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MARKET UPDATE

August 2021

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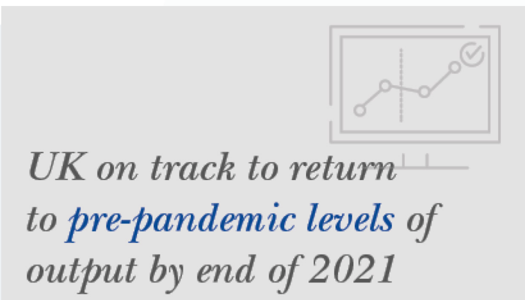
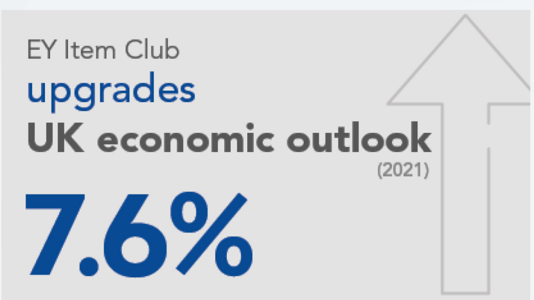
G&T's Market Update for August 2021 provides an overview of the UK construction market. Against a backdrop of ongoing disruption caused by the coronavirus (COVID-19) pandemic and new Brexit trading rules, our latest report highlights changes to key macro-economic indicators over the reporting period, as well as construction-specific metrics such as the IHS Markit/CIPS UK Purchasing Managers' Index (PMI) construction output, new orders and key material costs. We also outline our latest trade package and tender price inflation forecasts based on our quarterly surveys and regular discussions with the supply chain.

In this update we:

- Review some of the factors putting upward cost pressure on rising input costs as workloads rise
- Provide our insights and forecasts on trade package inflation for the next 12 months
- Analyse the ONS' Business Insights and Impact on the UK Economy dataset in order to gain an insight into the impact of the pandemic on turnover, trade and employment

Please note – whilst our Market Update uses the most recently published data at the time of writing, release schedules between datasets differ. This inevitably means that not all datasets will cover identical periods.





The UK economy surged forward in Q2 2021, growing **4.8%** as consumer spending picked up and COVID-19 restrictions began to ease.

The rapid quarterly growth rate allowed the economy to recover much of the lost ground over the past two years. Although output is still below the pre-pandemic level, the economy is on track to return to these levels before the end of the year and emerge from the pandemic with less long-term scarring than had been initially feared.

The Bank of England's Monetary Policy Committee (MPC) expects the economy to grow by **8%** in 2021 - up from its previous forecast of **7.25%** - but it warned that with this robust recovery, inflation will hit **4%** this year. However, it noted that the above-target rise was likely to be temporary and will begin to wane "as commodity prices stabilise, supply shortages ease and global demand rebalances," pushing down price growth next year towards its **2%** target.

Having peaked at **5.2%** in the Oct-Dec 2020 period and fallen gradually since, the BoE's upbeat assessment suggests that there will be no negative fallout from the ending of the furlough scheme in September. Wage rises, which it said were averaging **3.5%**, would also remain strong.

In its Summer Forecast the EY Item Club upgraded its economic outlook and it now expects the economy to grow by **7.6%** this year (previously **6.8%**).

- Business investment to lag economic performance, with growth of **3.1%** this year, albeit followed by a much stronger outlook (**12%** growth) in 2022
- UK is well-placed to reap a strong bounce-back in growth but because the economy shrank so much compared to most of its peers means there's more lost ground to make up
- Fiscal policy remains in loosening mode, while the Chancellor may be able to rein back planned future tax rises and spending cuts if the economy recovers more strongly than the Office for Budget Responsibility (OBR) expects
- Involuntary household savings expected to drive consumer spending
- Technical factors, combined with supply disruption connected to the reopening of economies globally, will push inflation up further during the rest of this year and into 2022. But other influences, including the stronger pound, will keep a lid on price pressures. The ingredients needed to support sustained high inflation appear to be lacking.

UK Construction activity expanded rapidly in both May and June, when it reached a 24-month high of 66.3. But output lost momentum in July (with the IHS Markit/CIPS UK Construction PMI falling to 58.7) and slower growth was seen across all three main sectors (residential, commercial and civil engineering).

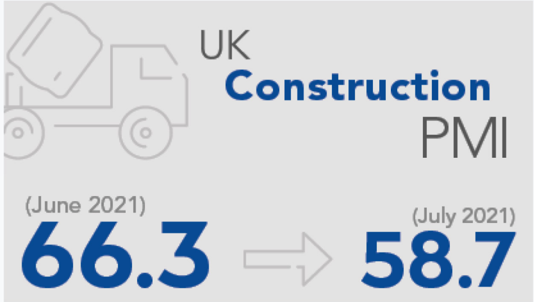
There were reports of difficulties in keeping pace with high workloads and a surge in demand for projects, especially in light of the ongoing material supply shortages and the shrinking availability of sub-contractors.

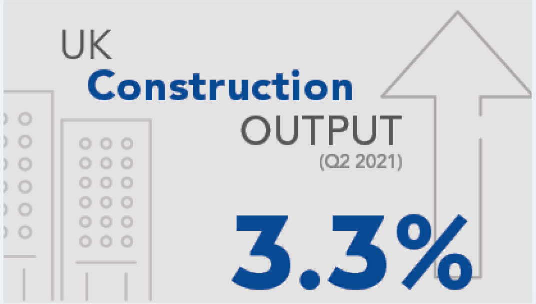
Reduced availability of materials acted as a brake on purchasing volumes and on output growth. Difficulties in filling staff vacancies is also holding back construction activity and adding to price pressures but despite capacity concerns, new orders continue to rise sharply.

While there are signs that the initial spurt of activity in the first half of 2021 appears to be coming off the boil, optimism toward future output growth remains historically high.

According to the latest ONS data:

- UK construction output ('All Work') rose by **3.3%** in Q2 2021 compared to the previous quarter, driven in part by new work growth. However, construction output growth was some way below the economy overall at **4.8%**
- The low base effect meant that construction output grew by an average of nearly **60%** across all regions in the UK in Q2 (year-on-year)
- On a monthly basis, construction output fell for a third successive month in June, declining by **1.3%** compared to the previous month – a sign that capacity issues and supply shortages are starting to bite
- Following two consecutive quarters of decline, total construction new orders grew by **17.6%** (or £1,998m) in Q2 2021 compared with the first quarter
- New orders rose above their pre-pandemic level for the first time in Q2 2021, with the infrastructure and commercial sectors being the biggest drivers of growth





Material Price Index (All Work)

20.1%

(July 2020 - July 2021)

Ongoing inbalances between global supply and demand

Supply chain **pressures** holding back work on site

The basic trends of the last six months remain. Ongoing imbalances between global supply and demand have given rise to higher prices for a wide range of construction products and materials. Furthermore, a severe lack of haulage availability is causing transportation costs to rise and lead times to extend.

- The ONS' material price index for **'All Work'** rose by ***20.1%*** in the year to July 2021. Inflationary rises are no longer a short-term problem and are creating challenges for businesses across the supply chain
- Contracts being signed for delivery now for delivery in 2022 will face challenges in sourcing materials. These challenges could be exacerbated if there are no contractual mechanisms in place to recover cost inflation and so organisations should look to include price adjustment clauses to help manage the issue
- While some shortages for items produced in the UK should be resolved in the coming months, steel and timber shortages could last longer and support sustained inflationary pressure as they are both imported and impacted by international demand and shipping costs
- Official BEIS data revealed that both fabricated structural steel and imported timber prices for sawn or planed wood have increased by more than **64%** in the year to July 2021
- Some key commodity prices have begun to stabilise or fall in recent months. Copper prices are down from their highs in early May and Iron ore prices fell by **28%** in the month to 17th August. Timber futures have also plummeted by more than **70%** from their record-high in May to mid-August
- However, with retailers still selling inventory bought at higher prices these commodity price falls are not yet being passed on down the supply chain. With demand so strong, there is little reason to immediately lower prices
- Contractors are managing the situation by collaboratively working with suppliers, helping all parties better understand forward demand and taking mitigating actions to help alleviate pressure on suppliers
- With the severity of widespread shortages yet to peak, further material prices rises are expected. In fact, a recent RICS survey indicated that surveyors expect material prices to rise by around **10%** over the next year – significantly higher than expected annual tender price inflation

Resurgent Consumer Spending
Consumer spending rebounded to pre-pandemic levels in July - up **11.6%** compared to the same period in 2019

OECD Projects Strong Economic Growth
OECD upgraded its UK GDP growth forecasts to **7.2%** (2021) and **5.5%** (2022)

PRS Demand Growing
Residential demand spurs increased investment in high rise construction projects outside of London

Commodity Prices Stabilising
Prices for some key commodities such as iron ore, copper and timber have **fallen from their peak**

UK Construction PMI 58.7 *(July 2021)*
Down from an all-time high of **66.3** in June amid supply bottlenecks

CPI 2% *(July 2021)*
Annual inflation eases back from three-year high, helped by a low base effect

