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G&T Main Contractor Survey

July

2023

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G&T's Main Contractor Survey report for July 2023 summarises some of the key trends and themes generated from the responses to our most recent Main Contractor survey.

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Please note: *For confidentiality reasons, the names of the individual contractors that responded to the survey have not been disclosed in this report. Survey respondents operate across all geographical regions of the UK, but the majority tend to operate in Greater London and the South East.*

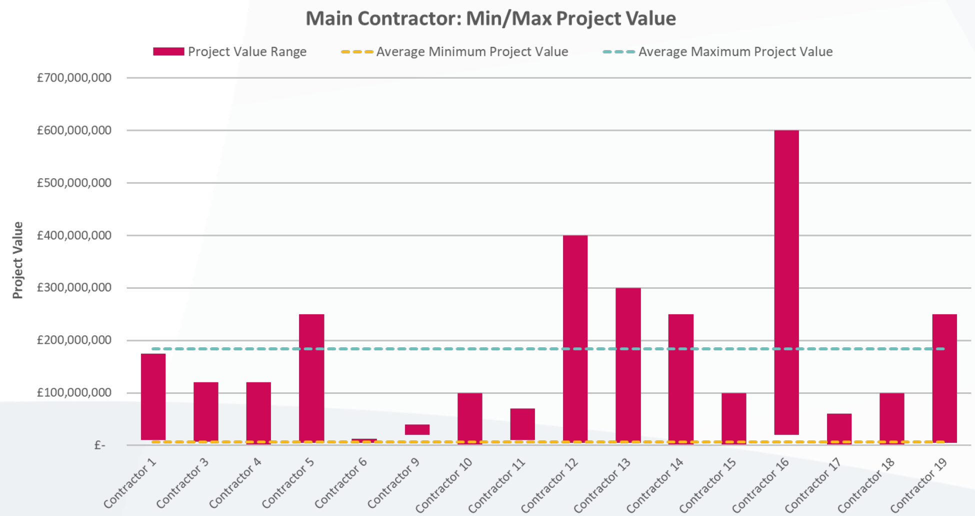
G&T's latest Main Contractor Survey revealed a host of insights on the current state of the UK construction market. The contractors that responded to our survey are among the most time-served and financially secure construction companies trading.

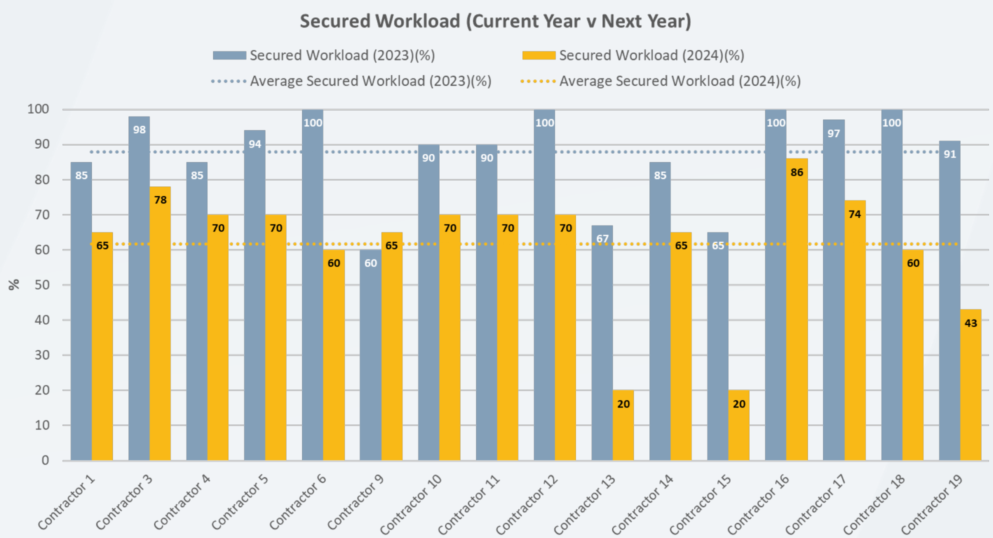
Since our last survey in 2022, the inflationary landscape in construction has become more settled. Contractors continue to benefit from a high volume of opportunities across most sectors that allow them to pick and choose which tenders to pursue, but new risks have come to the fore. Financial pressures have increased the risk of contractor insolvencies, while ongoing skilled labour shortages have resulted in the supply chain downsizing. This is, according to some contractors, taking capacity out of the market and risks putting further pressure on prices.

Despite the weaker demand conditions this year compared to 2022, contractors reportedly remain busy. Most surveyed main contractors have secured 90% or more of their 2023 workloads. Workloads for next year are also in better shape than they were in our last survey, suggesting pipelines remain strong in the short to medium-term. However, the uncertain macroeconomic outlook and slowing new order growth in construction raises questions over longer-term demand and construction activity.

Some of the highlights from our latest report include:

- **Typical Overheads and Profit (OH&P) have dropped for all but the highest value projects.** The prospect of cooling demand and market activity has seen contractors become more flexible with their controllable costs in order to win work
- **Project Labour and general lack of skills is probably the biggest challenge the industry is facing**, and there is no quick fix. There continues to be a significant cost premium to secure certain skilled trades and staff roles
- Lower energy costs and softer demand have helped **ease material price inflation**. The **overall supply picture has improved significantly** in 2023 and product availability has mostly returned to pre-pandemic levels, helping **lead times to stabilise**
- Most **trades continue to experience a degree of moderate cost pressure**, largely driven by labour shortages. However, later trades (ie façades and M&E) are facing the greatest inflationary pressures and availability issues
- Contractors continue to be **selective in their bidding activities**, but an uncertain growth outlook has encouraged a **greater tender submission rate** as contractors seek to secure pipeline and turnover
- **Market tendering conditions have cooled** since last year. Fewer bidding opportunities have led to a greater willingness among contractors to consider a **variety of procurement routes**, but many remain wary of being caught out by further price spikes

