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MARKET UPDATE

November 2021

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CONTENTS

G&T's Market Update for November 2021 provides an overview of the UK construction market. Against a backdrop of ongoing supply chain issues and rising costs, 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 pressure on rising input costs as demand recovers and workloads rise
- Compare key input cost inflationary metrics with tender price indices to reveal insights about market conditions
- Analyse various ONS datasets in order to determine the impact of the pandemic on construction labour availability and costs
- Highlight some of the key takeaways and feedback from our recent Main Contractor Survey

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.

Click **HERE** to view the TPI online

UK economy
EXPANDED
BY
1.3%
(Q3 2021)

UK economy to regain pre-COVID peak at year-end (OBR)

Bank of England anticipates CPI will hit
5%
next spring

The UK economy is recovering but the pace of that recovery lost momentum in Q3 2021. Output expanded by **1.3%**, leaving it still more than **2.1%** below its pre-crisis level in Q4 2019.

Staff shortages and supply constraints blunted the impact of the ending of remaining lockdown restrictions in July, with a poorer trade performance – influenced by more expensive imports of oil – also acting as a brake on growth.

Notably, business investment remained well down on pre-pandemic levels in Q3. Meanwhile, the trade deficit widened as goods exports to non-EU countries fell and imports – particularly of fuel – from non-EU countries increased.

Disruption to supply shows few signs of easing and supply chains will remain under pressure until mid-2022. There is likely to be an ongoing mismatch between the labour market and the supply chain that will keep headline CPI inflation above **4%** in H1 2022. This will put pressure on the ability of businesses to increase their pricing power and protect their margins, especially in an environment of significantly less state support and a start of fiscal consolidation bringing softer demand.

To tackle rising prices, the Bank of England is likely to raise interest rates. However, the global nature of these inflationary pressures means that traditional tools such as raising interest rates are likely to have little effect.

According to the Bank of England's Monetary Policy Report (November 2021):

- Spending, jobs and incomes continue to recover from the effects of COVID and the size of the UK economy is getting close to where it was before the pandemic
- Supply bottlenecks will continue to restrain growth somewhat in the near term but production difficulties businesses are facing will ease
- The BoE expects the consumer prices index (CPI) measure of inflation to rise to **5%** in the spring of next year but then fall back from mid-2022
- The high rates of inflation are expected to be temporary. Demand isn't expected to continue to rise as fast and many of the shortages that are currently making it difficult for businesses to produce their products should ease
- The BoE is in a highly data dependent position where it won't be too wedded to a pre-determined timeline of normalising policy
- Provided that incoming data, particularly on the UK labour market, is broadly in line with the central projections in November's Report, it will be necessary over coming months to increase the Bank Rate in order to return CPI inflation sustainably to the **2%** target

SUMMARY OF KEY FINDINGS: CONSTRUCTION

UK Construction activity rose to 54.6 in October, from 52.6 in the previous month. Amid reports of supply constraints and rapidly increasing purchase prices, the latest reading pointed to an acceleration in business activity growth across the sector, although it remained much softer than the 24-year high seen in June.

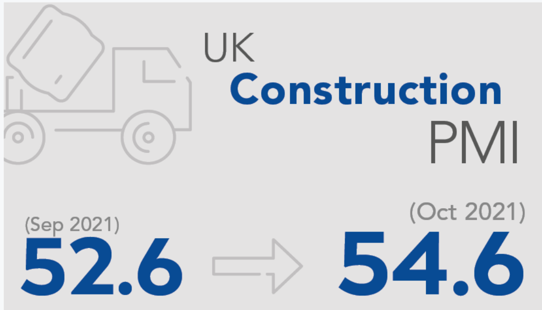
There were widespread reports that shortages of materials and staff were disrupting work on site, while rising fuel and energy prices added to pressure on costs. Nonetheless, the worst phase of the supply crunch may have passed according to data from purchasing managers.

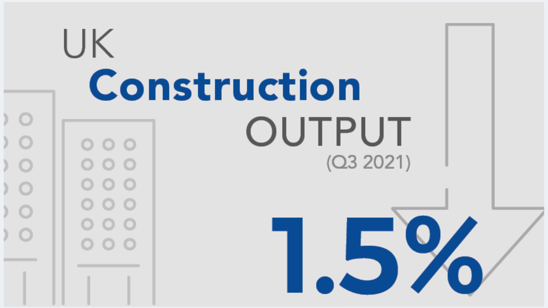
The number of construction firms citing delays fell to **54%** in October, down from **63%** in September. Furthermore, IHS Markit's input prices index showed that rate of input cost inflation receded for a third consecutive month, slipping to a six-month low.

Despite the headwinds from supply constraints and escalating costs, UK construction companies achieved a faster expansion of output volumes in October and the near term outlook construction growth remains positive.

According to the latest ONS data:

- After four consecutive quarters of growth, UK construction output fell by **1.5%** in Q3 2021
- The drop in output in Q3 was most likely due to problems in the supply chain. Shortages of materials and difficulties sourcing them were widespread. While order books were healthy, the availability of certain construction products was affecting projects currently underway
- Demand continues to be remarkably strong across the construction industry but supply chain constraints will continue to hinder output growth in the medium-term. There is also real doubt as to whether there is sufficient capacity in the supply chain to enable demand
- Following two consecutive quarters of double-digit growth, total construction new orders fell by **9.2%** (or £1.2bn) in Q3 2021 compared with the previous quarter
- An increasing number of clients pressed the pause button on their construction plans in light of soaring input costs and supply chain disruption. These issues have created business uncertainty and hindered contract negotiations
- However, COP26 has brought the carbon footprint of the built environment into sharper focus. An extensive and necessary programme of retrofitting and regeneration will help sustain new order growth in the years ahead





Material Price Index
(All Work)
23.6%
(Sep 2020 - Sep 2021)

Supply and demand are rebalancing but challenges remain

Upward pressure on materials prices to extend into 2022

Although demand for construction products has fallen from the peaks seen during spring and summer of 2021 and product supply has improved in some areas, several critical challenges remain.

Logistics has become a key issue. The shortage of HGV drivers and well-known global shipping issue continue to hamper deliveries and delay work on site. Rising energy and fuel prices have also come to the fore, impacting energy-intensive heavy-side manufacturers.

Rising energy prices will have a knock-on effect on the price of producing certain products such as steel and concrete. Wholesale energy prices are unlikely to fall in the near term so upward pressure on materials prices will extend well into 2022.

- The ONS' material price index for **'All Work'** rose by ***23.6%*** in the year to September 2021. However, the rate of inflation eased in September and prices rose by the least amount over the last twelve months
- Both fabricated structural steel and rebar prices fell in September (by **0.6%** and **2.4%** respectively) but many see softening prices as a blip rather than the start of a longer-term downward trend
- There are ongoing challenges with sourcing key materials as supply chains across the UK struggle to re-establish themselves post-Brexit and the pandemic
- There are widespread reports that shortages of materials are disrupting work on site and pushing back scheme completion dates. Due to the unpredictability of materials arriving on time, contractors are increasingly pre-purchasing materials to mitigate long wait times
- Half of the main contractors surveyed by G&T expect material prices to climb between **2.6% - 5%** over the next 12 months**,** but inflationary growth in short-term will likely be higher
- Escalating prices risk derailing the completion of current projects and could make some future projects commercially unviable
- Although still not cheap from a historical perspective, iron ore, copper and timber prices have all fallen from their recent peaks in late spring/early summer. This is a positive lead indicator for material price inflation in the medium-term, but falling commodity prices will take time to filter down the supply chain

Resurgent Consumer Spending

Consumer spending jumped **13.3%** in September compared to the same period in 2020

OECD Projects Strong Economic Growth

OECD downgraded its UK GDP growth forecast to **6.7%** (2021) and **5.2%** (2022)

PRS Demand Growing

Residential demand showing strong resilience with PMI data pointing to a solid expansion of housebuilding activity

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
(Oct 2021)

Slowdown in activity, caused by global supply chain problems and labour shortages, abated slightly in October

CPI 4.2%
(Oct 2021)

Annual inflation rose rapidly in October, driven by **shortages and higher fuel/energy costs**

0.1% Base Interest Rate

Base rate held but BoE indicated increases are on the horizon

Brexit reduces trade with EU

New costs and red tape takes **£17bn** from UK trade with EU in Q2

1.3% UK GDP

UK economy grew 1.3% in Q3 2021 – slowing from a 5.5% expansion in the previous quarter

4.3% Unemployment Rate *(Jul – Sep 2021)*

Unemployment rate on a downward trend, suggesting the labour market continues to recover

7.1% UK Construction Earnings

Average weekly earnings in construction (Y-on-Y three-month average) rose **7.1%** in Sep 2021

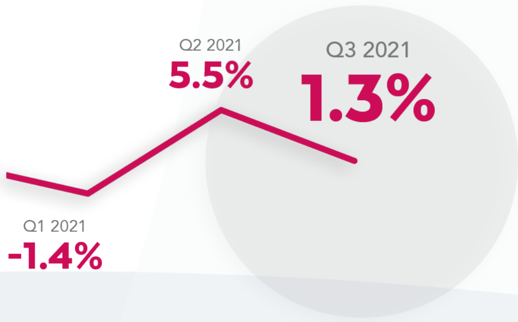
Source: Barclaycard, ONS, OECD

UK Economy

Overview	Actual	Forecast Q4/21	Q1/22	Q2/22	Q3/22	Units
GDP Growth Rate	1.3	0.9	0.7	0.4	0.8	%
Unemployment Rate	4.3	4.2	4.1	4.1	4.0	%
CPI (Annual Rate)	4.2	4.0	4.2	4.5	3.9	%
RPI (Annual Rate)	6.0	6.1	5.5	5.4	4.9	%
Interest Rate	0.1	0.1	0.25	0.5	0.75	%
GDP from Construction	31,269	31,354	32,687	32,426	32,363	GBP Million
Government Debt to GDP (the ratio between a country's government debt (cumulative amount) and its GDP)	94.9	98.4	97.9	97.9	97.9	%