0.1% Base Interest Rate
Base rate held but BoE could raise rates sooner than expected

Strengthening trade with EU
UK growth in exports to EU bucks trade deficit trend

4.8% UK GDP
UK economy grew 4.8% in Q2 2021 - the fastest Q2 quarterly growth seen in the G7

4.7% Unemployment Rate *(Apr – Jun 2021)*
Unemployment rate on a downward trend, suggesting unfurloughed workers are not moving into unemployment

14.3% UK Construction Earnings
Average weekly earnings in Construction (Y-on-Y three month average) rose **14.3%** in June 2021

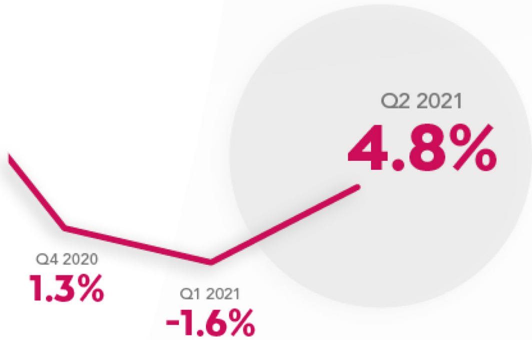
Source: *Barclaycard, ONS, OECD*

UK Economy

Overview	Actual	Forecast Q3/21	Q4/21	Q1/22	Q2/22	Units
GDP Growth Rate	4.8	2.5	1.1	1.4	1.2	%
Unemployment Rate	4.7	4.8	5.1	4.9	4.7	%
CPI (Annual Rate)	2.0	2.3	2.1	2.2	1.9	%
RPI (Annual Rate)	3.8	3.7	3.4	3.6	3.2	%
Interest Rate	0.1	0.1	0.1	0.1	0.1	%
GDP from Construction	29,812	30,218	30,307	31,839	31,332	GBP Million
Government Debt to GDP (the ratio between a country's government debt (cumulative amount) and its GDP)	97.4	107	107	110	110	%

Source: *Trading Economics and ONS*

Please note: *The economic forecasts provided above have been sourced from Trading Economics. These forecasts are updated periodically and do not necessarily reflect G&T's UK economic outlook. The 'Actual' column indicates the latest confirmed figures at the time of writing in August 2021.*



GDP: Quarter on Quarter Growth: Chained Volume Measure Seasonally Adjusted

The UK economy rebounded strongly from its winter lockdowns with GDP jumping by **4.8%** in Q3 2021. Growth was supported by the easing of restrictions and reopening of hospitality venues, spurring a recovery in consumer spending. However, the economy is still **4.4%** smaller than it was in Q4 2019

UK GDP From Construction

GDP from Construction in the UK increased by **2.3%** in Q1 2021. However, GDP from construction still remains some **1.5%** lower than it was one year ago

Construction Productivity Index: Output per job (Q1 1990=100), SA, UK

The ONS Construction Productivity Index rose by **2.2%** in Q1 2021, meaning that productivity is now broadly on par with pre-pandemic levels. While construction sites may keep some precautions in place CLC site 'SOP' guidance is no longer current, which may provide a boost to site productivity

***Please note** – Chained Volume Measure (CVM) means that data from successive years has been put in real (inflation-adjusted) terms by computing the production volume for each year in the prices of the preceding year, and then 'chain linking' the data together to obtain a time-series of production figures from which the effects of price changes (ie monetary inflation or deflation) have been removed.*

***Source:** Trading Economics and ONS*

Europe

The eurozone's economy emerged from recession in Q2 2021, growing by **2%**.

The 19-bloc nation suffered from a double-dip recession after contracting in the previous two quarters but individual economies reported growth in Q2.

GDP remains **3%** down from its pre-pandemic level in late 2019 but strong growth is expected in Q3 as business and consumer confidence continues to rebound.

Bottlenecks and supply constraints continue to impact eurozone manufacturers, pushing up prices of manufactured goods. Accordingly, inflation in the bloc rose faster than most economists had expected to **2.2%** in July - above the ECB's target of **2%**.

The ECB expects eurozone GDP to reach **4.6%** by the end of 2021, followed by **4.7%** next year.

US

US GDP rose by **1.6%** in Q2 (or **6.5%** on an annualised basis), bringing output back above its pre-pandemic level for the first time since COVID-19 struck.

Labour shortages and supply chain disruptions are acting as a drag on what is otherwise a robust US expansion supported by strong consumption. However, surging prices could weaken purchasing power and cause GDP growth to slow in Q3.

The Biden administration's $3.5tn budget plan may have further inflationary effects but some argue that most things in the spending bill should increase the capacity of the economy and create efficiencies, helping to moderate inflation. However, the plan's 10-year time horizon will limit its immediate economic impact.

The IMF raised its US growth forecasts to **7%** (2021) and **4.9%** (2022).

China

The Chinese economy advanced **7.9%** year-on-year in Q2 2021.

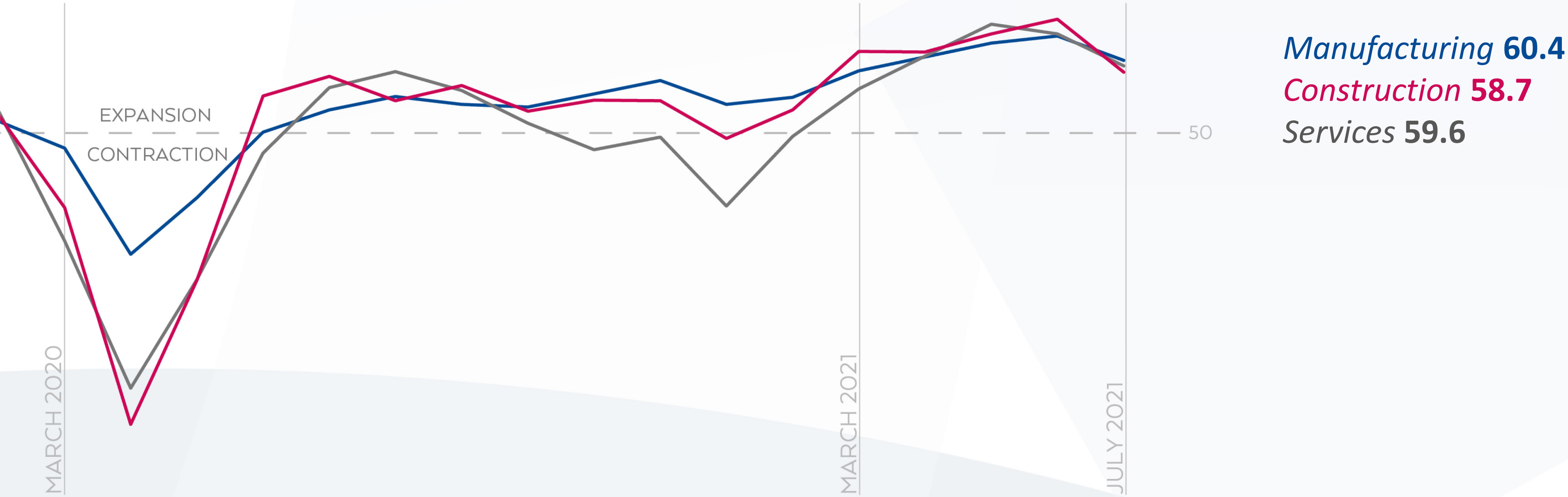
A slowdown in factory activity, higher raw material costs, and new COVID-19 outbreaks in some regions all weighed on growth.

China has set an economic growth target of "above **6%**" for 2021. However, widespread flooding, coronavirus outbreaks and an expectation that consumers globally will start to spend more on services (hitting China's export sector) could impact the country's growth trajectory in the second half of 2021.

China's factory output growth slowed sharply in July. Producers are grappling with higher costs, supply bottlenecks and production controls, which has resulted in a slump in export growth.