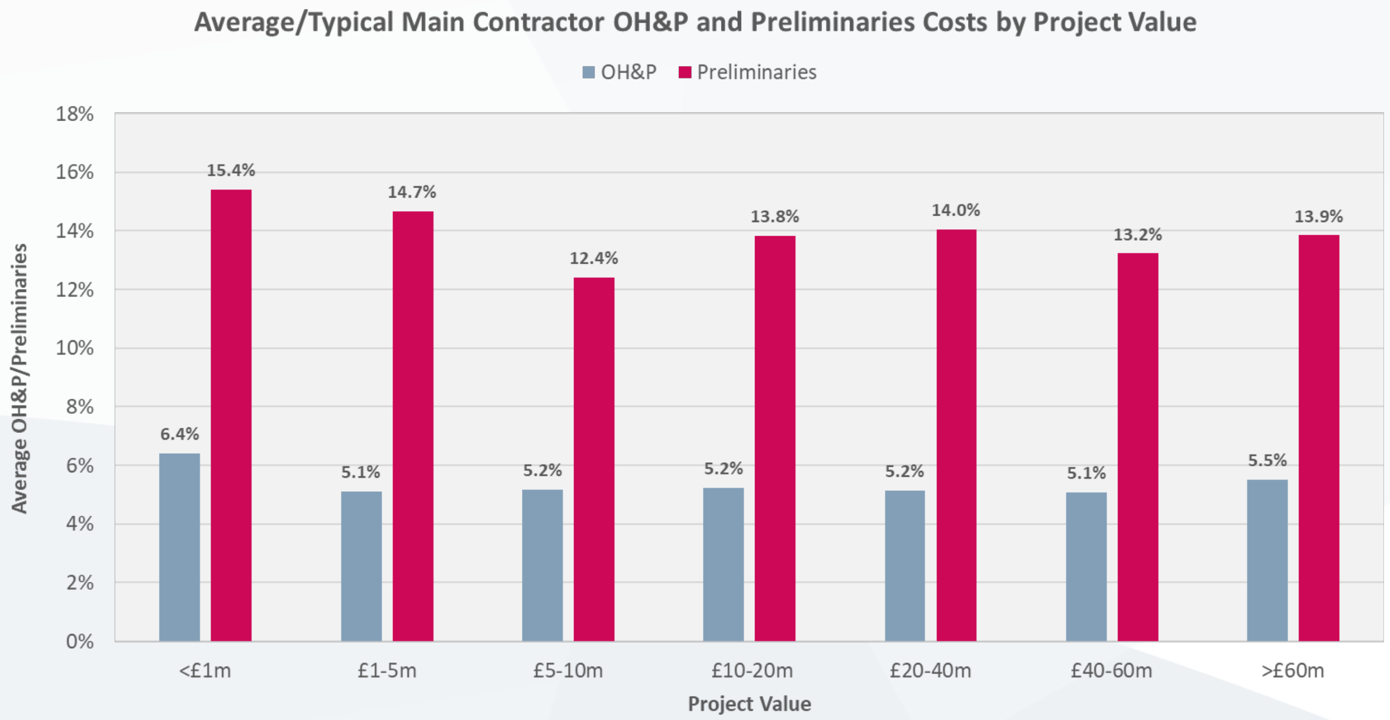




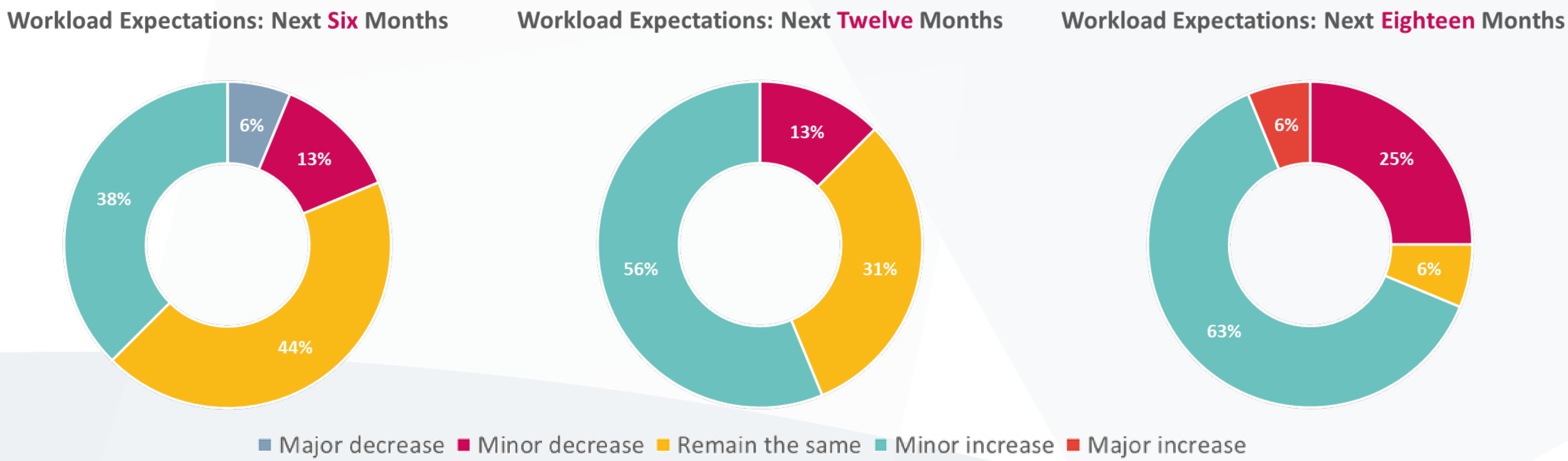
- The average minimum project value across all surveyed contractors was **c.£6.2m**, while the average maximum project value was **£184.2m**
- Six of the contractors were able to deliver schemes with values in excess of **£200m**. The same contractors generally had a minimum project value of **£5m** or more (apart from one, which had a minimum value of **£2m**)
- The average minimum project value was **£6.2m** – some **73%** lower than in our June 2022 survey (**£23m)**. However, it's worth noting that the latest survey does not capture responses from the identical set of contractors as the previous survey
- On average, surveyed main contractors have secured ***88%*** of their workload capacity for 2023 and ***61.6%*** for 2024
- The majority of contractors have secured ***90%*** or more of their workloads for this year with four reporting full capacity or ***100%***

- 2024 has a wider spread of secured workloads, with the some having secured ***c.20%*** while others have secured **86%**
- Secured workloads are marginally higher than they were in our June 2022 survey, where **87%** was the average secured workload figure for the current year (2022) and **56%** for the following year (2023)
- Pipelines remain strong in the short to medium-term but slowing new order growth may impact the ability of contractors to secure workload, creating more spare capacity in the market in 2024 and beyond

Prospect of cooling demand and market activity has seen contractors become more flexible with their controllable costs in order to win work



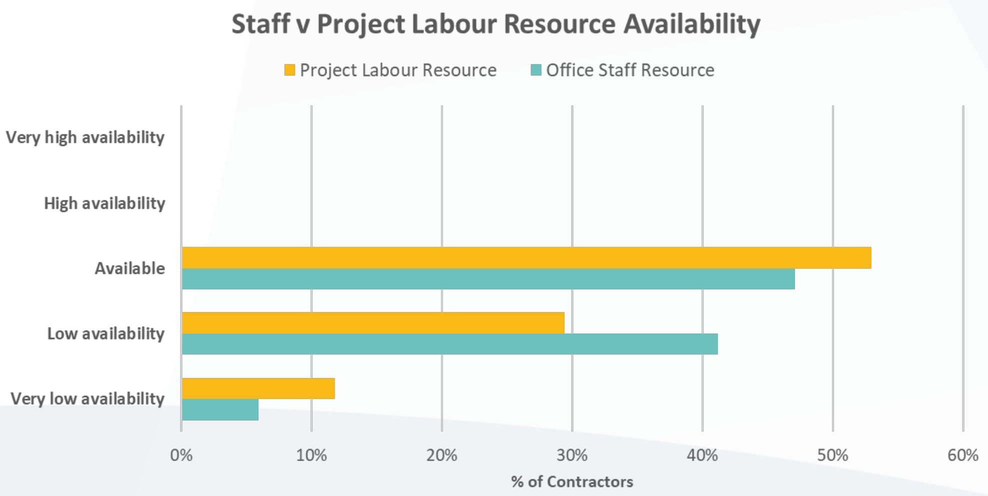
- For the lowest value projects (<£1m), OH&P and preliminaries costs averaged at ***9.3%*** and ***18.6%*** respectively but decreased to ***6.7%*** and ***14.3%*** for projects over £60m
- Preliminaries costs have fallen marginally compared to our previous (June 2022) survey. Across all project values, average preliminaries costs in June 2022 were **16%**. In this survey, the average was **15.5%** operational costs, eg falling fuel/energy prices have started to lower plant costs. However, pressure on wages will keep preliminaries elevated
- OH&P levels have dropped significantly over the last year for all but the highest value projects. Average OH&P across all project values has dropped from **8.7%** in June 2022 to **7.3%** in this survey. This has been driven by the prospect of cooling demand and its anticipated impact on market activity and workloads