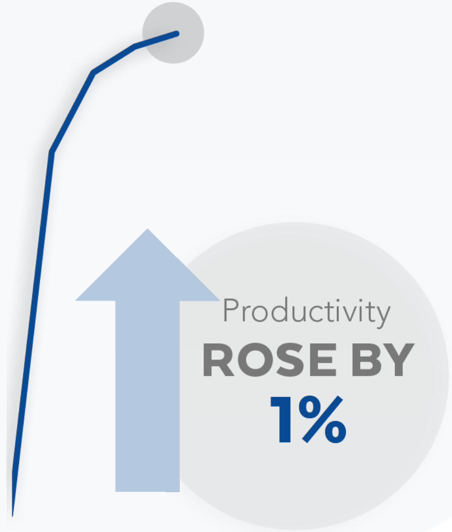
Source: *Trading Economics and ONS*

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 November 2021.*



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

UK GDP From Construction



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

The pace of UK economic growth slowed sharply in Q3 as consumer spending weakness and supply issues put the brakes on the recovery. However, the UK is getting ever closer to regaining the income lost during the crisis. GDP in September was just **0.6%** shy of its level in February 2020, before the pandemic struck.

GDP from Construction in the UK increased by **3.8%** in Q2 2021 and was **57.3%** higher than it was one year ago due to the low base effect. This is the fourth consecutive period of quarterly growth but GDP remains slightly below pre-pandemic levels.

The ONS Construction Productivity Index rose by **1%** in Q2 2021 (Q-on-Q), putting productivity on par with Q3 2019 levels. Although there is considerable variation in productivity levels between firms and across sub-industries of the construction industry, the level of productivity in construction remains below the UK average.

***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 economic rebound gathered pace with growth of **2.2%** in Q3 2021.

The bloc is on track to regain its pre-pandemic level of output later this year but there is a mixed picture of growth between countries.

Economists say the eurozone's outlook is worsening as supply chain bottlenecks and surging energy prices hold back factory production and push up inflation. Both will weigh on growth.

Driven by rising energy prices, inflation in the bloc rose to a new 13-year-high of **4.1%** in October, up from **3.4%** in the previous month.

The sharp rise in prices has put pressure on the ECB to start winding back stimulus measures, tighten monetary policy and raise interest rates.

The ECB expects eurozone GDP to expand **5%** this year, followed by **4.3%** in 2021.

US

US economic growth slowed sharply in Q3 with GDP growing at an annualised rate of **2%** - the weakest quarterly growth since the coronavirus recession last year.

Supply chain disruptions, a resurgence of COVID-19 and slower consumer spending challenged growth.

These factors fed into rising inflation with US CPI rising **6.2%** in October – the fastest annual ace since 1990. This in turn poses a risk to consumer spending and confidence by further eroding purchasing power.

Despite sluggish Q3 growth, new data shows the economy and corporate America continue to rebound from the pandemic. As such, the Fed will begin to scale back its $120bn-a-month asset purchase programme, ending stimulus altogether by H2 2022.

The IMF forecasts the US economy will grow **7%** (2021) and **5.1%** (2022).

China

The Chinese economy grew at an annual rate of **4.9%** in Q3 as momentum slowed.

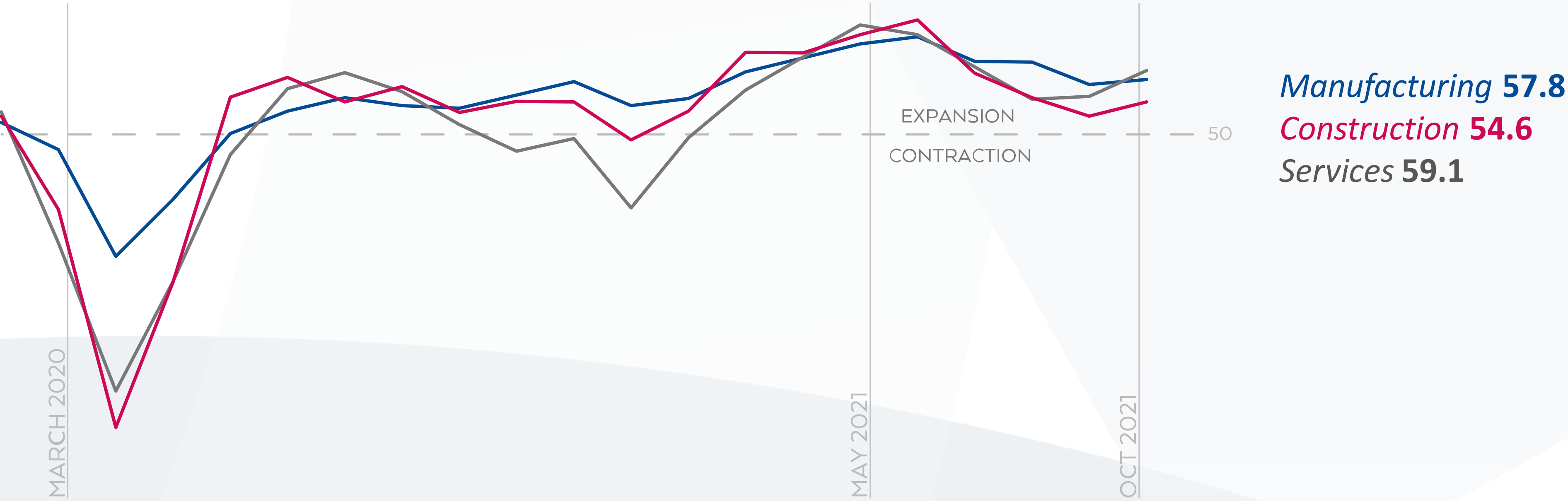
A real estate slowdown and energy shortages that sent factory output back to early 2020 levels, saw economic growth slump to its slowest pace in a year.

A drive to make structural changes that address long-term risks and distortions, which has involved crackdowns on the property sector and technology giants, as well as carbon emission cuts, has taken a toll

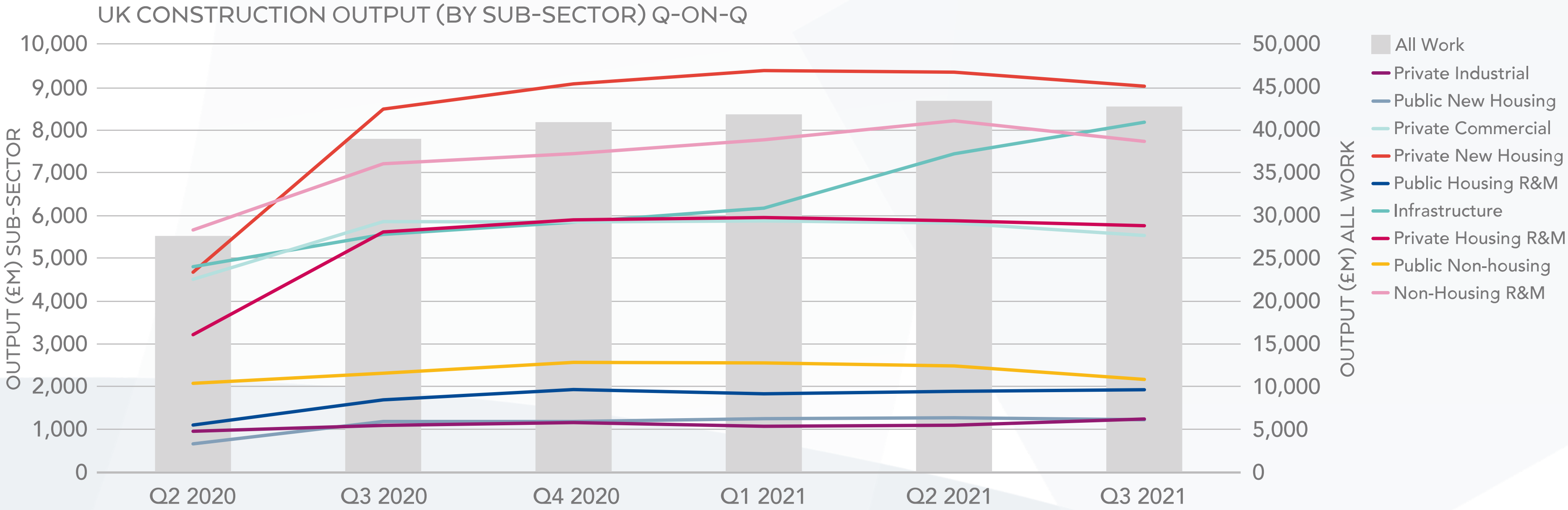
Power rationing has prompted production cuts, pushing factory gate inflation to its highest level since 1995.

Energy shortages and production cuts are expected to become less of a problem in Q4 but the real estate downturn (led by constrained mortgage lending and borrowing by property developers) could weigh substantially on growth.