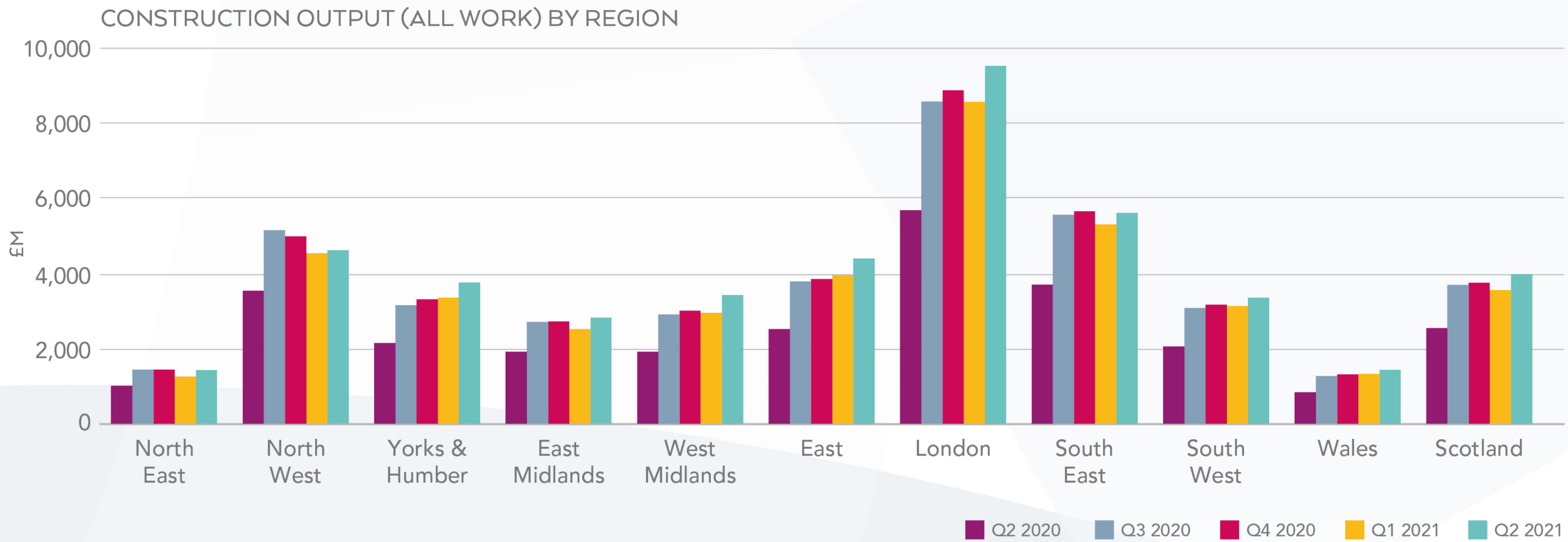
The IMF reduced its 2021 growth forecast to **8.1%**, citing a scaling back of public investment and overall fiscal support.

*** The PCE** *(or 'Personal Consumption Expenditures') price index is a measure of the prices that people living in the United States pay for goods and services. It captures inflation across a range of consumer expenses.*



- Slowest overall increase in construction output since February, amid difficulties in keeping pace with the recent surge in demand for construction projects, raw material supply shortages and rapidly shrinking sub-contractor availability.
- Slower output growth was seen across all three categories of work with housebuilding being the best-performing category, followed closely by commercial.
- Total order books continued to improve but new work rose the least since March 2021.
- The rapid pace of input cost inflation continued in July, fuelled by supply shortages and robust demand for construction items.
- Higher charges from sub-contractors and difficulties filling construction vacancies added to price pressures
- Reduced materials availability acted as a brake on purchasing volumes and around **66%** of the survey panel reported longer wait times for supplier deliveries
- Supply chain delays were amplified by a lack of transport availability, port congestions and Brexit-related trade frictions.
- The pace of hiring at construction firms remained strong, reflecting rising new orders and confidence regarding the near-term outlook.
- Business confidence eased to a six-month low but remained strong by historical standards.

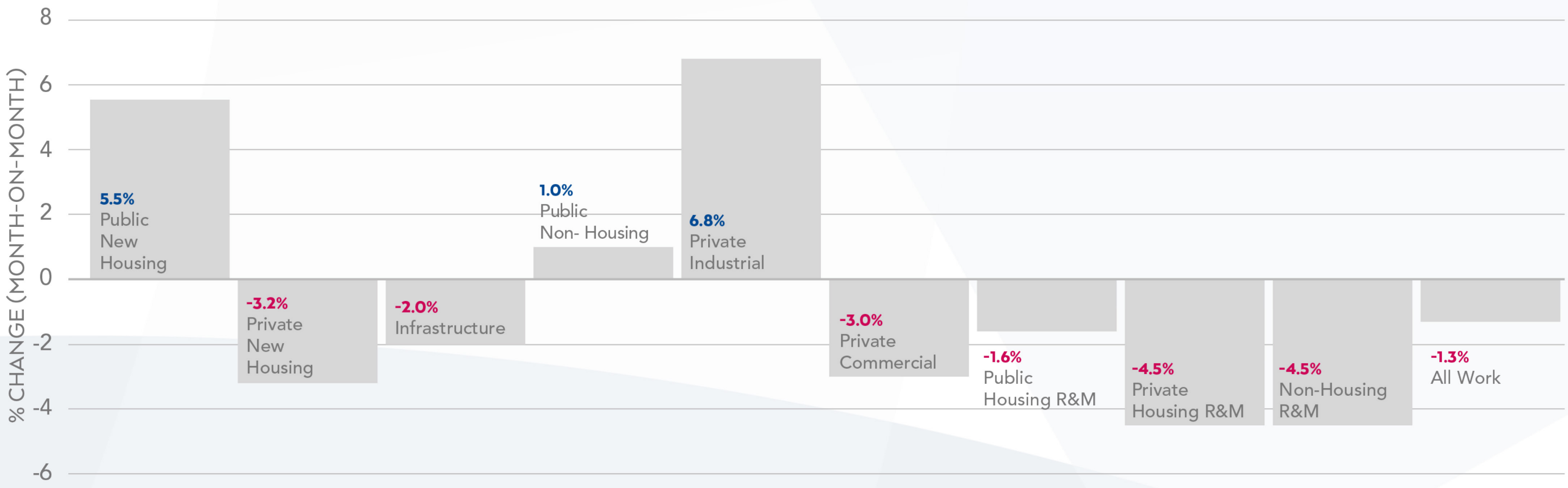
Source: *IHS Markit/CIPS*



- Construction output ('All Work') across all regions in Q2 2021 grew by an average of nearly **60%** compared to the same quarter one year earlier.
- However, this significant increase was due to the low base effect as construction activity on site was suspended for a period during the first lockdown.
- For most regions, Q2 2021 was the best performing quarter over the past year in terms of output growth. Only the North East, North West and South East regions experienced lower quarterly output growth in Q2 than they did in previous quarters over the last year.
- Comparing Q1 2021 to Q2 2019 output, five regions have exceeded their pre-pandemic quarterly output levels: Yorks & Humber, East, London, South West and Scotland.
- Almost all other regions in Q2 2021, apart from the East and West Midlands, have nearly returned to their Q2 2019 (pre-pandemic) levels of output.
- Across all regions most output growth has come from a handful of key sectors; namely the private residential, infrastructure and private industrial sectors. These sectors have led the recovery in output.

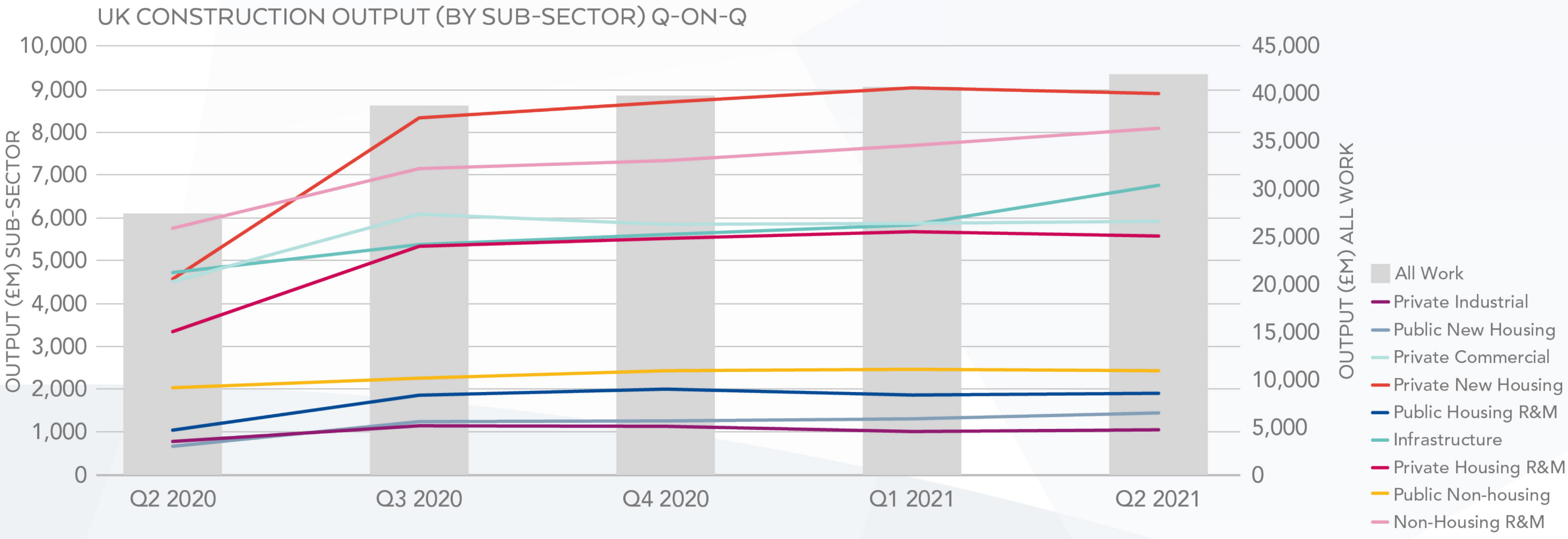
Source: *ONS*

ONS UK CONSTRUCTION OUTPUT (JUN 2021 V MAY 2021)



- Construction output ('All Work') fell for a third successive month in June, declining by **1.3%** compared to the previous month.
- Monthly construction output fell by £178m in June due to a **4.2%** decline in repair & maintenance (R&M) work. This was partially offset by a **0.5%** increase in new work that was driven by the public new housing and private industrial sectors.
- Construction output in June was marginally lower (**-0.3%**) than it was just before the pandemic hit the UK. The recent cooling of output growth is due to contractor/sub-contractor capacity issues as well as the well-publicised raw material supply shortages.
- The third consecutive drop in output raises some concerns that the pandemic bounce-back could potentially be scuppered by the ongoing materials shortage issues, inflationary material price rises, difficulties recruiting labour and also a shortage of HGV drivers to supply sites.
- Activity on site has also been impacted by the so-called 'pingdemic' in recent months. Forcing employees that come into contact with COVID-19 throughout the supply chain to isolate is having an impact on both capacity, productivity and ultimately output.
- Construction PMI data from IHS Markit/CIPS suggests that official output figures will come off the boil in the coming months, unable to maintain growth at the 24-year high reported by purchasing managers in June.

