digital work and test inspection becoming more commonplace and readily integrating with main contractor CDE's through APIs
- ISO 19650, its data naming protocols and data management procedures are becoming more widely adopted in the industry, partly in response to the Building Safety Bill
- Increases in warranty periods

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