** **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.*



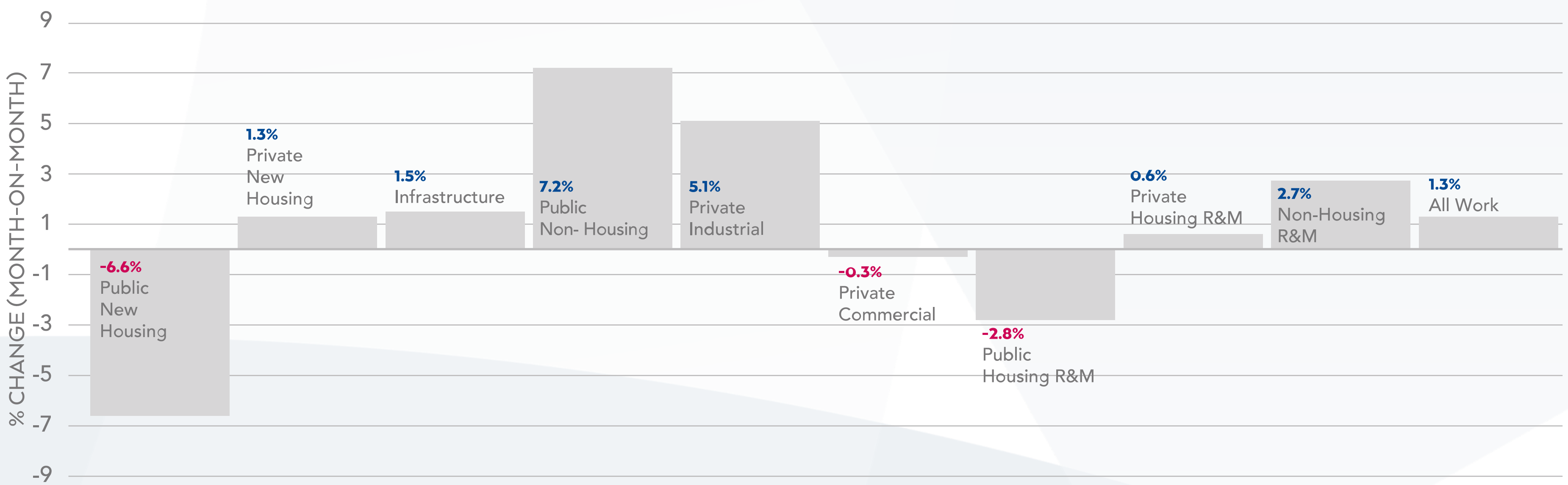
- UK Construction PMI accelerated from September's eight-month low but activity growth remains much softer than the 24-year high seen in June
- There was a robust and accelerated rise in output volumes but new order growth was unchanged from September's eight-month low and much weaker than seen on average over the summer
- Housebuilding replaced commercial as the best-performing category of construction but commercial did expand at a quicker pace than in September due to a sustained boost from looser pandemic restrictions
- Construction companies continue to report widespread supply constraints and rapidly increasing purchase prices but these trends were the least severe since April
- Demand remains strong but some construction companies suggested that supply shortages and escalating costs had hindered contract negotiations
- **54%** reported longer delivery times among suppliers and delays were overwhelmingly linked to haulage driver shortages and international shipping congestion
- Another steep rise in input costs but the rate of inflation slipped to a six-month low
- Increased purchase prices were attributed to rising energy and commodity prices as well as raw material shortages and a lack of transport availability



- After four successive quarters of growth, construction output fell by **1.5%** in Q3 compared to the previous quarter.
- Only three sectors experienced output growth in Q3: Private Industrial (+**13.6%**), Infrastructure (+**9.9%**) and Public Housing Repair and Maintenance (+**1.9%**). The rest saw quarterly contractions.
- Despite the surge in demand, New Housing output growth (both Private and Public) fell by around **3.5%** compared to the previous quarter. This meant that total housebuilding output in Q3 was nearly **9%** below the average quarterly output value from two years prior to the pandemic.
- According to the ONS, the drop in output in Q3 was most likely due to problems in the supply chain. Shortages of materials and difficulties sourcing them were widespread. While order books were healthy, the availability of certain construction products was affecting projects currently underway.
- Evidence from November's ONS Business Insights and Conditions Survey suggested that one in 10 construction companies was unable to source materials, goods or services needed from within the UK in the last month, while one in four had to change suppliers or find alternative solutions.
- Despite the fall in output in Q3, the CPA upwardly revised its construction output growth forecast for 2021 from **13.7%** to **14.3%** in its latest forecast. It also revised down growth for 2022 from **6.3%** to **4.8%**.
- The CPA's Autumn 2021 Forecasts said that although demand continues to be remarkably strong across the construction industry, supply chain constraints are hindering growth and will continue to do so in the medium-term. There is real doubt as to whether there is sufficient capacity in the whole construction supply chain to enable demand.

Source: *ONS*

ONS UK CONSTRUCTION OUTPUT (SEP 2021 V AUG 2021)



- In contrast to the quarterly fall in Q3, construction output ('All Work') rose by **1.3%** in September compared to the previous month.
- This is the first monthly increase since June 2021 and the largest since March 2021, when output increased by **4.8%**.
- Public new housing and public housing repair & maintenance offset some of the monthly growth, seeing a monthly fall in September of **6.5%** (£27m) and **2.7%** (£17m), respectively. Anecdotal evidence gathered over the month suggests that the slowdown in public new housing was coming from the sharp increase in prices, the ONS said.
- Conversely, public non housing (+**7.2%**) and the private industrial sector (+**5.1%**) saw the largest monthly increases in output growth.
- The level of construction output in September 2021 was **1.0%** (£141m) below the level of February 2020, before the coronavirus pandemic, new work was **3.5%** (£334m) below the February 2020 level, while repair & maintenance work was **3.9%** (£194m) above the February 2020 level.
- Following a concerning trend of declining output in recent months, the growth recorded in September is an encouraging sign. Surveys such as the PMI point to returning client confidence and strong demand which is expected to lead to more green lit projects in the coming months.
- Supply chain issues and price rises for raw materials will not be an insurmountable challenge but they, along with an unprecedented number of additional constraints, will likely stifle output growth in Q4 and beyond.

Source: ONS

CONSTRUCTION OUTPUT (ALL WORK) BY REGION

- Construction output ('All Work') across all regions in Q3 2021 grew by an average of **17%** compared to the same quarter one year earlier.

- The region with the highest year-on-year growth rate was the West Midlands, where output increased by **37.6%.** The North West, where output declined by **8.9%**, was the worst performing region.

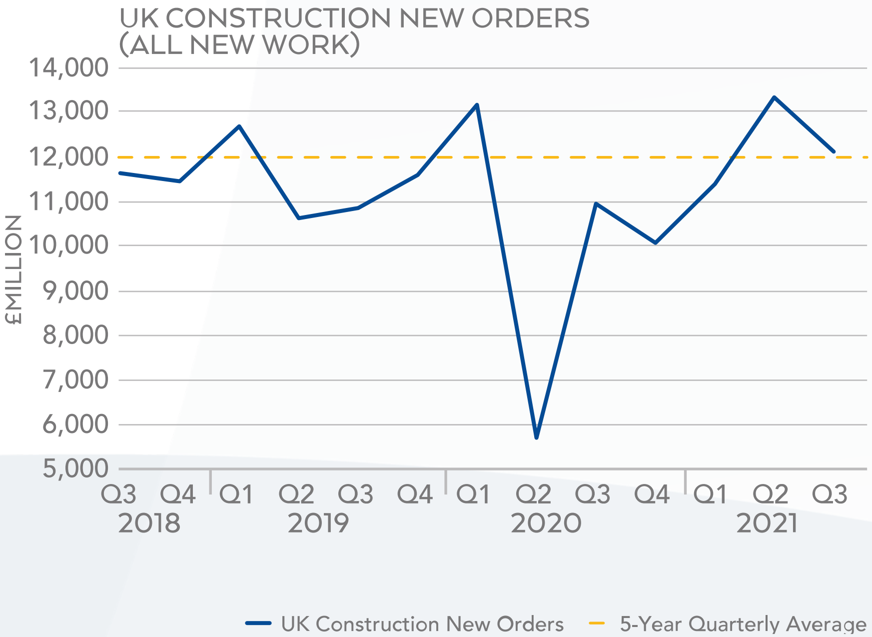
- For all regions apart from one, Q3 2021 was the best performing quarter over the past year in terms of output growth. The general trend since Q3 2020 across most regions has been quarter-on-quarter growth in output.