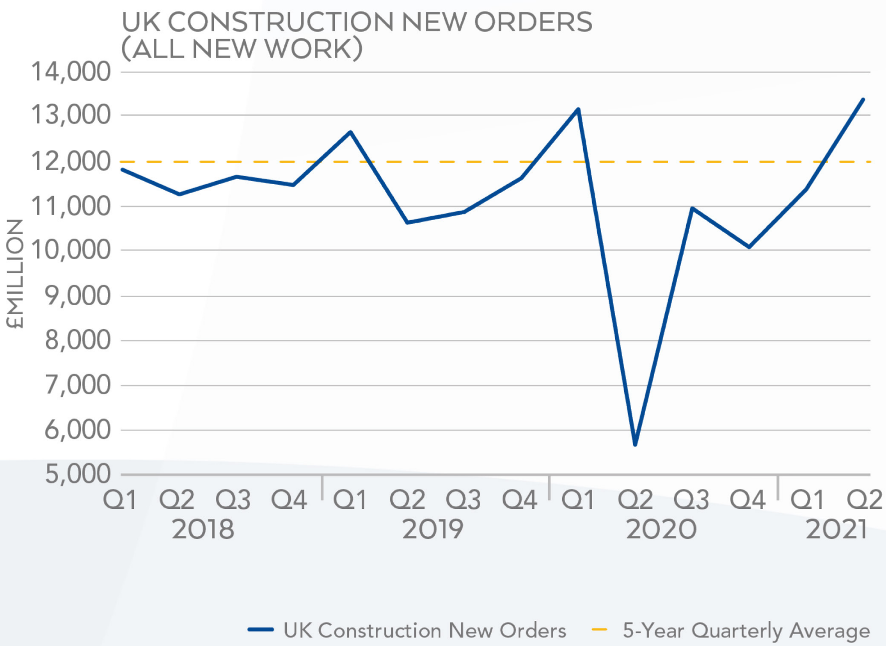
Source: *ONS*

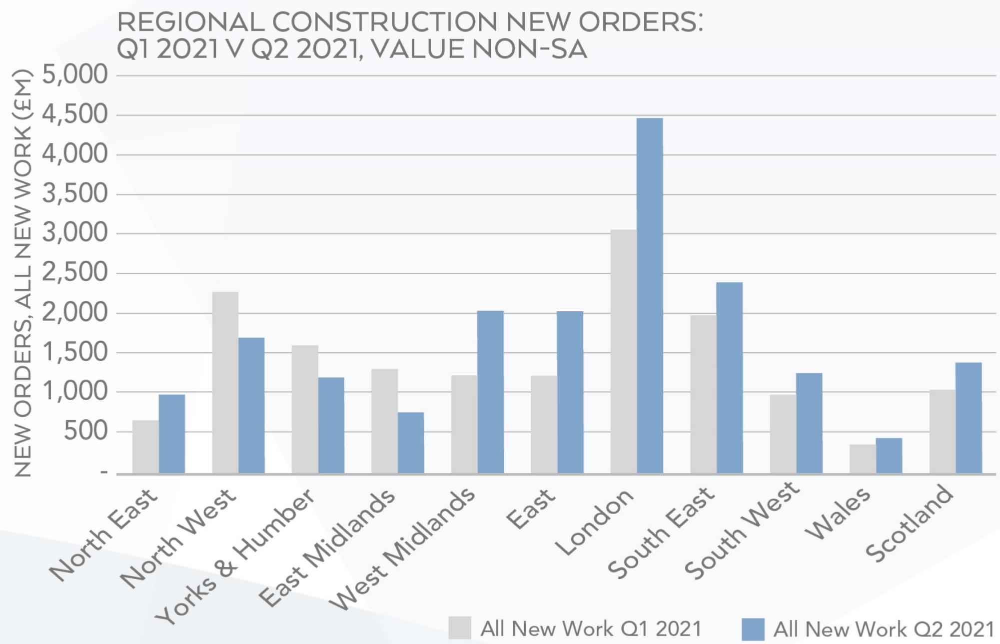


- In contrast to the monthly fall, the quarterly UK construction output series painted a more positive picture, which grow by **3.3%** (Q-on-Q) in Q2 2021.
- Both 'new work' and 'repair & maintenance' output rose in Q2, increasing by **3.9%** and **2.3%** respectively. Output from new Infrastructure (**+15.9%**) and Public Housing (**+10.6%**) grew the most over the quarter but other sectors, namely Private Industrial (**+3.8%**) and Private Commercial (**+0.8%**) new work, made positive contributions.
- On an annual basis, construction output grew by **3.4%** in June 2021 - the strongest annual rate of output growth since August 2019.
- While encouraging to see output growth in Q2, the rate of growth was some way below the economy overall at **4.8%**. However, with the first quarter of 2021 spent under lockdown it's unsurprising that construction was outperformed by the services sector in Q2.
- Slowing momentum and weakening sentiment about future output growth points to a potential drop in output values in Q3, but certain sectors (eg housebuilding and public infrastructure) will likely see strong growth trends.
- Despite the recent marginal monthly falls in output, the CPA say that output is still buoyant and predict a **13.7%** overall rise in output in 2021.

Source: *ONS*

REGIONAL CONSTRUCTION NEW ORDERS





- Following two consecutive quarters of decline, total construction new orders grew by **17.6%** (or £1,998m) in Q2 2021 compared with the first quarter.
- New orders rose above their pre-pandemic level for the first time in Q2 2021 – **1.6%** higher than they were in Q1 2020 and also **11.6%** higher than the five-year quarterly new order average.
- New orders were strong across the board in Q2, confirming the sustainability of the post-pandemic bounce back. However, Infrastructure and (perhaps somewhat surprisingly) the Commercial sector were the biggest drivers of new order growth, rising by more than **24%** and **48%** respectively quarter-on-quarter.
- On a regional level, eight of the 11 regions saw positive quarterly new order growth in Q2. Of those eight regions the average Q-on-Q growth was just over **42%** – a substantial jump that, once again, appears to have been largely driven by strong Infrastructure, housebuilding and Private Industrial new orders.
- In the three regions where new orders declined in Q2 (North West, Yorks & Humber and East Midlands), new order values in the previous quarter were particularly high by historical standards. Q2 new orders in each of these regions were still around their long-term quarterly average.
- Q2 new order data indicates that client confidence is returning and a good pipeline of work is starting to be built. They also suggest that construction activity will be reasonably well spread across the UK.

Source: *ONS*

- London private residential new orders rose by **112%** in Q2 2021 to **£1.66bn** – well above of the five-year quarterly average of **£1.09bn**.
- While private housing new orders in London rose in Q2, new order values in London's public housing sector fell by **45%** to **£177m**
- The number of new residential construction starts in London (on sites with more than 20 homes) remains low. There were **15,891** new starts in the year to Q2 2021 – **16%** fewer than in the same quarter last year.
- With completions outpacing new starts, the number of homes under construction in London shrunk to its lowest in six years (**55,326** homes).
- Demand for prime residential has been sluggish but the mainstream market has fared better, helped by the Build to Rent sector. As international travel restrictions ease, demand for prime London residential is likely to rise.
- The London residential pipeline promising. There was a **17%** rise in the number of permissions granted in the year to Q2 2021, but new planning applications submitted continue to fall (**-10%** annually).
- According to Savills, although London's private residential supply is forecast to increase over the next 18 months, subdued permissions and applications in previous years will likely mean that future housing delivery in London will remain short of targets.
- Public/ affordable housing new orders are expected to rise in the coming years as councils build significant development pipelines. However, due to excess demand large shortfalls are still expected over the next five years.

Source: *ONS, Molior, Savills*

- London Commercial new orders rose by **64%** in Q2 2021, from **£1.45bn** to **£2.36bn** – the highest quarterly value since Q2 2007.

- There is a strong central London office pipeline for 2021 but it has been boosted by a significant number of delayed schemes that shifted many completions from 2020 to 2021.

- Q2 new order figures point to growing confidence of developers and clients who had previously delayed speculative commercial office developments, waiting for further clarity on future working practices before deciding on long-term strategies.