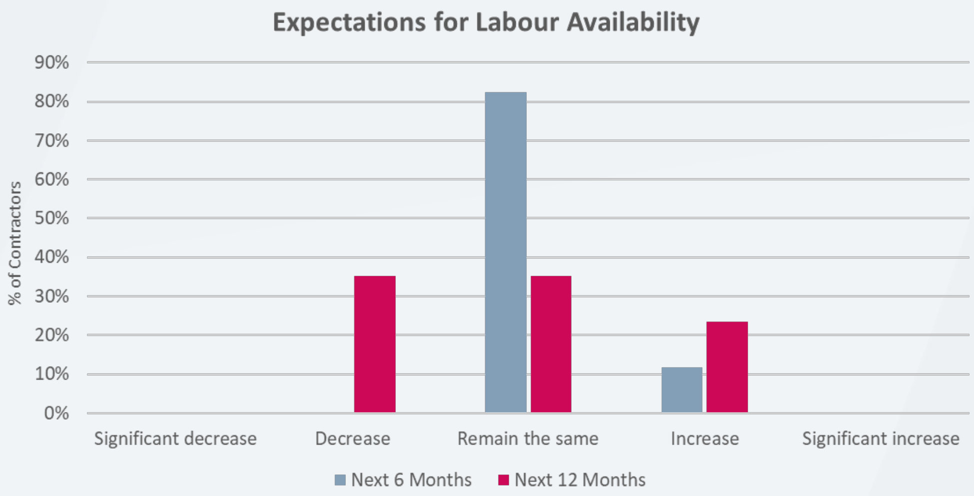
- A significant proportion of contractors remain neutral on workload expectations for the next six months, with **44%** expecting no change from current levels
- Over the next 12-18 months, contractors were generally more optimistic with **63%** of respondents expecting a 'minor increase' in workloads over the next 18 months
- However, a quarter (**25%**) of contractors also thought their workloads would fall over the next 18 months, suggesting a polarisation of views with regards to longer-term workload prospects

Contractors expect strong order books to support workloads in the short-term while hopes for wider economic growth will boost demand in the longer-term. However, with forecasters predicting declines in construction output and new order growth in 2023 and only marginally recover in 2024, workloads for some could fall.

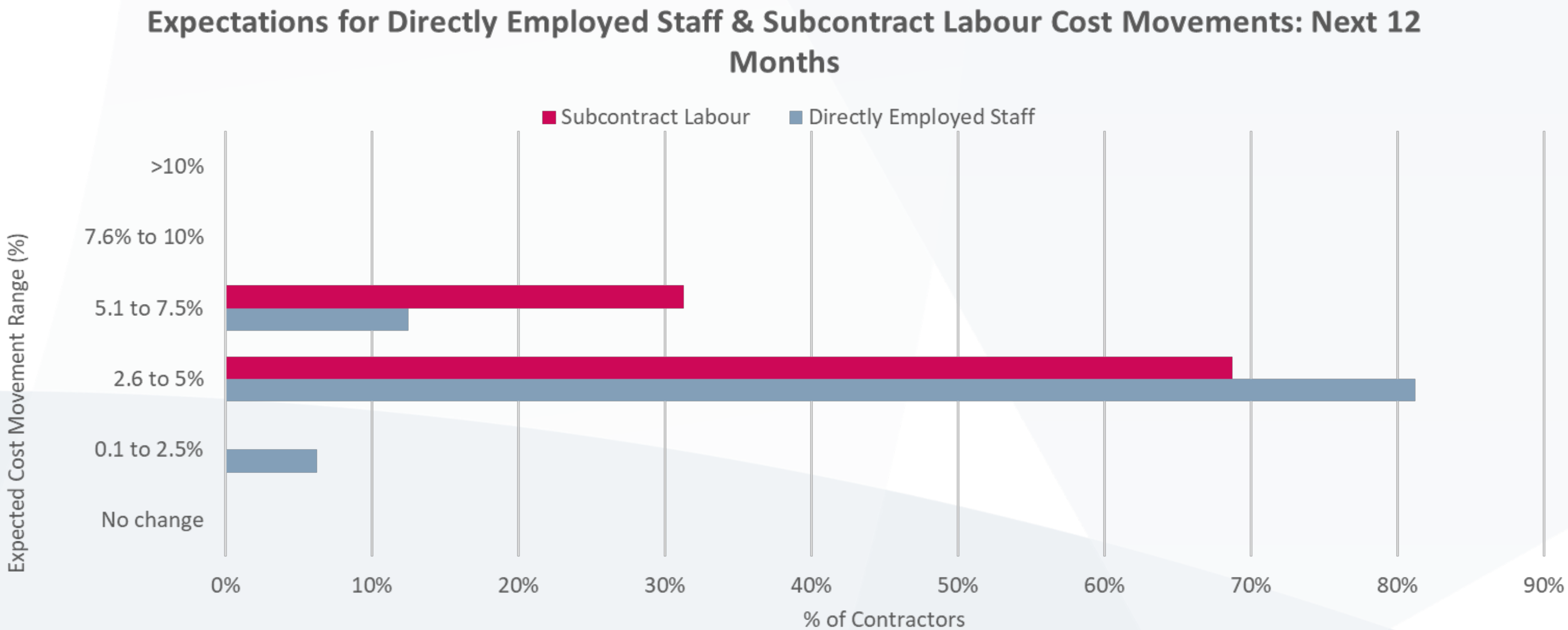
***Note**: The classifications used workload expectations are subjective – influenced by personal opinions, feelings, or perspectives rather than being purely objective or based on factual evidence.*



- Most main contractors (**53%**) still indicate that project labour resource is 'Available', but there has been an increase in the number of respondents reporting 'very low availability' compared to the June 2022 survey
- There has been a significant shift in the reported availability of office staff resource. In June 2022, **73%** of respondents stated that staff resource was 'available', but this figure decreased to **47%** in the latest survey
- The proportion of respondents reporting 'low availability' of staff resource has seen a substantial increase in this survey. While only **18%** reported low availability in June 2022, this number has risen to **41%** in the current survey
- Many explained that labour was a limiting factor to growth at present, noting difficulty in recruiting good quality candidates to fill roles. There is therefore a premium to secure certain trades and staff roles