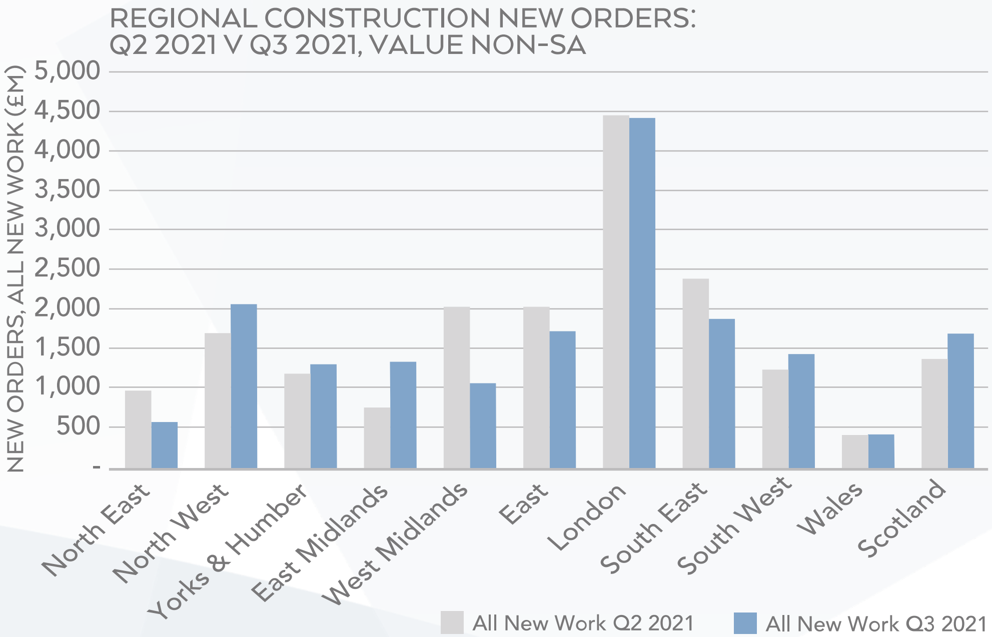
- Most regions saw strong year-on-year output growth in both the infrastructure and private industrial sectors. In six of the 11 regions, the infrastructure sector was the best performing, while in the remaining five regions the private industrial sector saw the most annual output growth.

- In London, total construction output was up by around **15%** in Q3 2021 compared to the same quarter one year earlier. In fact, the 'All Work' output value in London hit an all-time high in Q3 as a number of delayed schemes started on site.

- London has now experienced six quarters of infrastructure output growth, culminating in a record quarterly value of £1.7bn in Q3. Although not setting any all-time records, the private industrial sector saw the most output growth in Q3 compared to a year earlier. Private industrial output rose by more than **87%** to due to growing demand for urban, last-mile logistics and warehousing space.

Source: *ONS*

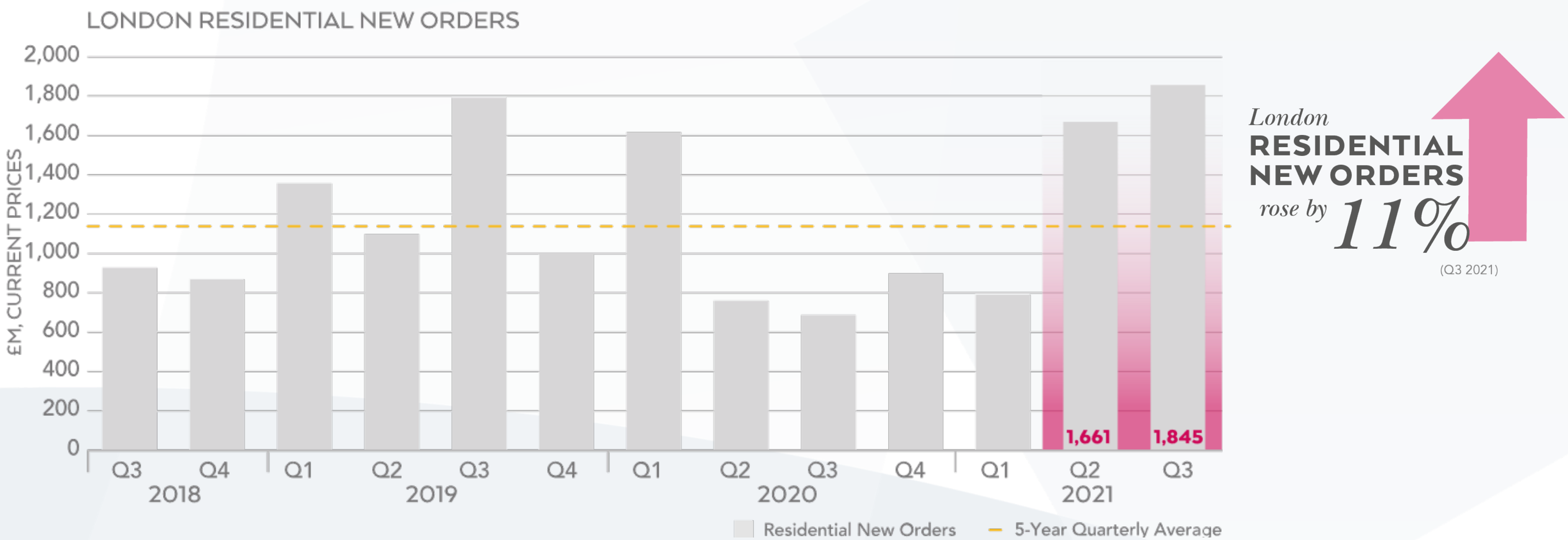




- Following two consecutive quarters of double-digit growth, total construction new orders fell by **9.2%** (or £1.2bn) in Q3 2021 compared with the previous quarter.
- Despite the quarterly fall, new orders were still **1.9%** above the five-year quarterly average and **10.7%** higher than they were in the same quarter in 2020.
- The commercial and infrastructure sectors performed particularly badly, with new order values falling by more than **21%** and **25%** respectively compared to the previous quarter (Q2 2021). However, falls in both sectors come after a particularly strong Q2.
- On a regional level, six of the 11 regions saw positive quarterly new order growth in Q3 while in the remaining five regions growth contracted.

- Due to the volatility of the new order data series, it's important to view Q3 new order values in context. In Q3, new order values in eight of the eleven regions were still above their respective five-year quarterly averages. Only the North East, West Midlands and Wales had Q3 new order values below their five-year average.
- Although the latest new order data is far from a washout, an increasing number of clients pressed the pause button on their construction plans in light of soaring input costs and supply chain disruption. These issues have created business uncertainty and hindered contract negotiations.
- The growth market was expected to slow after the initial dramatic recovery from the pandemic but order books are still healthy. Whether falling new orders become a sustained trend depends, in part, on when the current issues with material and labour shortages subside. However, there are some early signs input price inflation is moderating.