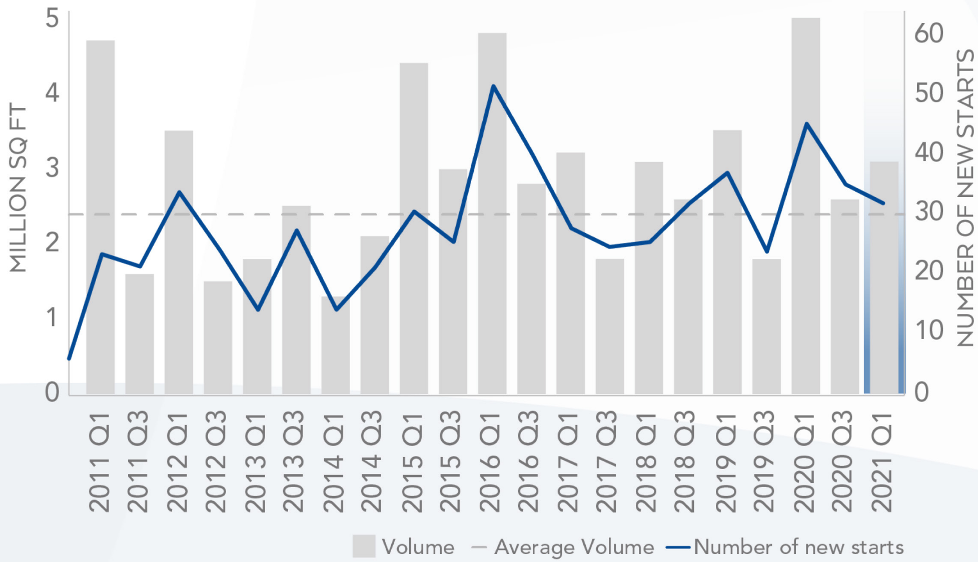
- Similarly, some retail, leisure and hospitality clients waited for the services sector to pickup before mobilising postponed schemes. Signs of a recovery in the services sector prompted a flurry of repurposing and refurbishment projects in preparation for the reopening of the economy in Q2.

- Grade A commercial office space remains the preference for occupiers. Savills reported that in H1 2021 **89%** of take up in the City was for such space and the 'flight for quality' shows no signs of slowing. Demand for high quality office space with strong ESG, sustainability and health and wellbeing features across central London is likely to continue to increase.

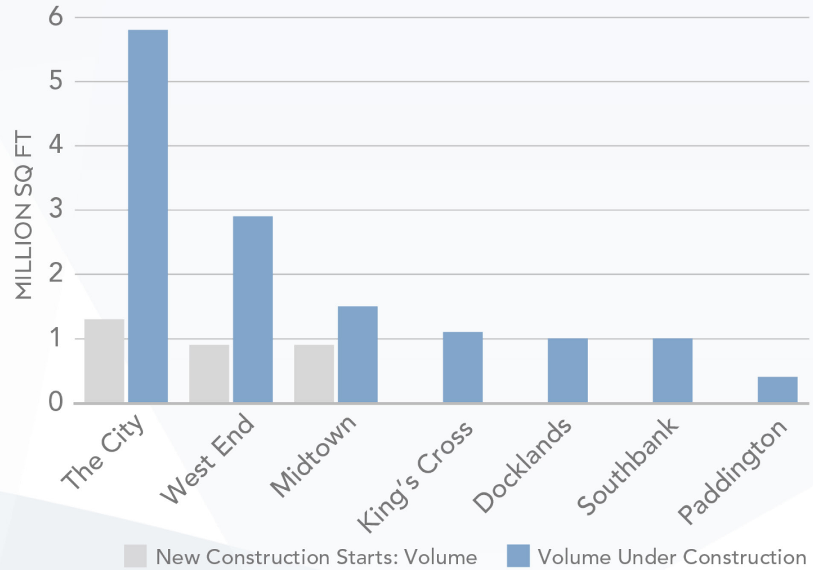
- Although relatively little new commercial office construction is expected to start over the next six to nine months, the current hive of activity in the commercial fit out sector could continue to support new orders in H2 2021 as occupiers reconfigure/ redesign their space.

Source: *ONS, Molior, Savills*

CENTRAL LONDON:
VOLUME AND NUMBER OF NEW STARTS PER SURVEY



NEW CONSTRUCTION STARTS V VOLUME UNDER CONSTRUCTION (LONDON) OCT 2020 - MAR 2021

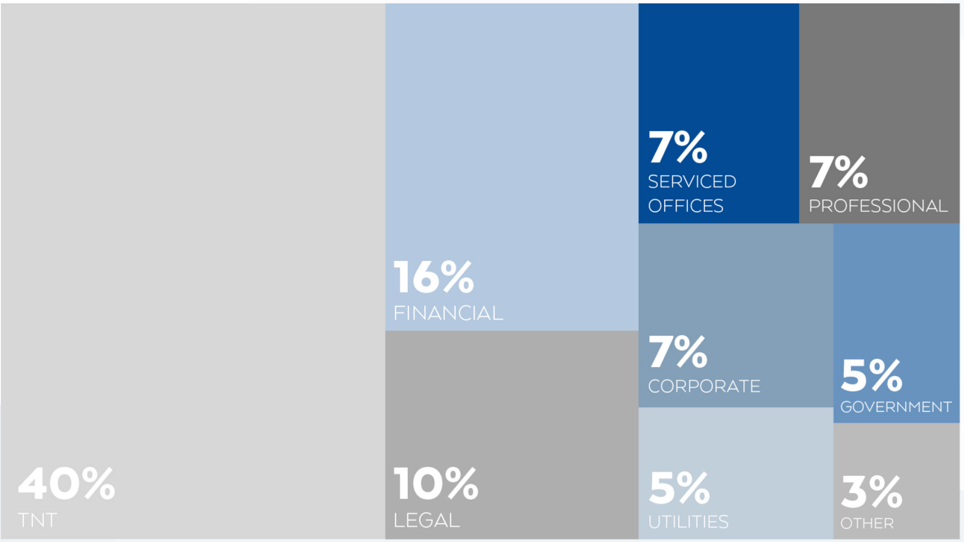


- **20%** increase in the volume of new construction starts (both new build and refurbishments) compared to the six months to March 2021.
- 3.1m sq ft of new London office projects started in the six months to March 2021 across central London.
- 32 separate new schemes commenced during the survey period – a higher figure than the long-term average of 25.
- The level of pre-letting in new construction starts dropped from **45%** to just **19%,** suggesting a higher proportion of speculative office developments.
- **56%** of new construction starts involved an extensive upgrade to existing office stock in as many as 21 schemes.

- In the six months to March 2021, new starts were concentrated in London's core City, West End and Midtown markets, with the West End and Midtown combining to account for 57% of all new office construction in central London.
- There were no new starts reported in Southbank, Docklands, Paddington or King's Cross.
- New office starts in the West End almost doubled from the previous survey, with 0.9m sq ft breaking ground across 14 new developments. The City saw the highest volume of new starts but only two schemes were new-build developments.

Source: *Deloitte Real Estate*

PERCENTAGE OF PRE-COMPLETION SPACE LET BY SECTOR



Homeworking expected to **reduce office demand** (sector-dependent)

Occupiers becoming more discerning about **net zero offices**

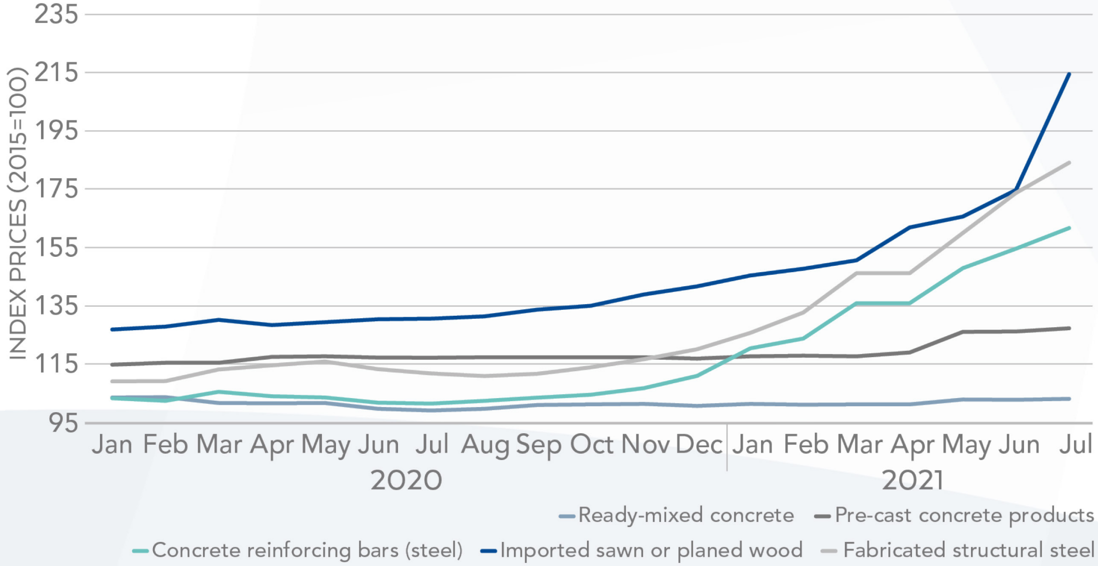
Majority of developers looking to **increase their pipelines**

Stronger focus on **'best-in-class'** office space

- Pre-letting activity weakened. **59%** of completions were pre-let, down from **70%** in the previous survey and below the five-year average of **65%**.
- In terms of office space under construction in central London, less than a third (**32%**) is committed to compared to **45%** in the previous survey.
- TMT sector continues to drive office demand taking up **40%** of all pre-let space under construction. The sector is not intending to scale back on space to the same degree as others due to its expectations of business growth.
- Financial Services accounted for a modest **16%** of the pre-let space under construction. This reflects the sector's shift towards scaling down on real estate by consolidating its office presence in central London, and with many back-office functions being moved to the regions.
- Appetite for flexible office space has diminished due to weaker tenant demand for short-term space as a result of the increase in homeworking. However, there is growing demand from tenants that are unable to agree terms to extend their lease with their current landlord and who need short-term space while they assess their accommodation needs.