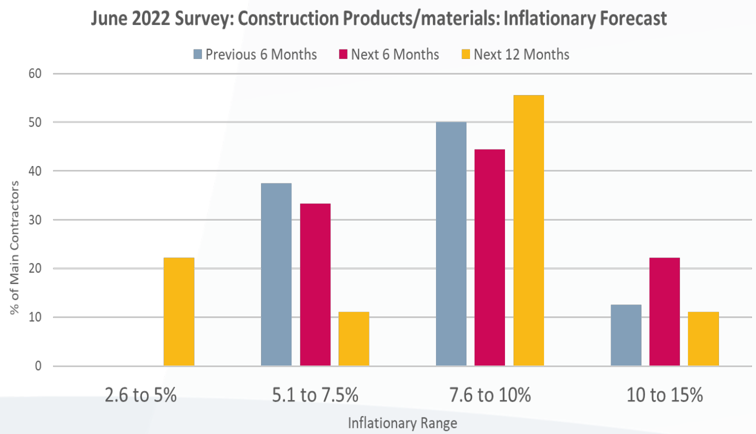


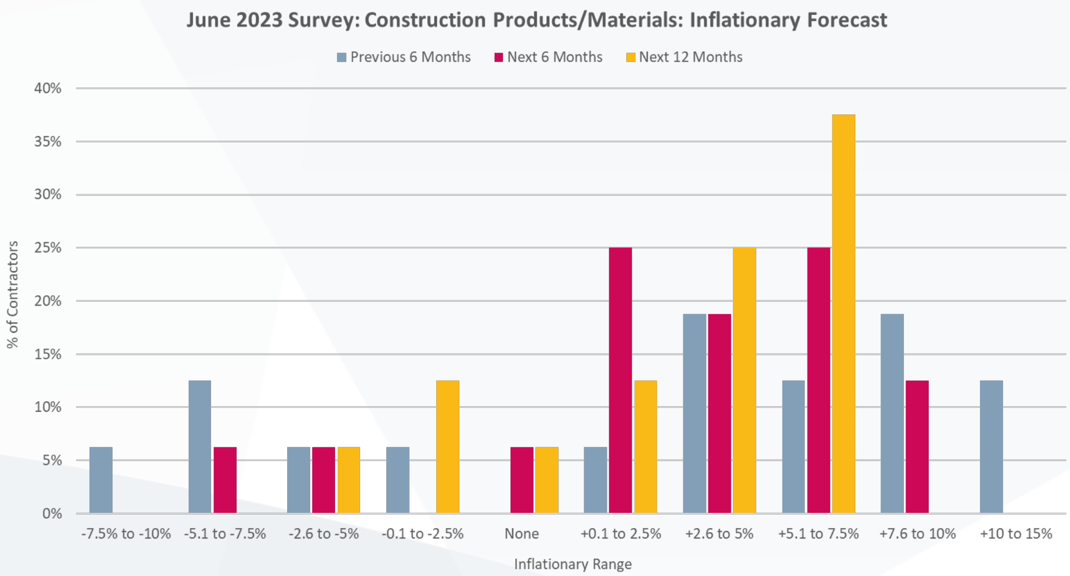
- Most contractors (**82%**) don't expect any changes in the availability of labour over the next six months
- However, over the next 12 months, opinion becomes more split, with **35%** expecting availability to worsen while **24%** expect availability to increase
- The decline of the Eastern European workforce post Brexit was mentioned by some as a contributing factor, while others attributed the current availability issues to increased staff mobility, the poaching of resource driven by supply and demand and pressure on wages to retain labour



- The majority of contractors expect directly employed staff and subcontract labour costs to rise by **2.6%** to **5%** over the next 12 months
- **31%** anticipate that subcontract labour costs will increase between **5.1%** to **7.5%** over the next year. Certain trades are reporting significant skills shortages for which there is no quick fix
- Average weekly earnings in the UK construction rose **6.1%** in April 2023 (on a single month annual basis) but further rises are expected to be a major contributor to construction cost inflation in 2023

"...Post Brexit, good quality project labour resource remains challenging to secure, and there is a significant cost premium to secure certain trades."

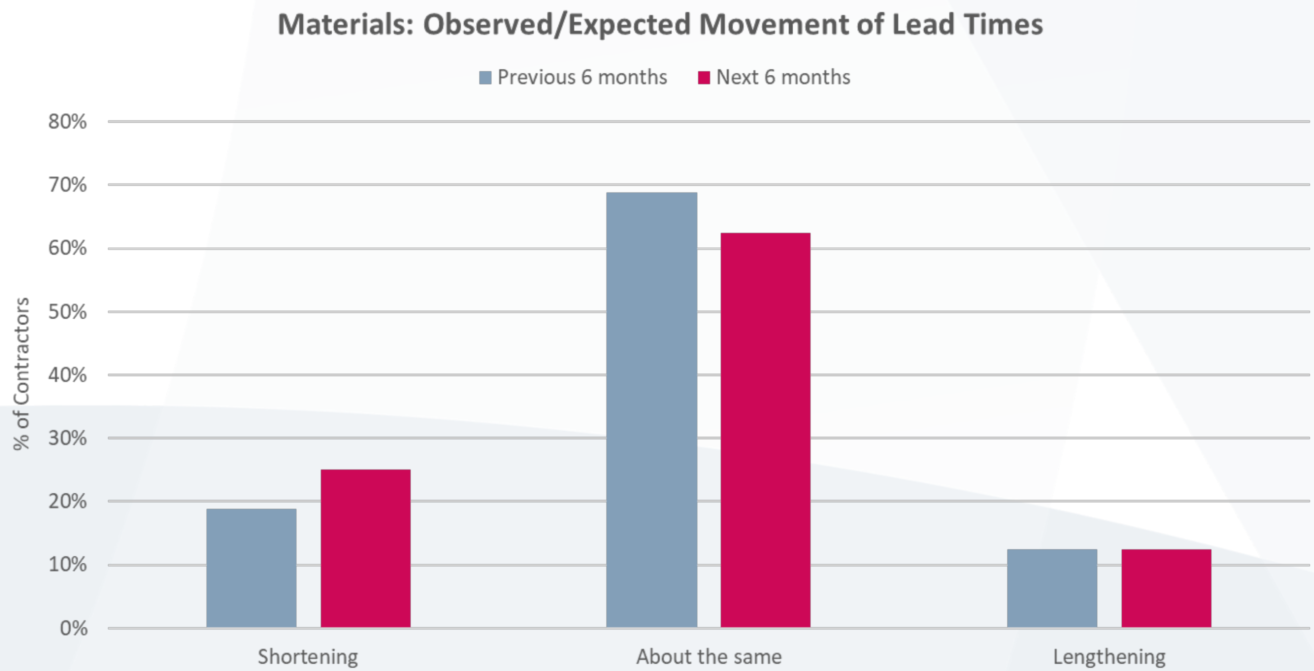




The overall supply picture has improved significantly in 2023. Product availability has mostly returned to pre-pandemic levels, helping material price inflation to soften

- There was a wide range of views with regards to estimated material price inflation over the past six months, but most responses clustered around the ***'+0.1 to 5%'*** and ***'+5.1 to 7.5%'*** ranges
- Most noted that inflation had slowed in the previous six months, but explained that certain materials (ie concrete, insulation, and plasterboard) continued to rise while others (ie steel and rebar) saw significant price falls
- In light of lower energy costs and softer demand, one quarter of contractors expect material price inflation to ease over the next six months (to **'+0.1 to 2.5%'**)
- Over the next 12 months, nearly ***40%*** of contractors anticipate materials inflation will be in the region of **'+5.1% to 7.5%'** – down from an annual inflation rate ***11.2%*** in 2022.*
- There was a **greater spread of inflationary opinions in our 2023 survey** compared to the June 2022 survey, with more contractors reporting lower inflationary rises and falling material prices for each respective period

*According to the *BEIS 'All Work Material Price Index' between Dec 2021-Dec 2022*