Source: ONS

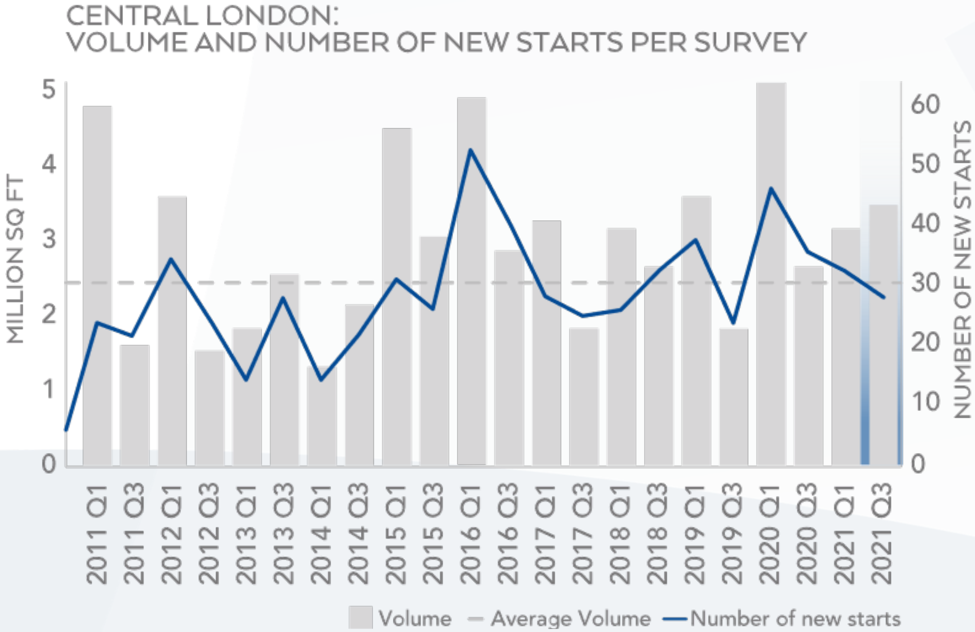


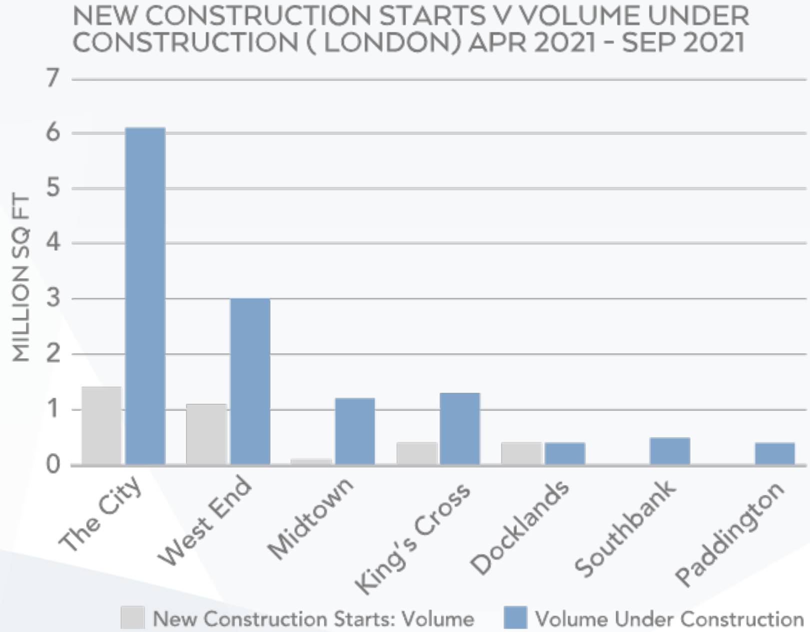
- London private residential new orders rose by **11%** in Q3 2021 to **£1.85bn** – well above of the five-year quarterly average of **£1.13bn**.
- While private housing new orders in London rose in Q3, new order values in London's public housing sector fell by **3%** to **£172m**.
- The number of new 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 looks 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 fell by **29%** in Q3 2021 – from **£2.38bn** to **£1.69bn** – but were still well above the five-year quarterly average.
- After an accelerated rise in Q2 (boosted by delayed schemes), commercial new orders fell in Q3 amid greater supply chain uncertainty and reduced willingness to commit to new commercial development projects.
- Robust demand for commercial office fit-out/refurbishment projects, as well as the repurposing of redundant commercial premises, helped keep commercial new order values relatively strong in Q3.
- The pandemic has brought about a structural change to working patterns with many companies shifting to remote/hybrid working policies. In the short term, this may mean below average volumes of new office space being built, but the office sector will see a rise in refurbishment projects as tenants and landlords adapt their premises to accommodate new working practices.
- According to Glenigan, the value of office project-starts in London fell sharply in 2020 but has recovered swiftly in 2021 and project starts are expected to increase **21%** this year.
- There is also a strong office development pipeline in London. The value of underlying office project-approvals in London climbed **58%** in 2020 following growth of **46%** in 2019 and **47%** in 2018. However, a number of these pipeline projects are expected to be delayed due to structural changes in occupiers' accommodation requirements.
- 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.

Source: *ONS, Molior, Savills*





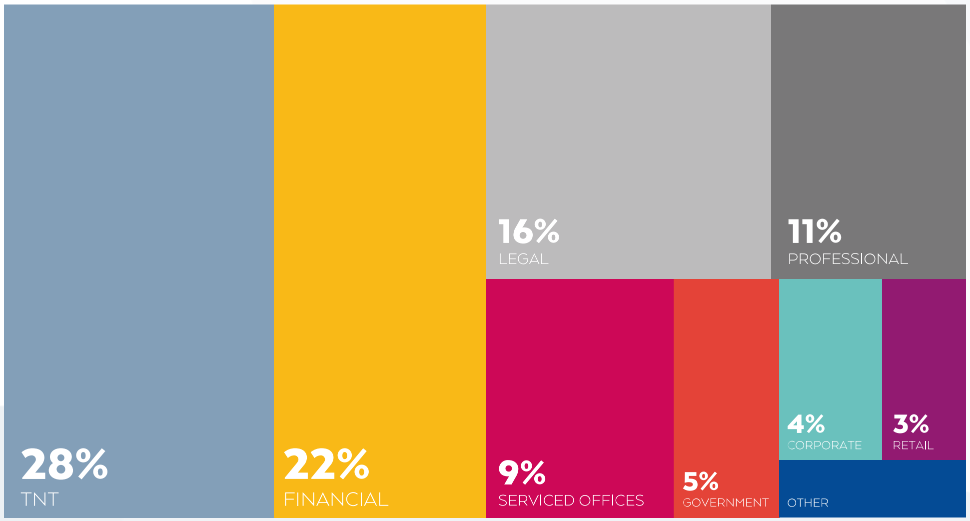
- The volume of new starts increased by **10%** (from 3.1m to 3.4m sq ft) between April and September 2021, above the long-term average of 2.4m sq ft.
- The total number of new construction starts fell by four to 27, below the long-term average of 30. This means that the average scheme size increased by **28%** to 122,339 sq ft.
- Comparing the type of new start volumes in central London, the proportion of new builds vs refurbishments increased to **46%** of the total – up from **33%** in the Winter 2020 Crane Survey. This reflects a recovery in confidence after the initial shock of the pandemic.
- The uptick in new builds has not disrupted the trend towards refurbishment. This is a structural shift being driven by a greater focus on sustainability.

- In previous surveys, new starts were concentrated in three main markets: the City, Midtown and the West End. The City and West End maintain their dominance in this survey (with a combined 2.5m sq ft of new starts), but Midtown starts are at their lowest since Q3 2019.
- There has been an upturn in volume of new construction at King's Cross and Docklands but there were no new starts at Southbank or Paddington.
- Across all markets, the total volume of office space under construction is 13m sq ft – just over a third (**35%**) of which comprises new starts over the past six months. The total volume under construction fell by a modest **5%** compared to the previous survey period but did mark the third consecutive fall.

Source: *Deloitte Real Estate*

DELOITTE LONDON OFFICE CRANE SURVEY (WINTER 2021)

PERCENTAGE OF PRE-COMPLETION SPACE LET BY SECTOR



Confidence of developers is growing with regard to the **future work agenda**

Climate change **collaboration helping to alter approaches** to development, refurbishment and asset management

Developers **optimistic about leasing demand** and most expect their **pipeline to increase**

Challenges to come from **supply constraints** (construction costs, lack of sites and planning)

- The proportion of pre-let offices under construction in central London fell from **45%** in the Winter 2020 survey to **31%** in the Winter 2021 survey. This is well below the long-term average of **44%** and suggests a willingness by investors to 'look through' current low physical occupancy rates due to the pandemic.

- The uptake of pre-completion office space among key sectors has changed. TMT firms took **39%** of new office lettings in Q1 2021. This fell to **28%** in Q3 2021.

- In contrast, there has been an uptick in letting activity in the financial (**22%** of lettings), legal (**16%**) and professional (**11%**) sectors – particularly among several of the large legal firms.

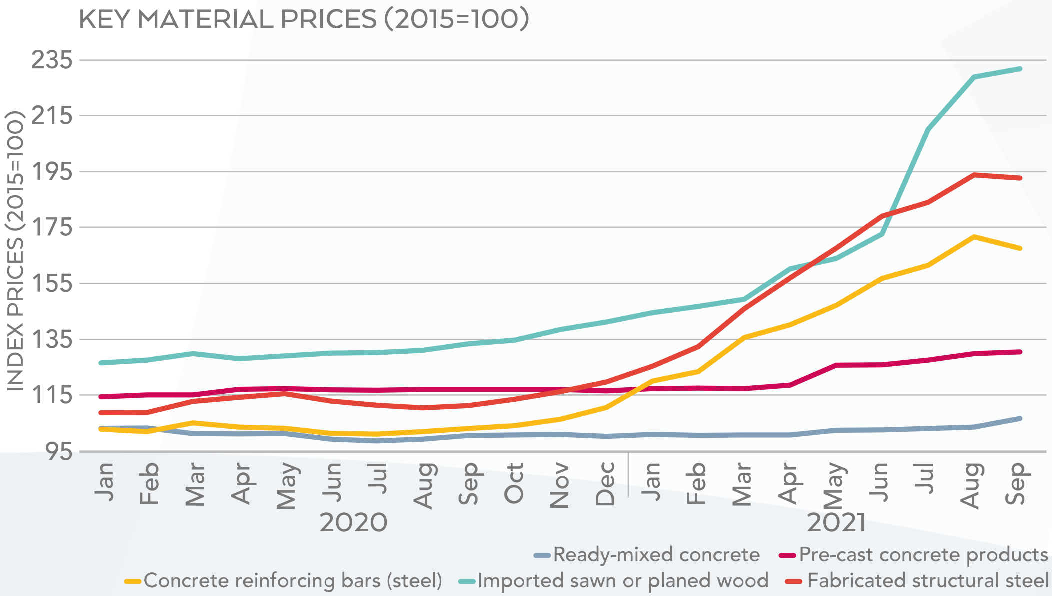
- Developers are now more sanguine about the impact of home working on demand for office space compared to the onset of the pandemic. More than one-third (**37%**) now expect home working to have no impact on leasing demand (compared to **12%** in Winter 2020).

- Reflecting healthy demand, developers now consider that three of the four main challenges stem from supply constraints (construction costs, lack of sires and planning). Just one challenge ('lack of confidence in leasing market') reflected concerns about demand.

- All developers surveyed have introduced measures to quantify carbon emissions and three-fifths have made "a lot of progress…towards achieving new zero from [their] new developments". A quarter of developers expect all their new developments will to be net zero by 2024.

Source: *Deloitte Real Estate*

KEY MATERIAL COSTS



	MONTH ON MONTH Aug 21 – Sep 21	YEAR ON YEAR Sep 20 – Sep 21
NEW HOUSING	**0.3%**	**22.1%**
OTHER NEW WORK	**0.1%**	**23.0%**
REPAIR & MAINTENANCE	**0.2%**	**25.5%**
ALL WORK	**0.1%**	**23.6%**

- The BEIS 'All Work' material price index rose by **23.6%** in the year to September 2021, hitting yet another record high as the sector struggles with ongoing supply chain disruptions.
- However, in September there were early signs that the rate of material price inflation is beginning to ease. The 'All Work index rose by just **0.07%** - the smallest month-on-month rise in nearly a year.
- Costs for certain key materials such as imported wood came off the boil and others, such as steel and rebar, fell by **0.6%** and **2.4%** respectively in September compared to the previous month.
- While there are still widespread reports that shortages of materials are disrupting work on site and contractors are pre-purchasing materials to mitigate long wait times, the worst phase of the supply crunch may have passed.
- Around **50%** of the main contractors surveyed by G&T said that over the next 12 months material prices are expected to climb between **2.6%** to **5%,** but inflationary growth in short-term will likely be higher.
- However, a recent RICS survey suggests even higher inflation is possible, with materials costs viewed as likely to rise by **10%** over the next year amid growing concerns around sourcing and the availability of materials.
- Some contractors have reported three-four month setbacks on certain projects because of shortages of key materials. Escalating prices risk derailing the completion of current projects and could make some future projects commercially unviable.
- Contractors are finding it increasingly difficult to stand over tender prices for longer periods due to the rising cost of materials.