Source: *Deloitte Real Estate*

KEY MATERIAL PRICES (2015=100)



CONSTRUCTION MATERIAL PRICE INDICES

	MONTH ON MONTH May 21 - June 21	YEAR ON YEAR June 20 - June 21
NEW HOUSING	5.8%	19.8%
OTHER NEW WORK	3.1%	19.6%
REPAIR & MAINTENANCE	6.7%	23.0%
ALL WORK	4.5%	20.1%

- The BEIS ‘All Work’ material price index rose by just over **20%** in the year to July 2021, hitting a record high as the sector struggles with supply ongoing chain disruptions.
- Material prices increased **4.5%** in July – the largest monthly rise on record – while the price of certain types of imported timber rose by **23%**.
- Securing imported products, especially from China such as copper and steel, remains difficult. Domestically produced products such as bagged cement are also in short supply. This is particularly affecting smaller contractors with less secure pipelines who typically don’t buy in advance.
- Material availability issues are largely COVID-related, stemming from factory slowdowns, closures constraining production and reduced freight container capacity.
- While supply side risks remain, some key commodity prices have stabilised or even fallen in recent months. According to the LME, copper prices are down from their highs in early May. Iron ore prices also fell by **28%** in the month to mid-August.
- By mid-August timber futures had plummeted by more than **70%** from their record-high in May. However, price falls are not yet being passed on down the supply chain as retailers sell inventory bought at higher prices. Furthermore, with demand so strong there is little reason to immediately lower prices.
- While output and building activity has returned to near pre-pandemic levels, supply hasn’t been able to keep up with demand. The recent falls in monthly construction output are, in part, related to rising material prices.

Source: *BEIS*

Key Trade Analysis Likely 12-month inflationary range for key trade packages based on our Q3 2021 TPI Survey results

Key Trade Packages	Summary	Likely Inflation Range (Next 12 months)
Demolition	New demolition/site remediation frameworks along with rising new orders indicating a growing new build pipeline is positive news for demolition contractors. However, with many of these schemes not committed to start until the end of the year there is likely to be spare capacity in the market in the short-term, keeping demolition and enabling works relatively competitive. With high scrap metal prices, contractors can continue to offer keen pricing and the credit for scrap is often being passed through in bids. Looking further ahead, the low carbon agenda is likely to change the profile of work being commissioned with a greater proportion of conversion and refurbishment relative to new-build. This will necessitate greater capture of second-hand materials for recycling/ repurposing, impacting demolition processes and pricing.	**-1% to 1%**
Groundworks	Cement and ready-mixed concrete prices have remained relatively flat, increasing by around 3-4% each in the year to July 2021. However, rebar prices continue to rise and are up by more than 59% over the same period, prompting groundworks and frame contractors to state that rebar is at an unsustainable level. Contractors continue to actively seek work but expect that planned infrastructure and enabling civils works will bolster their pipelines over the next 12 months.	**0% to 1.5%**
Concrete	Although ready-mixed concrete has seen more subdued price inflation than other materials, shortages of cement are causing delays and increasing project costs. The CLC say that demand for bagged cement is unprecedented and both bagged and bulk cement are on allocation. However, they note there regional variations with some areas more affected than others. All UK kilns are operating but it may be some time before stocks return to normal. With high demand supported by major infrastructure schemes getting underway, extended delivery times are expected to remain until the end of the year.	**1% to 2%**
Steel	According to BEIS data, fabricated structural steel prices were up by nearly 65% in the year to July 2021. Within infrastructure and commercial construction, steel continues to experience significant supply disruption and price inflation. However, iron ore prices have fallen sharply since mid-July after China announced it would reign in steel production. Ramped up commitments by China to reduce emissions by cutting steel output triggered a selloff in iron ore, but the 28% fall in the price of the steel-making ingredient in the last month has not yet passed through the supply chain and is unlikely to do so when demand remains so high.	**3% to 5%**
Facades	Supply pressure and increased cost of design, installation and materials creating uncertainty in the supply chain with bids being caveated. Some materials have increased significantly with aluminium prices hitting a record high in August. Brexit/tariffs not expected to be a major issue as glass, aluminium and fabrication generally comes from the EU and countries where trade deals are in place. Façade sub-contractor workloads are steady with 2021 pipeline largely secure. Lead times have lengthened due to reduced capacity of manufacturing facilities and suppliers increasing procurement periods. Contractors are still tendering competitively with low conversion rates and pricing is fairly tight.	**2% to 4%**

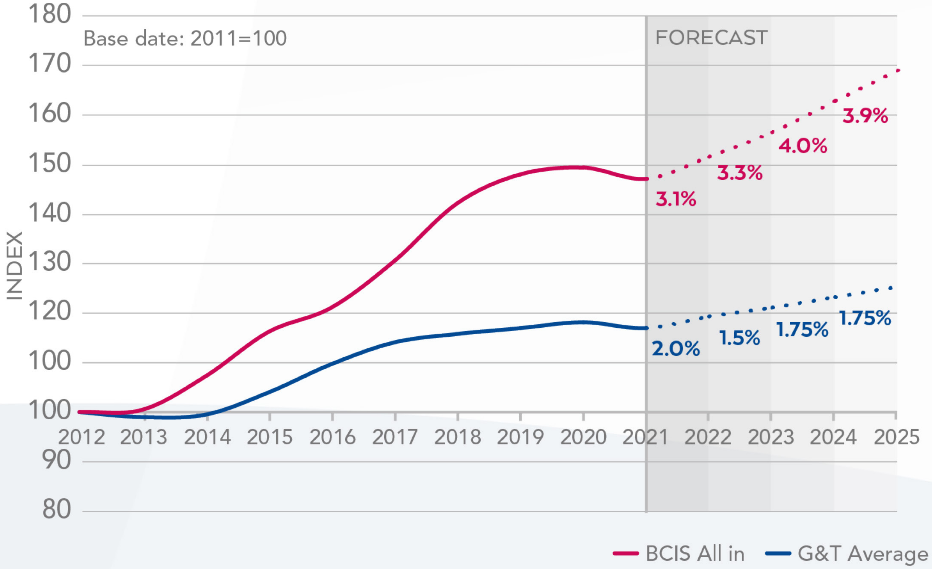
Key Trade Analysis Likely 12-month inflationary range for key trade packages based on our Q3 2021 TPI Survey results

Key Trade Packages	Summary	Likely Inflation Range (Next 12 months)
Brick	Brick production and deliveries (both lead indicators of residential construction volumes) continued to edge higher in Q2 2021 as stocks fell. Demand has recovered strongly (fuelled by a housebuilding boom and repair & maintenance improvements) and manufacturers are now back at full production capacity. However, manufacturers are wary that present shortages of labour, raw materials and transport across the wider construction sector could impact demand for bricks. According to a recent RICS survey, inflationary pressures are stemming from a scarcity of bricklayers which is putting upward pressure on rates.	1% to 2%
Dry lining	Shortages of skilled labour are supporting prices, particularly in residential. Costs are being pushed up by supplier stock shortages of plasterboard, plywood and insulation materials. Contractors are factoring in average inflationary rises of 10% per year (to 2023) from British Gypsum for plasterboard. High steel prices are a concern for metal studs and lay in grids and this is influencing supply and cost. Drylining lead times remain at 13 weeks but no further rise is anticipated.	1.5% to 2.5%
Carpentry	Demand for carpentry from the residential sector continues to stretch capacity and put pressure on labour supply. According to BEIS data, imported sawn or planed wood prices rose by more than 64% in the year to July 2021. Price rises are being driven by shortages – a result of Covid-19 restrictions limiting timber mill production, Brexit red tape complicating imports, compounded by a global increase in demand for timber construction products. Even though sawmill supply is being ramped up following the maintenance season in July, supply is expected to remain tight into Q3 2021 and unrelenting demand for imported timber means an immediate retail price correction is unlikely. Contractors expect carpentry lead times to increase further until there is a return to a more recognisable balance between supply and demand.	1.5% to 2.5%
Joinery	Workload and enquiries remain strong which is putting strain on labour availability. Strong demand from the residential sector, global supply shortages and rising raw material prices are putting upward price pressure on the trade.	1.5% to 2.5%
Finishes	Finishing trades are being impacted by increasing costs for finishing materials such as paints, varnishes and tiles. Fit-out firms are reporting rising enquiries as well as growing order books as tenants and landlords revamp their existing workspaces.	1% to 2%
M&E	Bidding competition has eased from 2020 but remains higher than it was pre-pandemic. An increasing number of lower tier subcontractors are bidding for larger open tenders which is keeping pricing keen. In addition to commodity-based material price volatility, contractors continue to report supply issues. Projects are being affected by microprocessor shortages, increased delivery costs and extending delivery periods. Demand is outstripping supply, increasing costs across ventilation packages, cablings, pipework and containment in particular. Even larger firms, that had extra stock, are now depleted and this is impacting programmes and costs on projects.	1.5% to 2.5%