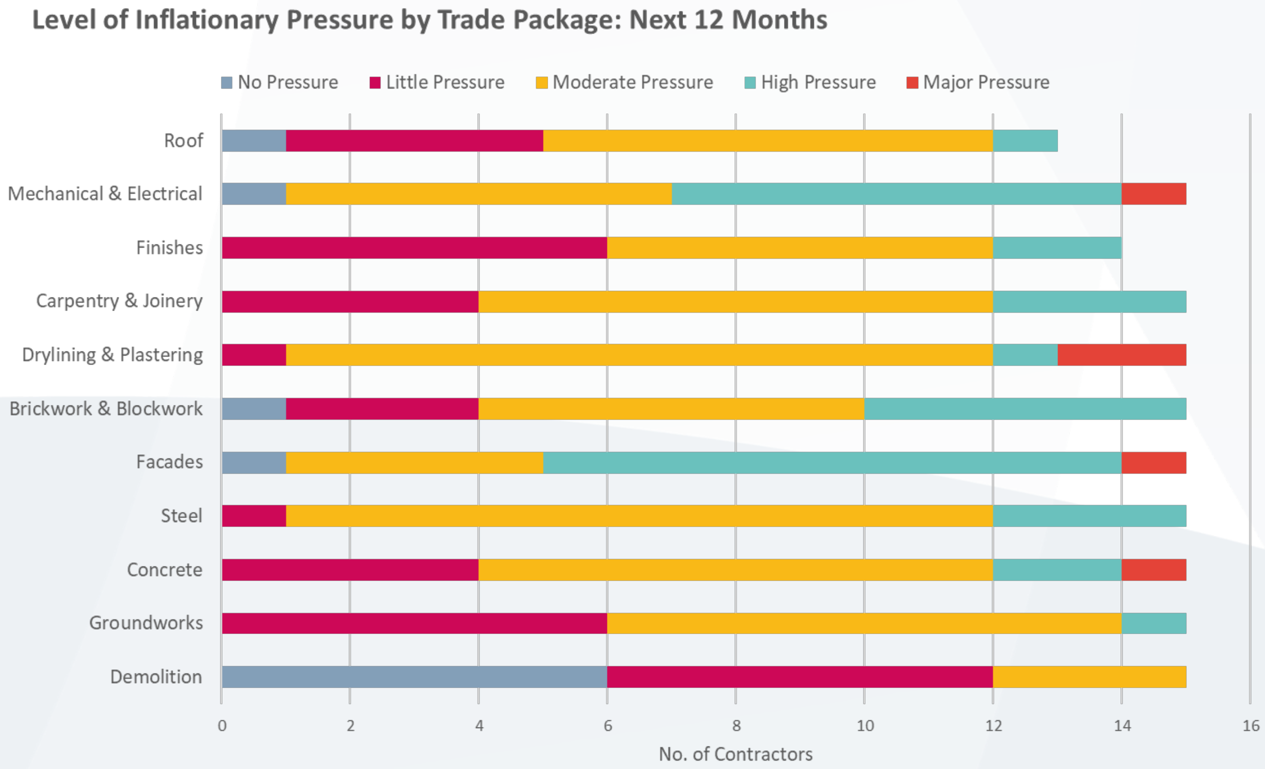


"Most materials are available providing the project cost base is correct and the design is completed early enough to allow for supply chain lead times. Change is however impacted by lead times across all products. Very little is 'off the shelf'..."

- Main Contractors noted increased stability in both observed and expected lead times over the past six months. Materials are generally available within standard lead in periods.
- Over the next six months, **63%** of surveyed contractors anticipate no further changes to overall lead times for materials, while **25%** believe lead times will shorten
- While some noted a continuing impact of the war in Ukraine on lead times, information from their supply chains indicate that lead times are stable. Few are forecasting any significant increases to lead times for the remainder of 2023

Supply issues related to the pandemic and Ukraine war have largely dissipated, but small delays can still crop up and need to be managed for...

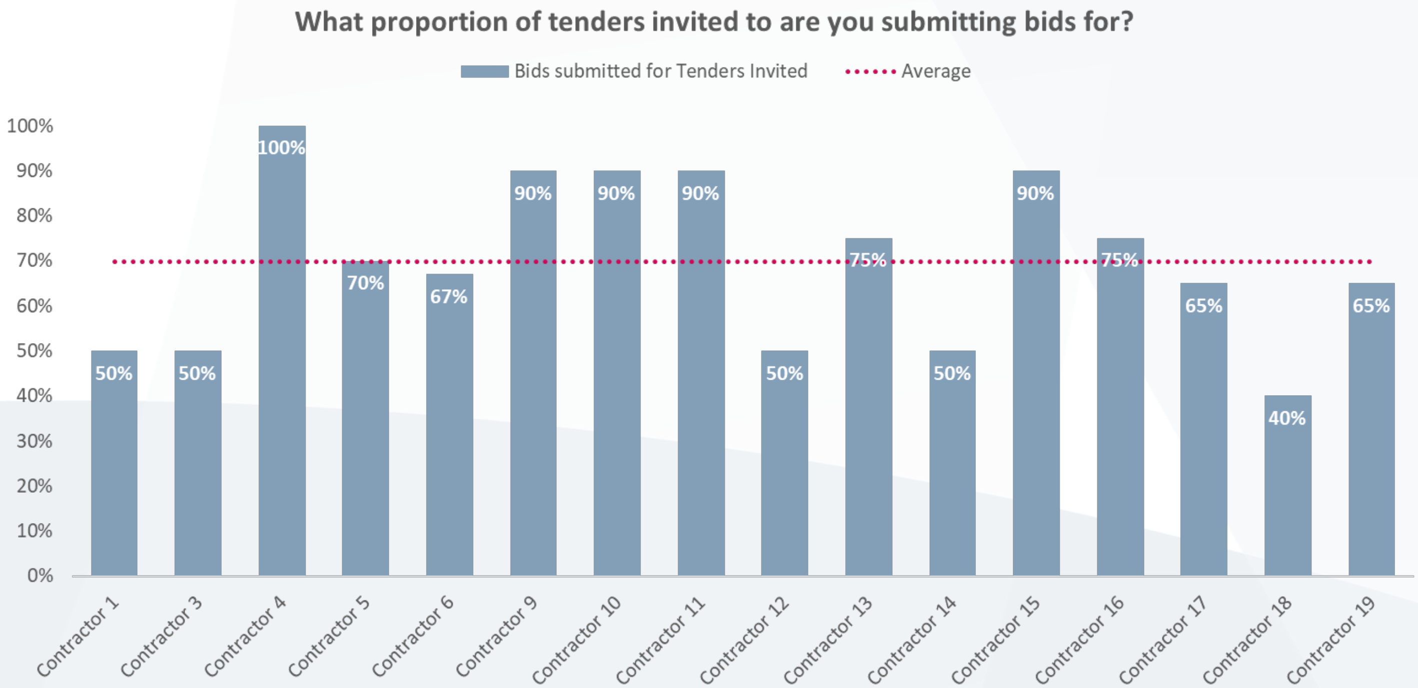
- Electronic Chips
- Batteries
- Component Parts (MEP)
- Insulation (Rockwool)
- Sprinklers
- GGBS
- Cladding



"Sophisticated sub-contractors are not going to reduce pricing levels or their view on risk just because commodity prices may have settled (which may be on a short-term basis), or gas and electricity have come off since the September 2022 peak. That is not enough of a sample size to quell their fears/concerns. Falling input costs will likely take longer to fully wash through, which means pricing will remain high unless workload dries up significantly (through postponement or cancellation)"

- Later trades are facing greater inflationary pressure compared to early trades. While early trades are usually the first to be affected by weaker new order growth, later trades are benefiting from strong workloads carried over from 2022, providing them with ongoing support
- Demolition and groundworks are experiencing the least inflationary pressure due to reduced demand for new build work. However, Facades, M&E and Drylining & Plastering are all under pressure according to contractors
- Most other trades continue to experience a degree of moderate pressure, largely driven by shortages of skilled labour across the board pushing labour costs higher
- Most packages are expected to revert to more typical levels of inflation in 2023, but the view on fixed price inflation risk has not abated (particularly where there is a long programme gap between agreement and these trades starting on site)

- Those trades experiencing the greatest inflationary pressure are also the ones facing the most significant availability issues (ie façades, brick and blockwork, drylining & plastering, M&E etc.)
- Contractors indicated that for façade work packages, labour must be secured well in advance of project start (and can often dictate contract requirements). A lack of façade sub-contractor capacity is making smaller works contracts difficult and is driving labour costs higher
- Brick and blockwork has limited availability, caused by a scarcity of bricklayers. However, bricklayers are likely to be added to new shortage occupation list which may alleviate some availability issues
- Conversely, trades such as demolition, groundworks and concrete all have good availability due to falling demand and lower workloads
- Demolition contractors are more active/hungrier for work as new construction activity eases. On tenders where contractors can secure significant workload, tender prices are competitive



Main Contractors, on average, are currently submitting bids for 70% of the tenders they are invited to.