Source: *BEIS*

Key Trade Analysis Likely 12-month inflationary range for key trade packages based on our Q4 2021 TPI Survey results

Key Trade Packages	Summary	Likely Inflation Range (Next 12 months)
Demolition	Across the country there is a large amount of development that will require demolition and site remediation to get going. New demolition/site remediation frameworks indicate a growing new build pipeline. However, with many of these schemes not committed to start until early 2022 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.	**-0.5% to 1%**
Groundworks	Cement and ready-mixed concrete prices have remained relatively flat this year (+3.2% and +6% respectively) but did edge higher in September. Rebar prices came off the boil, falling by 2.4% in the month, but are still up 62% year-on-year. Contractors continue to actively seek work but expect that planned infrastructure and enabling civils works will bolster their pipelines over the next 12 months.	**0.5% to 1.5%**
Concrete	Cement producers across the board are planning to hike prices by £15/tonne (or 16%) at the end of 2021 due to rising energy costs – the biggest single increase in decades. This would translate into an annual rise nearly 30% over the year. Such a jump will hit major projects hard and may impact planned spending on Government projects. The trade is also struggling with shortages due to suppliers committing to large orders from HS2 and Hinkley Point C. A shortage of lorry drivers and increased demand caused by the economic recovery are also creating cost and supply pressures as well as extended delivery times.	**1.2% to 2.5%**
Steel	According to BEIS data, fabricated structural steel prices were up by more than 73% in the year to September 2021. Steel prices fell for first time in over a year in September but with the rapid increase in energy and haulage costs in recent months the monthly fall could prove to be a blip. Unable to absorb the additional costs, British Steel announced a temporary surcharge of £30/tonne on new orders in October (on top of a near £500/tonne increase since July 2020). The most recent steel hikes could have a significant impact on smaller specialist contractors working on fixed price contracts, particularly in light of rising labour costs. However, one positive lead indicator for lower steel prices over the medium term is falling iron ore prices, which are the lowest since May 2020 amid weak demand from a sluggish real estate and property sector in China.	**2% to 4%**
Façades	Façades/cladding products (eg curtain walling and window systems) have been plagued by supply issues. The shortage of metal cladding (eg pre-coated aluminium cladding) and roofing materials is now a major problem across the industry. The UK has a heavy reliance on European-based suppliers/manufacturers such as Kingspan and Euroclad who are pushing up the price of façades and making some models financially unviable. Obtaining the steel coil for the sheet manufacture has become increasingly difficult which has extended delivery from weeks to 5-10 months in some cases. G&T anticipates that Euroclad will increase its materials rates by 20% by early 2022 and there are reports that once the material does arrive, a shortage of cladding fixers means there is an approximate 32-week lead-in.	**2% to 3%**

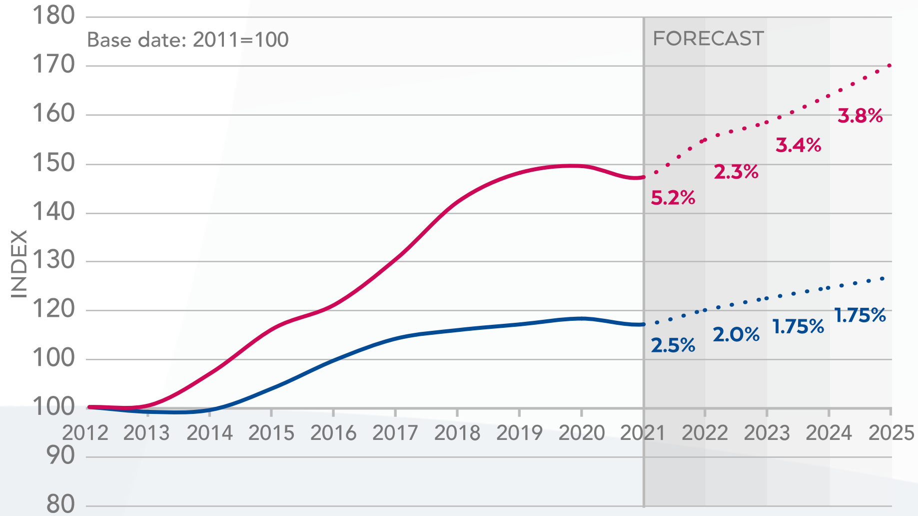
Key Trade Analysis Likely 12-month inflationary range for key trade packages based on our Q4 2021 TPI Survey results

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 towards the end of Q3 2021 as stocks fell. Manufacturing capacity for bricks is at its maximum and some brickmakers are investing in expansion, but exceptional demand has depleted current stock to a low level and the gap is being bridged with imported products. Extended lead times are likely to continue at least until the second half 2022. There is, however, better news in the longer term with additional capacity due to come on stream in 2023. However, high energy prices are impacting 'heavy-side' manufacturers which could lead to significant price increases for bricks. Manufacturers also remain cautious that shortages of labour, raw materials and transport across the wider construction sector could impact demand for bricks, but the main inflationary pressure currently stems from a scarcity of bricklayers which is putting upward pressure on rates.	**1.5% to 2.5%**
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 could drift higher in 2022 due to strong demand.	**1.75% to 2.75%**
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 73% in the year to September 2021. According to the CLC, timber is becoming more readily available and the price has fallen for some imported timber products. However, importers have cautioned that stock is being delayed at the ports here and abroad. After a year of record production and near-record imports, timber supply is now satisfying UK demand according to the TTF. This should encourage greater price stability in the market. However, HGV driver shortages are impacting the supply chain, as are higher fuel costs. An acute shortage of carpenters continues to keep lead times high.	**1.5% to 3%**
Joinery	According to Southern Construction Framework (SCF), its main contractor supply chains reported an average building cost increase of 15% for carpentry and joinery over the past 12 months. This is due to inflation rate rises across joinery products and materials. 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 3%**
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.	**1.5% to 2.5%**
M&E	Bidding competition has eased from 2020 but remains higher than it was pre-pandemic. An increasing number of lower tier sub-contractors are bidding for larger open tenders which is keeping pricing keen. China's cooling property market has slowed demand for copper and while still high from a historical perspective, copper prices have been flat since June and are expected to fall in 2022 as supply ramps up. Contractors continue to report supply issues for many MEP products. 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%**

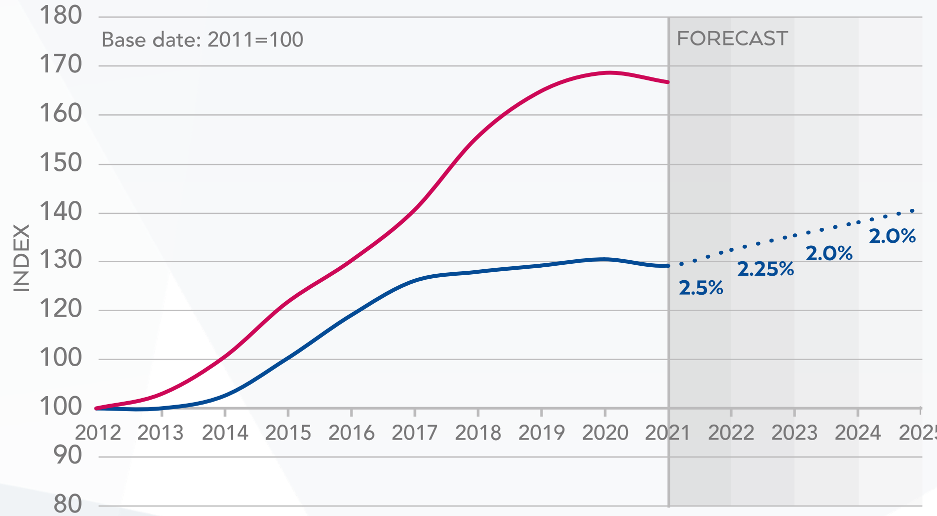
Key Trade Analysis Likely 12-month inflationary range for key trade packages based on our Q4 2021 TPI Survey results

Key Trade Packages	Summary	Likely Inflation Range (Next 12 months)
Roof	The National Federation of Roofing Contractors (**NFRC**) reported sustained growth in workloads and enquiries in Q3 2021, but this was accompanied by worsening material/labour shortages and inflation. Rising workloads have fuelled an increase in direct headcount and labour costs but roofing material availability and costs are of greater concern to contractors. According to the NFRC, concrete roof tiles remained the product in the shortest supply but other key shortage areas include timber battens, insulation and general timber. Contractors anticipate further, broad-based growth over the next 12 months but accompanied by ongoing disruption. Alongside the ongoing issues with materials shortages, the availability and cost of skilled labour is likely to be the next ticking time bomb with three-quarters of NFRC members reporting recruitment difficulties on all sorts of roles from roof slaters and tilers to cladders. These pressures are feeding through into a rise in contractors' tender prices.	**1.5% to 2.5%**
Preliminaries	After averaging at 15.3% in 2020, average main contractor preliminaries costs for the first ten months of 2021 fell to 14.1%. A less certain and more competitive tendering market in the first part of 2021 capped headline preliminaries cost increases, but as the year progressed and workloads/pipeline improved, rising labour costs and higher fuel/energy prices have increasingly pushed preliminaries higher. Other factors are also pushing up costs, such as increased adoption of BIM as well as additional welfare facilities and safety measures remaining in place (despite the CLC's SOPs no longer applying).	**Neutral - Increasing**
OH&P	Average overheads and profit (OH&P) levels have retreated slightly, from 6% in 2020 to 5.8% for first ten months of 2021. There continues to be a trend of large contractors (needing the overhead) entering new sectors and coming into different bands of contracts. This is pushing some incumbent contractors out of the market or causing them to reduce their margins to remain competitive. However, with greater certainty of workload, contractors generally no longer need to work to tight margins. Demand for their services is high and so contractors are increasingly able to pick and choose the most suitable schemes. Even in more competitive sectors with less new work, two-stage procurement strategies may allow headline OH&P to remain static over the next 12 months but margins are likely to be increased through package procurement.	**Neutral - Increasing**