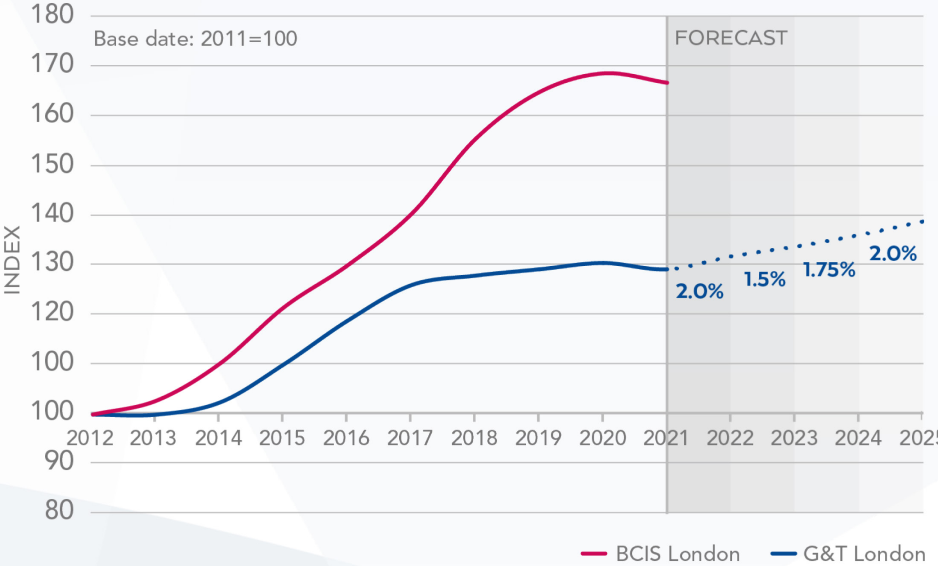
Key Trade Analysis Likely 12-month inflationary range for key trade packages based on our Q3 2021 TPI Survey results

Key Trade Packages	Summary	Likely Inflation Range (Next 12 months)
Roof	The National Federation of Roofing Contractors (**NFRC**) reports that workloads are rising and shortages intensifying. Most common shortage areas are concrete/ clay tiles, timber battens, insulation and general timber, pushing prices higher. Labour availability continues to worsen, pushing up wage rates. Contractors anticipate further, broad-based growth over the next 12 months. However, the availability and cost of skilled labour and materials will be potential brakes on the pace of the recovery.	**1% to 2%**
Preliminaries	After rising from 13.5% in 2019 to 15.3% in 2020, average Main Contractor preliminaries costs the first six months of 2021 have fallen to 12.3%. Contractors have evidently tried to be competitive with their elements of works so far this year as they filled their order books, particularly in light of the rapid rise of material costs. The CLC SOP's are no longer current but some of the additional site welfare facilities may remain in place for the short-term and so have little immediate impact on preliminaries costs. Skills shortages are pushing up staff and operative rates which will be a key contributing factor rising preliminaries costs over the next 12 months.	**Neutral - Increasing**
OH&P	Average overheads and profits (OH&P) have retreated from 6% in 2020 to 5.6% for first six months of 2021. Contractors have been sensible with their margins this year but with rising new orders, margins are likely to recover as tendering competition eases. Contractors bidding in thriving sectors will have greater headroom to raise OH&P.	**Neutral - Increasing**

TENDER PRICE TREND 'ALL UK TPI'



TENDER PRICE TREND 'LONDON TPI'



- Burst of pent-up demand and economic activity amid intense supply constraints causing transitory inflation.
- Price pressures expected to normalize as supply and demand meet in one place.
- Nearly all material prices moving upwards, putting pressure on contractors to pass these rises on through increased tender pricing.
- Expected wage-led inflationary growth as demand for skilled workers begins to outpace supply.
- Against this backdrop, our inflationary forecasts have been upwardly revised across all regions in 2021. Our resultant weighted UK average indicates that tender price inflation will rise by an average of **2%** this year – significantly higher than our previous forecast of **0.5%** in Q2 2021.
- If cost plans were being re-rated and materials procured now, tender price inflation would inevitably be much higher than **2%** but it's important to reiterate that we are forecasting across the whole year, providing an average inflationary rate across all sectors of the built environment. TPI is likely to vary from project-to-project more than ever.
- Signs that material-led input cost inflation has begun to give back some of its advances since the late spring. Commodity prices such as iron ore, copper and timber have all come off the boil, casting doubt on any inflation-related panic.
- Production output is recalibrating which should ease most supply-side issues, and once pent-up demand has passed through and begins to normalise, we anticipate that much of the inflationary pressures acting on material prices will ease.

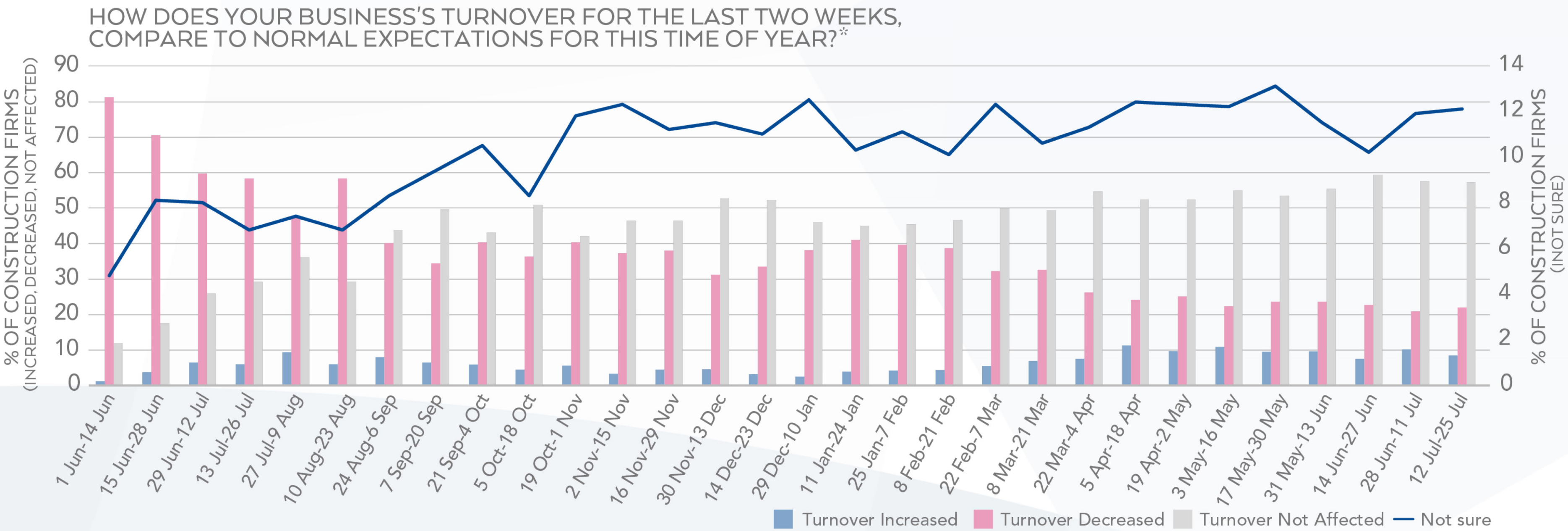
Note: BCIS does not publish regional TPI forecasts

- Key inflationary metrics such as the ONS's construction output prices index (**COPI**), CPI and RPI rose gradually in 2020 but growth rates have accelerated since January 2021.
- In the first seven months of 2021, CPI increased by **2.1%** and RPI by **3.7%**. The 'All Construction' COPI lagged both series, growing by just under **2%** but over a slightly shorter period (Jan – Jun 2021).
- The BCIS's general building cost index (which measures movement in the cost of labour, material and plant to a contractor) rose by **5.5%** in the first half of 2021, outpacing all other inflationary measures in the graph above.
- From mid-2021 onwards, there was a clear divergence between the BCIS All-in tender price index for the UK and all other inflationary metrics.