- While some main contractors continue to be selective, bidding on as few as **40-50%** of tenders invited to, an uncertain growth outlook has encouraged a greater tender submission rate
- On average, main contractors are bidding on **70%** of tenders they are invited to, but a handful are bidding on more than **90%** to secure pipeline and turnover

Main contractors noted the following reasons for choosing not to bid on an opportunity:

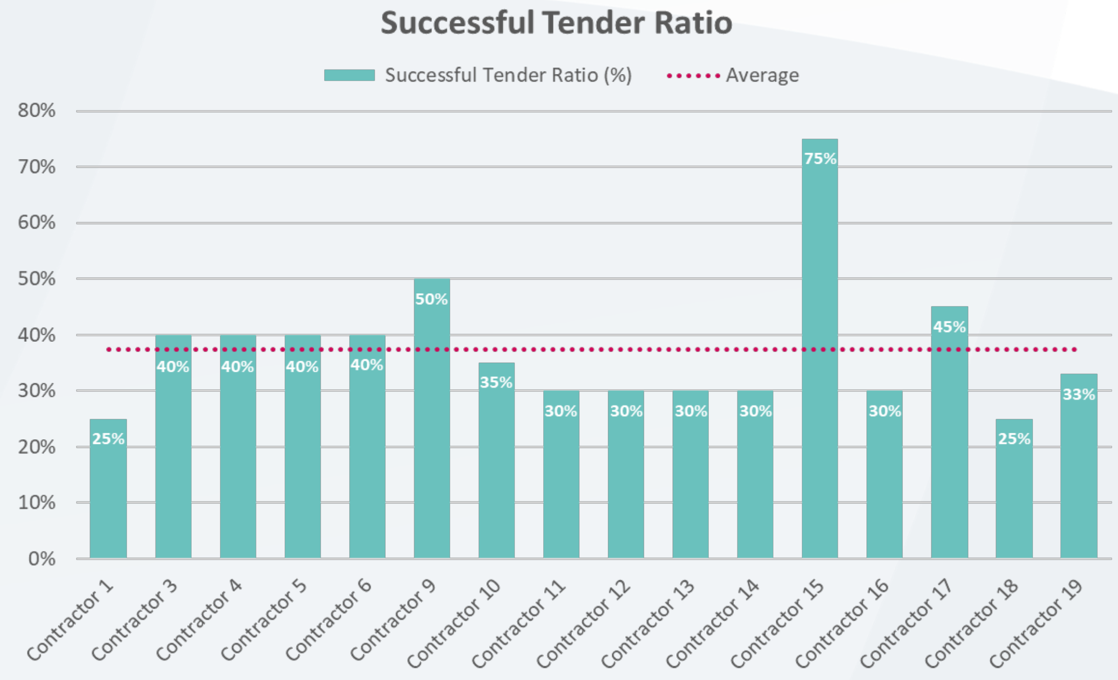
- Lack of bid resource/staff capacity constraints
- Risk profile of the project (and the client's willingness to share risk)
- Lack of two stage tendering
- Poor quality design information
- Not having a proven relationship or successful collaborations with certain clients in the past

Source: *BEIS*

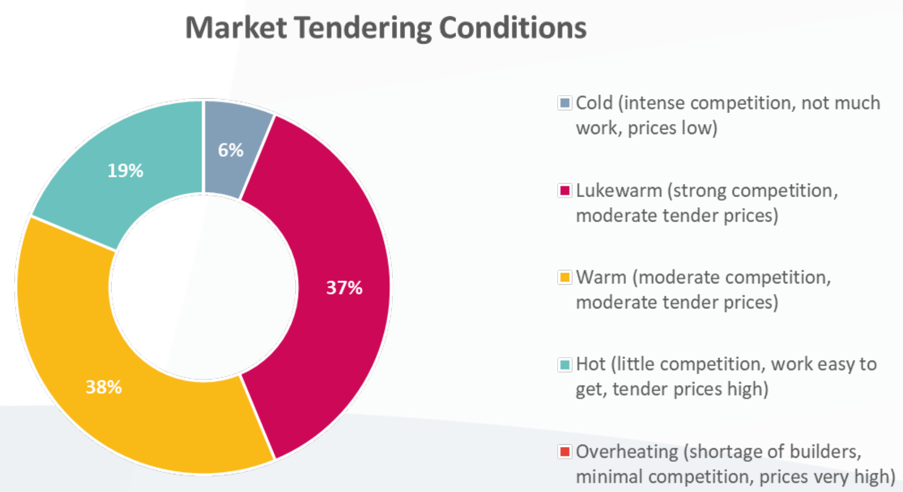
HOW LONG ARE YOU HOLDING TENDERED PRICES FOR?

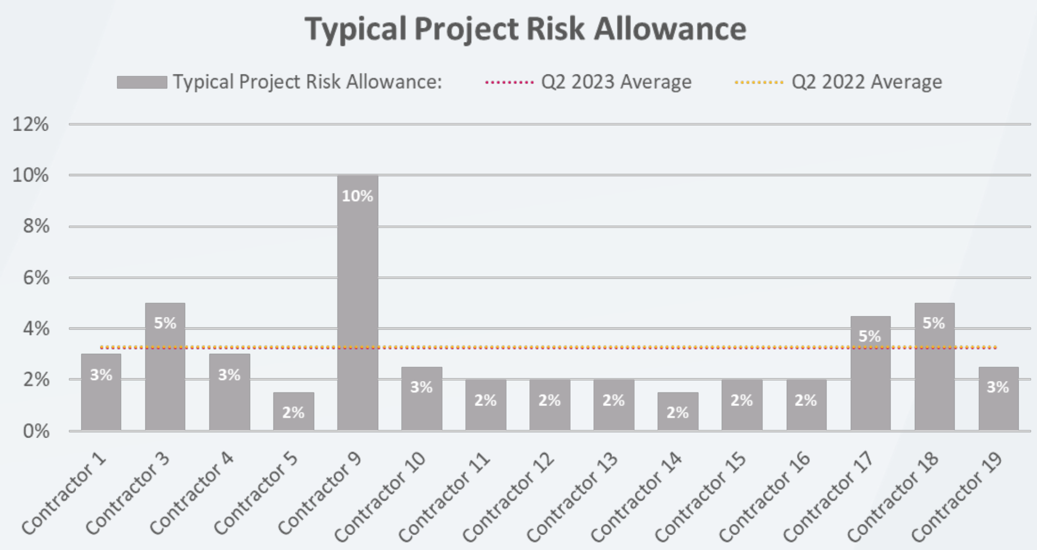
- Most contractors are holding tendered prices from anything between **1-3 months**, but the average period is currently **c.2.4 months (or 9-10 weeks)**
- Several contractors explained there was no simple answer on fixity, and that length of price fixing varied according to intended programme and that if the programme was pushed back, prices were adjusted accordingly
- One contractor noted clients are typically asking for prices to be fixed for **12 weeks**

"Trades are continuing to decline opportunities [to tender] and provide very little fixity unless design allows for material order adjacent to order placement."