TENDER PRICE TREND 'ALL UK TPI'

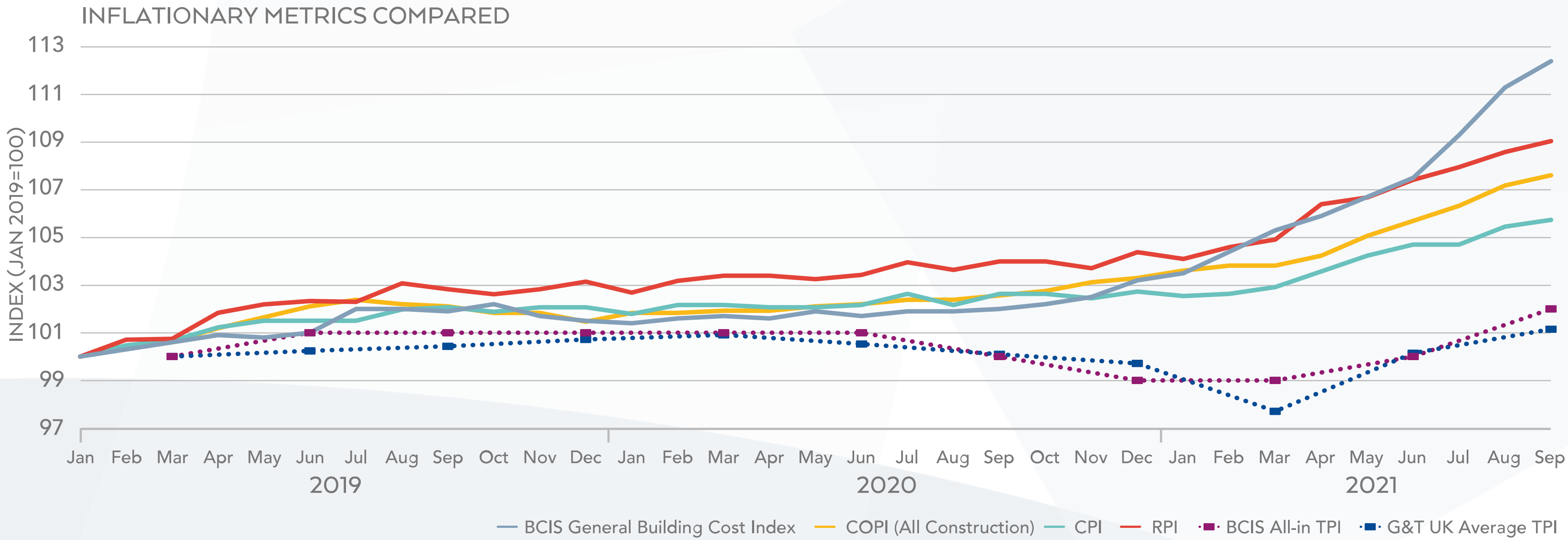


TENDER PRICE TREND 'LONDON TPI'



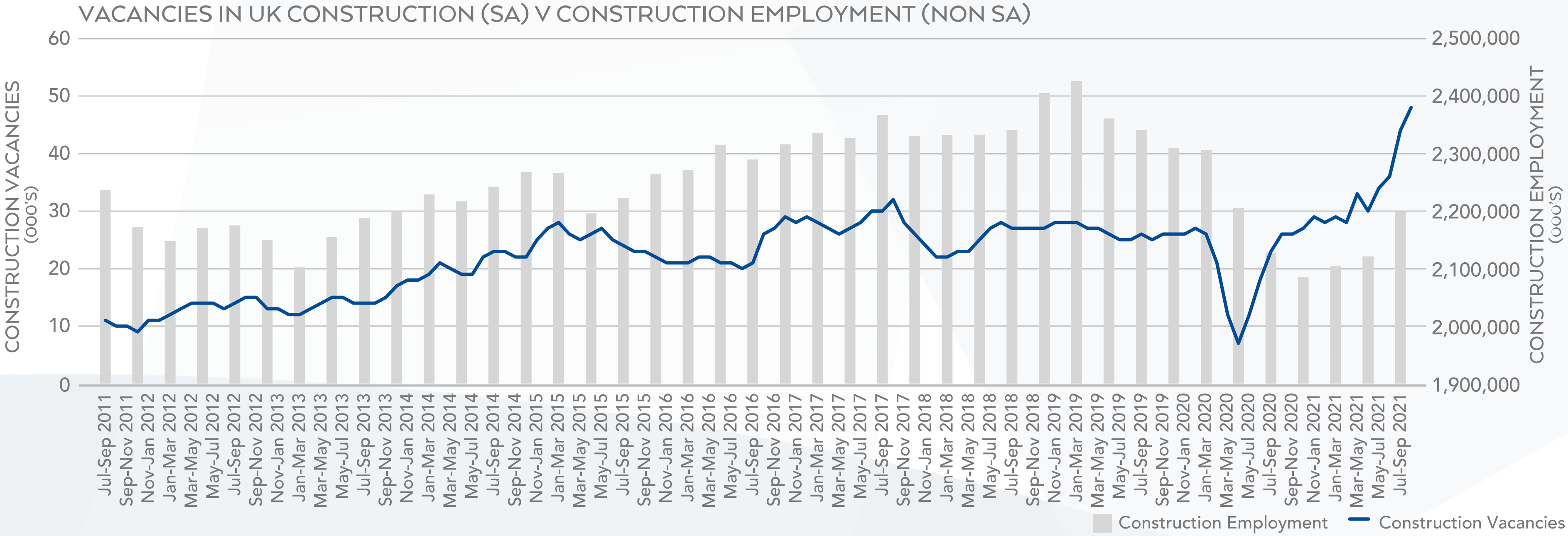
- Many of the current issues and underlying causes of inflation are set to spill over into 2022, but the rate of tender price inflation will begin to ease slightly as supply and demand begins to rebalance
- Demand for construction products has eased from the peak seen in the spring and product supply has improved in some areas, but elevated material prices and the ongoing supply chain crisis has softened demand and hindered construction activity growth
- Some key commodity prices are falling – a good lead indicator that material price inflation pressures will ease in the medium term – but other pressures look set to take centre stage
- An increasingly tight labour market and fierce competition to attract workers is likely to result in mounting wage pressures and translate into "stickier" inflation
- Labour constraints are likely to be the primary driver of inflation throughout 2022 and beyond
- Transport issues are impacting deliveries and extending lead in times. Record high shipping costs and increased energy prices are also feeding through into input costs
- Contractor 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

Note: BCIS does not publish regional TPI forecasts



- Key inflationary metrics such as the ONS's construction output prices index (**COPI**), the BCIS' general building cost Index, the CPI and RPI rose gradually in 2020 but growth rates have accelerated since January 2021.
- The UK's CPI (up **3.1%)** and RPI (up **4.8%**) inflationary measures, along with the 'All Construction' COPI (up **4.27%**), have all risen at similar rates during the first nine months of 2021. However, the BCIS' General Building Cost Index (which measures movement in the cost of labour, material and plant to a contractor) has increased at a sharper rate than the aforementioned indices.
- From mid-2020 to early 2021, the graph above shows an initial divergence between input cost inflation indices such as the COPI and BCIS' GBCI, and the tender price indices (ie G&T's UK Average TPI and BCIS' All-in TPI).
- During this period, weak new order growth and uncertainty over future workloads created competitive market conditions and contractors were more willing/able to absorb some of the initial input cost rises with competitive tender submissions in order to secure work.
- However, as input cost inflation accelerated further during 2021 and certainty of workload returned, the buying window closed and contractors were in a better position to pass the steep input cost rises on to clients.
- Although input cost inflation is generally expected to stabilise and begin to fall back in the second half of 2022, recent positive new order growth and strong contractor project pipelines will produce less competitive tendering conditions. As such tender price inflation will remain elevated throughout 2022.

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.*



- ONS data shows that construction vacancies continue to rise steeply. Job vacancies in the three-month period between August-October 2021 were 48,000 – **9.1%** higher than the previous period (July-September 2021). Construction vacancies have hit a record high and are well above the 10-year average of 23,000.