Typically, differences between tender pricing and input costs (as indicated by the COPI and BCIS general building cost index, above) are indicative of market conditions.

- While input costs were rising in H2 2020, tender price inflation was generally falling. This suggests that contractors were initially trying to absorb input cost rises, being competitive with their tender submissions while new order growth was still subdued.
- As input cost inflation accelerated further in H1 2021, contractors became less able to absorb the price rises. Recovering new orders also meant that contractors had greater capacity to pass inflationary rises on.

***Please note:** COPI is the ONS's best estimate of inflation within the UK construction industry. The index is compiled using existing ONS data sources on a project cost basis. Three types of input cost are estimated: materials, plant and labour. A mark-up is then applied, which accounts for profit. See ONS' methodology background for further information.*



- According to the ONS' fortnightly Business Insights and Impact on the UK Economy dataset, the proportion of construction firms reporting that their turnover was lower compared to what was normally expected for the time of year hit a low point in the 28th June – 11th July period.

- Although a significant proportion of firms (**20.8%**) reported lower than normal turnover for the period, this metric has seen a general downward trend since summer 2020. Furthermore, the majority of firms (more than **57%**) reported that turnover was unaffected while a small proportion (**10.1%**) believe that turnover has actually increased in the period compared to normal expectations.

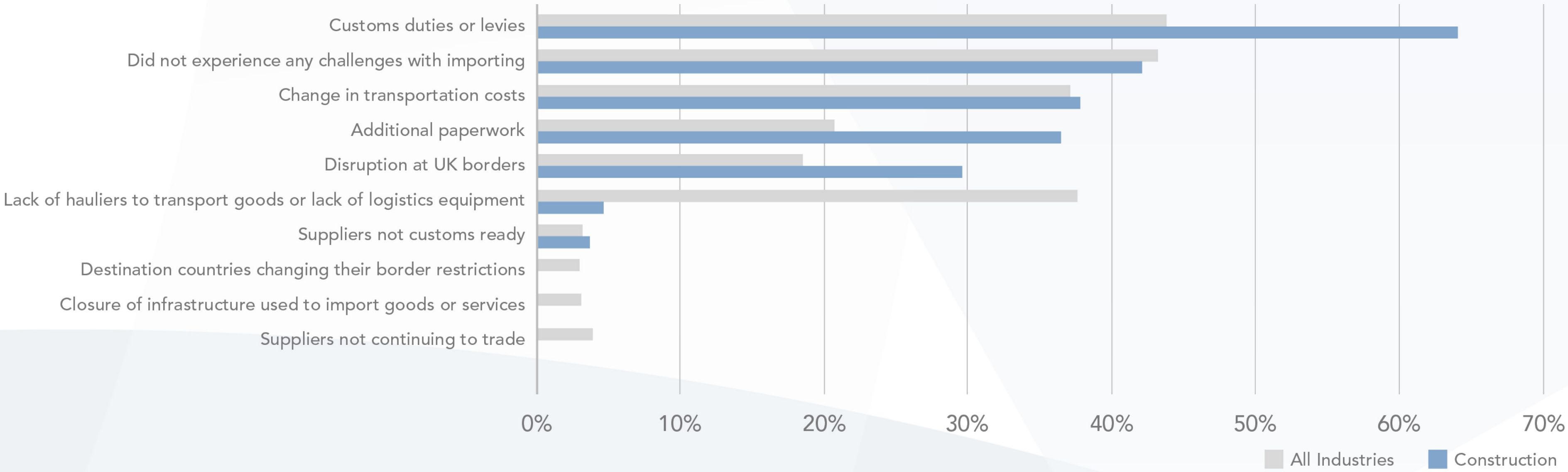
- A number of contractors have collapsed into administration as a result of falling margins on current jobs. According to Creditsafe, a total of thirteen companies in the construction sector went into administration in July 2021 – a rise from the seven that went under in June but lower than May's 15.

- Most companies have blamed this on a combination of the pandemic and Brexit, which have caused volatility in availability and prices of construction materials. This has made the completion of existing and future contracts both unprofitable and unviable. Delays to the completion of projects on site has also added complications.

** Percentage of construction businesses currently trading, broken down by industry and size band, weighted by turnover, UK, 1 June 2020 to 25 July 2021*

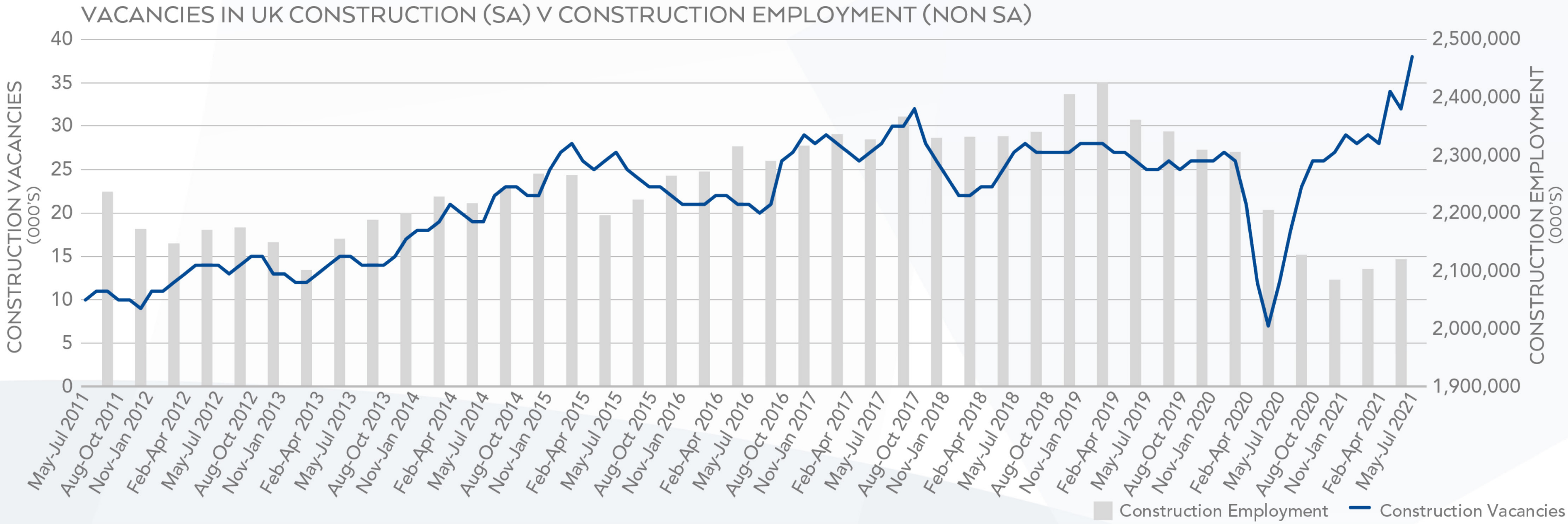
Source: ONS

HAVE YOU EXPERIENCED ANY OF THE FOLLOWING CHALLENGES WITH IMPORTING OVER THE LAST TWO WEEKS? (12^{TH} JUL- 25^{TH} JUL 2021)



- Between 12^{th} – 25^{th} July, surveyed construction companies said that the most common challenge with importing over the period was a ‘change in transportation costs’. Over **64%** of firms said that they experienced rising costs as contractors were hit by ripples of shipping ‘super inflation’ and a lack of transport availability.
- Following Brexit, ‘Additional paperwork’ (**42%**) and ‘Customs duties and levies’ (**38%**) have become increasingly burdensome to construction firms. A ‘Lack of hauliers to transport goods or a lack of logistics equipment’ was also a common challenge, affecting nearly **30%** of companies.
- Supply imbalances are being amplified by a lack of transport availability, port congestion and logistical logjams (caused by stretched international supply chains) and Brexit trade frictions. The result is historically long delivery times acting as a damper on overall construction activity and output growth.
- For contractors (particularly SMEs with less ability to hold stock and which don’t have professional procurement teams/established supply chains in place) that operate a ‘just in time’ delivery supply chain, even the slightest delay in materials or hike in transportation costs can have serious knock-on financial consequences. Companies on fixed-price agreements with clients could face difficulties if they don’t take proactive mitigating actions.

Source: *ONS*



- The latest ONS data shows construction vacancies hitting a 20-year high. Job vacancies in the three-month period between May-July 2021 were 38,000 - **19%** higher than the previous period (April-June 2021). Construction vacancies are now well above the 10-year average of 21,800.

- July's IHS Markit/CIPS UK Construction employment index signaled that the rate of job creation accelerated month-on-month and was close to its seven-year peak seen in May. Higher levels of employment were attributed to robust order books and optimism about near-term growth prospects.

- While the total number of construction employments appears to be growing in response to the sharp rise in vacancies, a substantial gap between the two data series remains.

- Employment growth is struggling to keep pace with growing workloads. This will be an obstacle for businesses looking to build out existing commitments or embark on new projects, and one that could limit activity in future months. In some sub-sectors, labour shortages have been driven by a sharp increase in infrastructure work and a surge in housebuilding and refurbishment work, drawing labour away from less active sectors.

Source: *ONS*

Market Update
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