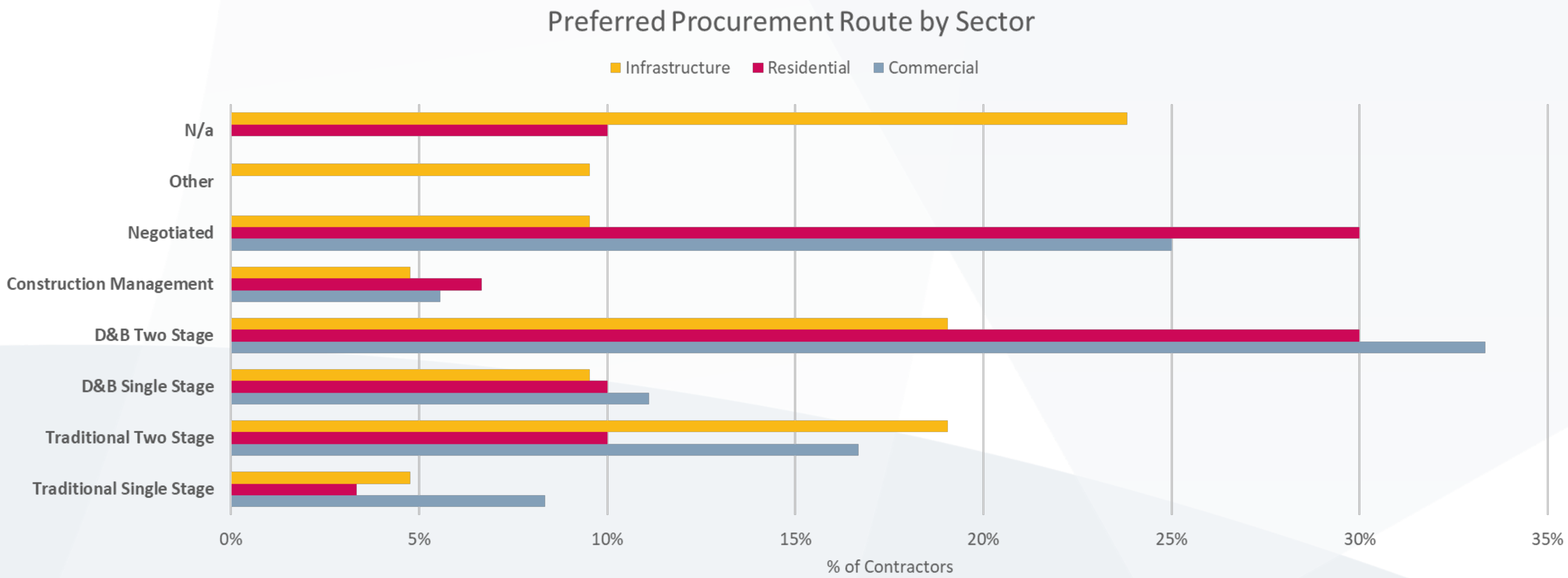
- The ratio of successful tenders (or the 'Bid-Hit' ratio) averaged at ***37%*** but ranged between ***25%*** to ***75%***
- This is slightly higher than the ratio recorded in our 2022 Main Contractor Survey, which averaged at ***36%*** and ranged between ***20%*** to ***60%***
- The higher success ratio may be reflective of a more risk-averse attitude among contractors, creating shorter bidding lists and less competition. The success ratio may have also been impacted by rising contractor insolvencies, eliminating potential competing bidders and increasing success ratios



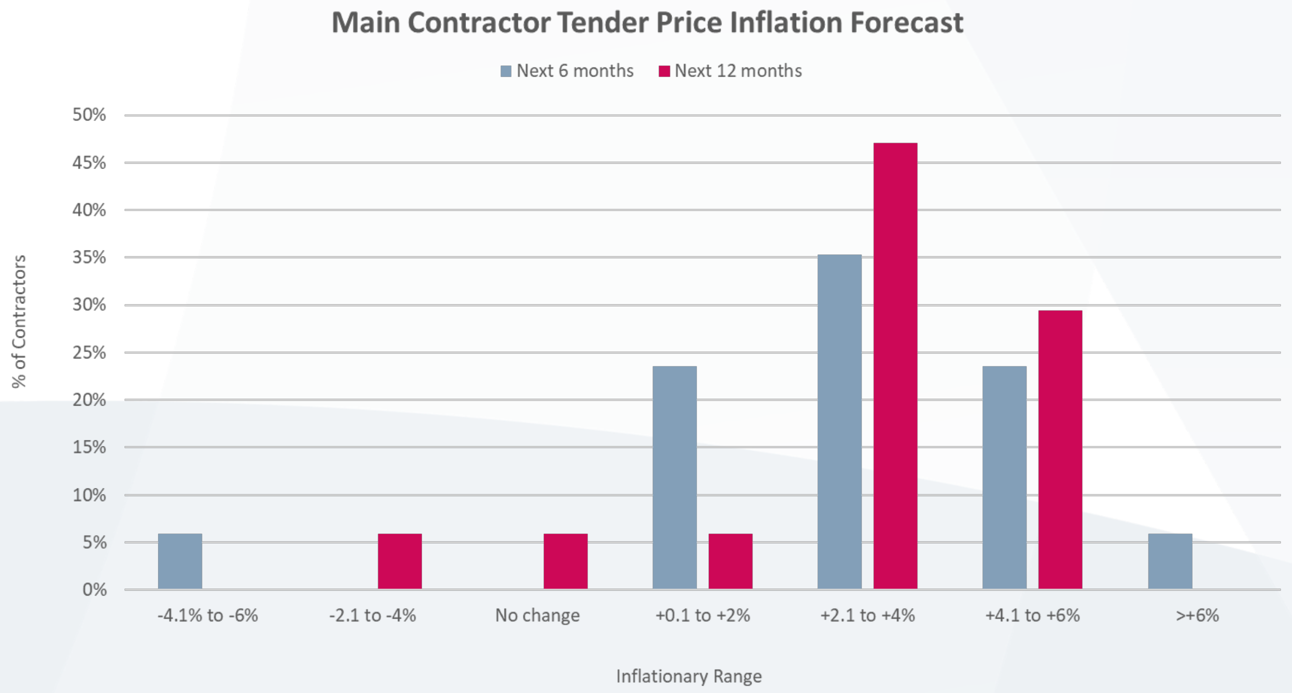


- Most contractors described the current market tendering conditions as either 'Warm' (**38%**) or 'Lukewarm' (**37%**)
- Compared to our 2023 survey, there has been a notable cooling in tendering conditions, with a decrease in the percentage of contractors (**19%**) describing the conditions as 'Hot'. In our previous survey, this figure stood at **25%**
- Unlike our 2022 survey, where **13%** of contractors described tendering conditions as 'Overheating', none of the contractors in this survey characterised market tendering conditions as such

- Average project risk allowances at contract award have dropped marginally, from **3.3%** in G&T's 2022 survey to **3.2%** in this survey
- By removing the outlier response of ***10%***, average risk allowances drop to ***2.8%*** **–** in line with what G&T is seeing in tender returns
- Risk allowance is dependent on multiple factors, including design stage, project type and key risks exposure
- The supply chain remains nervous about further cost volatility and continues to add significant premiums through higher risk allowances to fix prices for projects
- In the current uncertain market, volatility and lingering input cost pressures mean risk allowances are expected to remain elevated to accommodate potential fluctuations



- Given prevailing attitudes toward risk, contractors indicated that **Negotiated** and **Two Stage** continue to be most favored procurement routes for residential and commercial schemes
- With a cooler market and fewer potential bidding opportunities compared to 2022, we may see more clients push for **Traditional Single Stage/D&B Single Stage**. Some clients are biding their time to take advantage of preferential procurement arrangements and a softening of tender prices
- Following recent weakness in new order growth and a softening in construction cost inflation, contractors may be more willing accommodate **D&B Single Stage** to secure turnover in an uncertain market
- Contractors remain wary of being caught out by further price spikes. As such, we may see more 'provisional rates' at the point of contract for projects moving forward
- In this uncertain market, mature clients and suppliers will opt to engage in more collaborative procurement models, where early engagement and progressive fixity (where risk is fully transparent and understood) is likely to become more common. However, this will depend on how projects are funded as most funds require agreed lump sum contracts before commencement on site



"The lack of labour is resulting in many businesses across the supply chain downsizing. This is taking capacity out of the market and increasing prices."

- ***47%*** of contractors expect tender price inflation to increase by '***+2.1 to +4%***' over the next 12 months (compared to **c.70%** that thought inflation would rise '***+4.1 to +6%***' over the next 12 months in our 2022 survey)
- However, nearly one-third of those surveyed anticipate a higher rate of tender price inflation (***+4.1 to +6%)*** over the next year
- Contractor forecasts suggest that annual tender price inflation will be front-loaded, with most of the expected inflationary rise taking place withing the next six months
- Although numerous factors are expected to drive inflation (eg legislation, sustainability premiums, insolvencies, and material prices), tightness in the labour market caused by skills shortages was mentioned by almost all respondents

WHAT STEPS ARE YOU CURRENTLY TAKING TO MITIGATE INFLATION RISK?