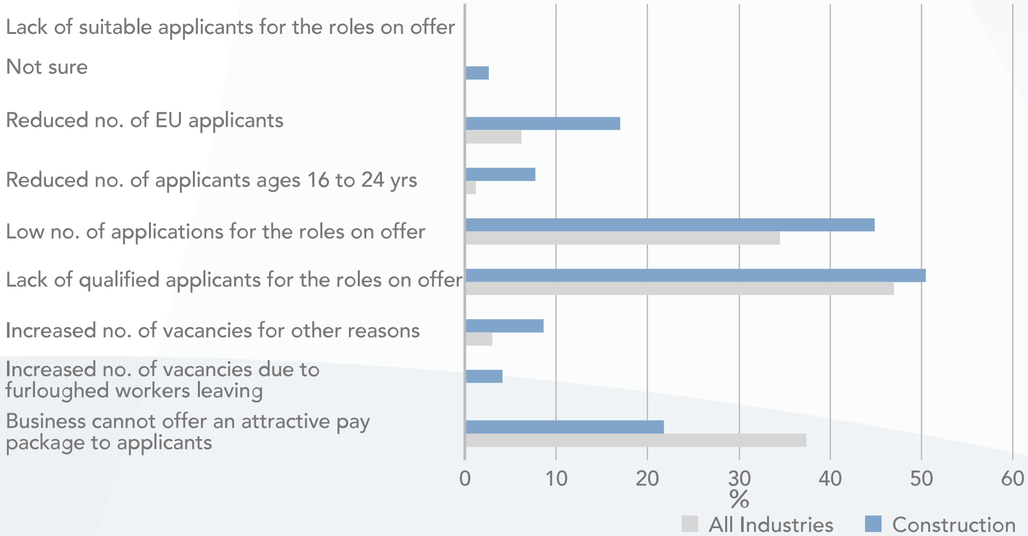
- October's IHS Markit/CIPS UK Construction employment index signaled that, although down from its seven-year peak in May, employment numbers increased at a sharp and accelerated pace in October. Although **26%** of the survey panel reported an increase in staffing numbers during the month, construction companies often noted that a lack of available candidates had led to unfilled vacancies.

- Higher levels of employment can be attributed to robust order books and optimism about near-term growth prospects, but widespread shortages of staff have disrupted work on site and led to longer wait times to agree new contracts. 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.

- The latest RICS Survey as well as G&T's main contractor survey both point to the availability of skilled labour as a key area of concern that will impact on both cost and profitability. The acute shortage of skilled subcontracted labour is particularly affecting bricklayers, carpenters, plasterers, electricians and plumbers and there is a concern that workload will shrink to fit the reduced labour market.

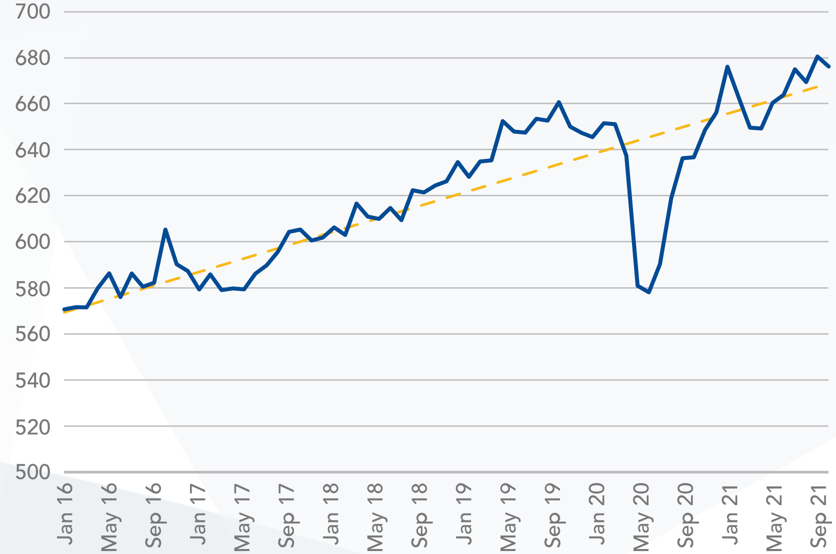
Source: *ONS*

WHY DID YOUR BUSINESS FIND FILLING VACANCIES MORE DIFFICULT, OVER THE LAST MONTH COMPARED WITH THE NORMAL EXPECTATIONS FOR THIS TIME OF YEAR? (4 OCT - 31 OCT 2021)



AVERAGE WEEKLY EARNINGS (UK CONSTRUCTION)

SEASONALLY ADJUSTED



- The reasons for the current difficulties in filling vacancies are highlighted in the ONS's dataset (Business insights and impact on the UK economy). The three key issues were a lack of qualified applicants (**47%**), an inability to offer an attractive pay package to applicants (**37.4%**) and a low numbers of applicants and for the roles on offer (**34.5%**). A reduced number of EU applicants was also a significant factor that made filling vacancies more difficult.

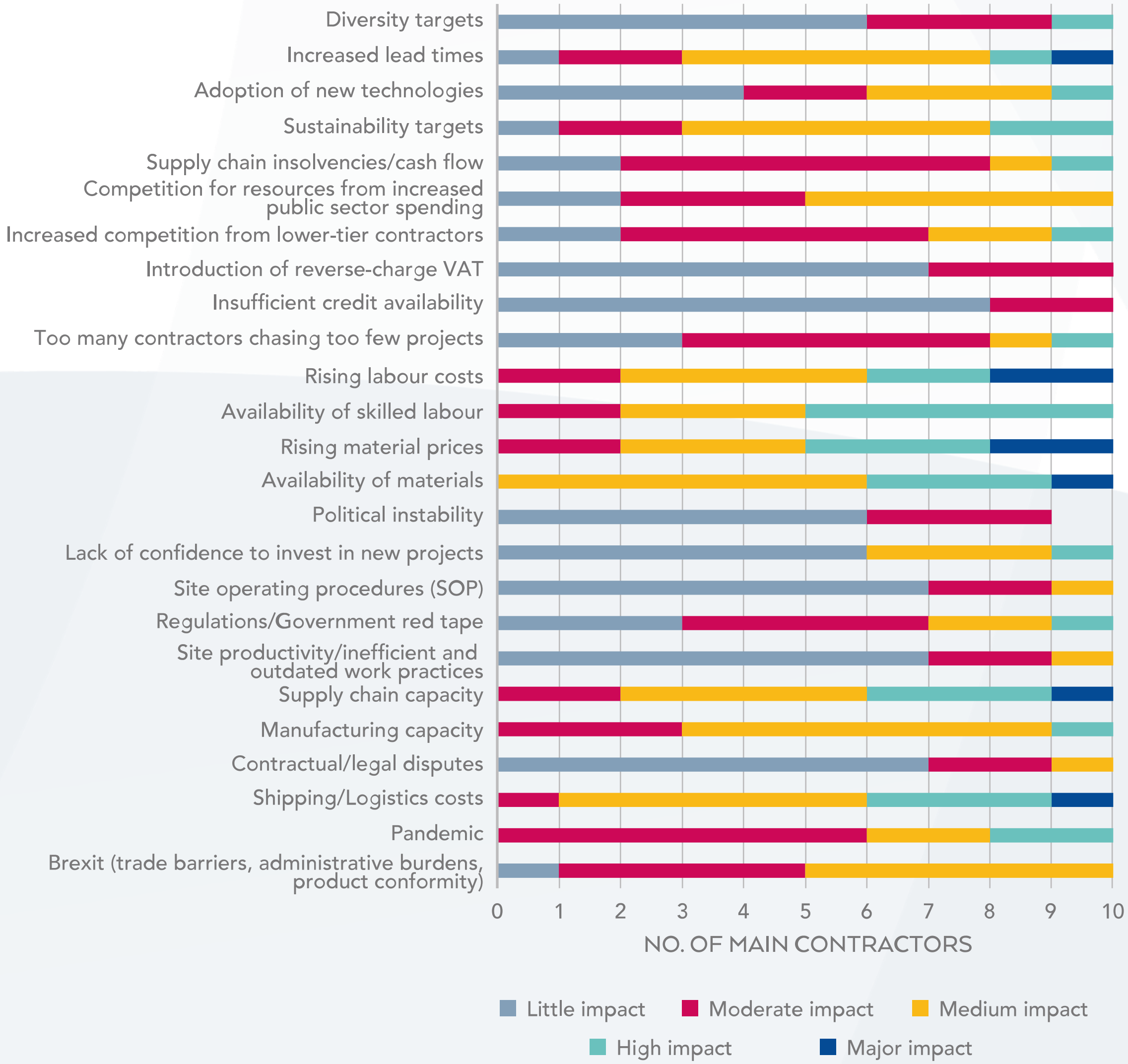
- Labour shortages are not only affecting the construction sectors ability to work to capacity, they are also driving wages higher. Average weekly earnings in the three-months between July-September 2021 were up **7.1%** compared to the same period one year earlier.

- The expectation among main contractors surveyed by G&T is that both directly employed staff costs and sub-contracted labour costs will increase further over the next 12 months. Although most contractors have been able to match resources with their project workload and planned growth, the reduced availability of operatives in key trades has prompted some to demand unrealistic and unsustainable rates. This is becoming a major business and industry issue according to some contractors.

- Raised salary expectations have led to a significant increase in churn. The labour squeeze has also been a key factor for stalling projects and there are growing concerns that it will dampen appetite for new investment.

Source: ONS

TO WHAT EXTENT ARE THE FOLLOWING LIKELY TO IMPACT YOUR BUSINESS OVER THE NEXT 12 MONTHS?



- In G&T's Main Contractor Survey Report (October 2021), 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
- 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

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 CDEs 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

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

Market Update
November
2021