SUPPLY CHAIN
Early engagement with the supply chain during the design and procurement process

ORDERS
Early/advanced placement of orders for certain packages and direct engagement with suppliers

PARTNERING
Partnering arrangements with certain supply chain members (ie façades and MEP packages)

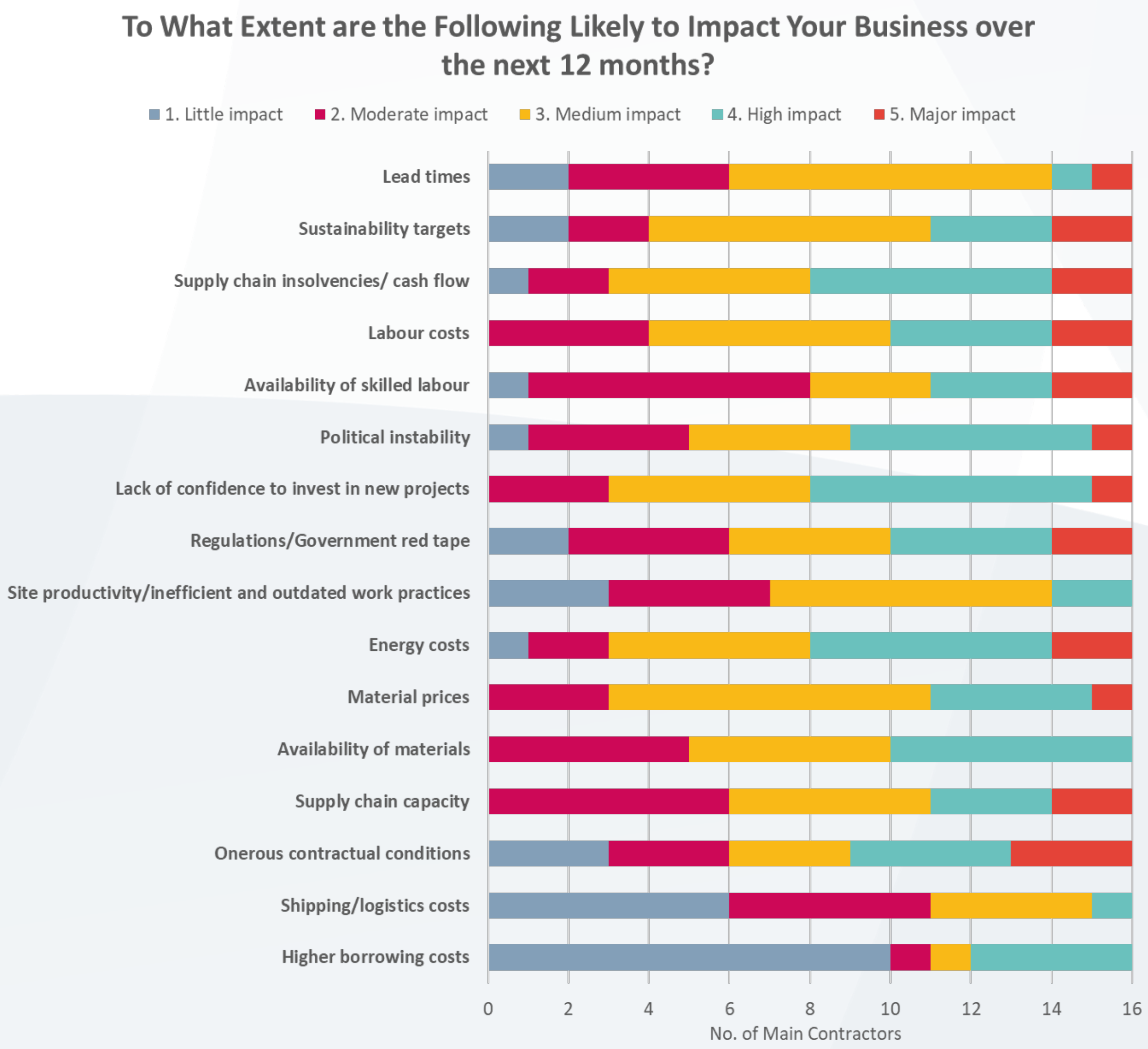
MONITOR THE MARKET
Monitoring the market, maintaining close contact with suppliers and trade bodies

ALTERNATIVE PRODUCTS
Researching alternative products and specifications of materials, as well as utilisation of MMC

DESIGN
Amending design elements early on to help mitigate areas subject to more volatile cost pressures

CONTRACTUAL PROVISIONS
Incorporating contractual provisions that allow for the sharing of inflation risks and potential benefits with clients

OPEN BOOK PROCUREMENT
Embracing open book procurement and transparency across a managed supply chain



In G&T's 2023 survey, main contractors said that:

Supply chain insolvencies/cash flow and energy costs

were likely to be **two of the biggest issues** faced by businesses over the next 12 months.

This was followed by:

- **Lack of confidence to invest in new projects** and
- **Concerns over onerous contractual conditions**

Labour and material-related issues, as well as supply chain capacity were also significant concerns.

What market pressures are driving construction prices?

- High volume of opportunities across most sectors mean **contractors can still pick and choose** which tenders to pursue
- Higher **staff and labour costs** driven by availability issues and cost-of-living pressures
- Lack of labour resulting in the **supply chain downsizing**, taking capacity out of the market and increasing prices
- Reduced contractor **appetite for risk**
- Societal **shift away from demolition and new build**, towards re-use of existing buildings (sustainability/carbon driven)
- War in Ukraine causing **energy price destabilisation** and potential for further volatility
- Forecasted inflationary rises mean **sub-contractors are not fixed to any degree** and main contractors pass this on
- Drive towards **sustainable solutions and deconstruction methods** (with corresponding time and cost premiums)
- EFC GGBS (ground granulated blast furnace slag) and reclaimed steel are putting **extra costs on tender pricing**
- Although much improved, there are **some availability issues** with certain materials and products
- Higher **borrowing costs** reducing **availability of funding** and raising questions over Government public sector spend
- Uncertainty over **legislation** (eg implementation of the Building Safety Act)

“We are seeing a drive towards sustainability and deconstruction methods which comes at a premium in both time and cost.”

Are you currently embracing any strategies to secure work?

- Securing **repeat business with existing** clients that are well established and financially secure
- For unknown clients, lengthy and rigorous **financial checks are undertaken** to mitigate risk
- Seeking **synergy with client's aspirations** on carbon
- Prioritisation of sectors with **limited competition** (eg ports & harbours, marine work, defense, and healthcare)
- Greater focus on **emerging and growth markets** (ie life sciences, health and data centres)
- Focusing on projects that **utilise in-house group companies** that best allows contractors to control supply chain for manufacturing and on-site installation
- Working to **identify projects with a clear mandate**, are **fully funded** and are **likely to progress** beyond tender stage
- Consideration of **Government-backed schemes** (healthcare, education) framework procurement routes
- Providing clarity of tender deliverables and clear tender documentation (ie a reliable BoQ)
- Targeting **specific procurements routes** (eg two stage and negotiated) to reduce business risk
- Declining bids for projects with **budgets that look too low for the scope of the work** so are likely to suffer distress during the project development
- Getting to **know the client and the project team** ahead of the bid to raise the chance of bid success
- **De-risking projects** through utilisation of MMC and C2P (Construction-to-Permanent loan financing)
- Avoiding projects with **higher risk profiles**, **long construction programme periods** or **onerous contractual conditions**

"We are focusing on servicing repeat business clients and working hard to identify those projects which are funded and likely to progress beyond a tender stage. Quite often tenders stall once received due to finding and/or commercial viability."

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