MARKET UPDATE

February

2021

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ACCOUNTING

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G&T's Market Update for February 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 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:

- Provide an overview of some of the key takeaways from Deloitte's Winter 2020 London Office Crane Survey
- 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 and trade, as well as furloughing trends and construction vacancies
- Summarise some of the impacts that EU–UK Trade and Cooperation Agreement could have on construction

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

UK economy
EXPANDED
BY
16%
(Q3 2020)

UK on track for a
W-shaped recovery
(in Q3 2020)

EY Item Club
upgrades
UK economic outlook
(2021)
6.2%

Two consecutive quarters of economic decline in 2020 were followed by a **16%** expansion in Q3.

While output in the services, production and construction sectors increased by record amounts in the third quarter of 2020, the level of output remained below Q4 2019 levels, pre-COVID-19.

On an annual basis, 2020 will record the biggest drop in national output since 1709. The bounce in Q3 2020 prompted some to hope that the UK would recover much of the lost ground by the year's end. However, this proved to be a false dawn. GDP growth in Q3 2020 proved to be fleeting and the UK economy now looks set to end 2020 more than 10% smaller than it was in the final few months of 2019.

In light of the Government's lockdown restrictions in Q4 2020, it's highly probable that the UK will experience a double-dip recession in 2021 or, if assigning a shape to it, a 'W'-shaped recession and recovery. A significant bounce back is expected later on in the year as pent up demand is released.

- In early December 2020, the EY Item Club forecasted that the economy would grow by **6.2%** in 2021, a slight improvement from previously expected growth of **6.0%**.
- Since then, the vaccine rollout programme has gathered pace and a free trade agreement with the EU has been secured. Once the economy fully re-opens, pent-up demand will be released and a sustained recovery can begin.
- Although business activity is expected to slump and economic growth to contract sharply in Q1 2021, economists anticipate the second leg of the double-dip recession will not be as severe as the first. This is largely due to manufacturing and construction having stayed open throughout the latest lockdown.
- Macro indicators, namely the CPI and the RPI, indicate that the UK is in a sustained low-inflation environment. Price conscious consumers, excess capacity, limited earnings and curtailed economic activity are likely to limit inflation in the near term, but the expectation is that this trend will reverse in the coming months and inflation will gradually edge back up.

SUMMARY OF KEY FINDINGS: CONSTRUCTION

UK Construction extended its robust recovery, with activity expanding for the seventh consecutive month. December's PMI reading was **54.6**, little changed from **54.7** in November.

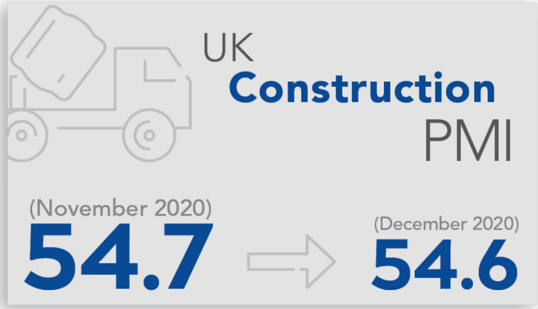
December's survey reported strong business optimism as both output and new orders have increased every month since June. Although growth is slowing, overall output levels are encouraging and show strong underlying demand.

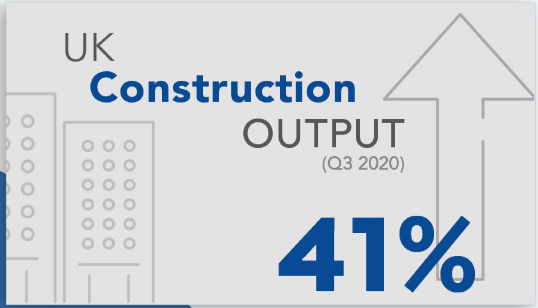
It's clear that the housing sector is currently the biggest driver of growth. However, demand is expected to broaden out beyond residential projects over the next 12 months, led by infrastructure spending and a small potential rebound in new commercial work from the current depressed levels.

Rising workloads in recent months have contributed to a sharp increase in purchasing activity at the end of 2020 as some companies brought forward input buying due to concerns about longer lead times among suppliers.

According to the latest ONS data:

- UK construction output (All Work) rose by **41%** in Q3 2020 – the largest rise since quarterly records began
- Output has now grown for seven consecutive months and in November 2020, construction output was just **1.4%** lower than it was in the same month in 2019
- New orders (All New Work) rose by **89%** in Q3 compared to the previous quarter. In fact, new order values in Q3 were marginally higher than they were in the same quarter in 2019 – **0.6%** or £70m higher
- In London, commercial new orders closely followed the national trend and rose by **72%** in Q3. Residential new orders, however, fell by **10%** from the previous quarter.





SUMMARY OF KEY FINDINGS: MATERIAL PRICES AND TPI

Material Price Index
(All Work)
3.1%
(Nov 2019 - Nov 2020)

Structural Steel experienced **high rates** of **inflation**
8.4%
(Aug 2020 - Nov 2020)

Upward inflationary pressure on *input costs* likely in 2021

Material price inflation in 2020 was driven by a supply and demand imbalance. Manufacturing capacity struggled to keep up with a rapid rise in demand for finished products and raw materials. This was exacerbated later on in the year by port disruptions and rising shipping costs. Suppliers were able to name their price for goods in acutely short supply.

- The ONS' material price index for **'All Work'** rose by ***3.1%*** in the year to November 2020. After briefly falling in the summer months, the index rose sharply in the autumn.
- Several key materials such as fabricated structural steel and imported timber experienced above-average cost inflation of ***8.4%*** and **5.8**% respectively in the three months to November 2020.
- Dislocated supplier and distribution channels are largely a result of the pandemic. In December, limited container capacity at UK ports and factories closing and re-opening led to longer delivery times and the fastest rate of input cost inflation since April 2019.
- EU-UK trade agreement meant that immediate material price hikes were avoided at the border.
- Risk of delays at the border as trading volumes pick up, new customs systems bed in and full declarations have to be made from July 2020.
- Higher input costs will put upward inflationary pressure on tender pricing in 2021. However, countering this in the early part of 2021 will be subdued new orders and muted workloads/activity in certain sectors (eg retail, hospitality and commercial office).
- Some clients are likely to withhold investment and delay decisions to move ahead with new projects whilst national lockdown restrictions are in place.
- Many contractors, particularly lower tier ones, are still very keen to secure turnover and pipeline work. This will create a competitive tendering market, especially for smaller schemes with single-stage tendering deployed.

-2.3% Consumer spending **contracted** by 2.3% *year-on-year in December*

4.2% OECD forecast a 4.2% **expansion in GDP** *for 2021*

Demand Subsiding Residential housing's **vigorous growth** expected to level off

Oil US$56 (Jan 2021) **Moderate rises expected** in 2021 as supply fails to meet recovering demand

54.6 (Dec 2020) Down from **54.7** in Nov *but activity still expanding*

CPI 0.6% (Dec 2020) Inflation expectations **for 2021 are gradually rising**

0.1% **Base Interest Rate** held

£895bn **Quantitative easing programme target** by Bank of England

£46.4bn Paid through **Coronavirus Job Retention Scheme** *since April*

5% Unemployment Rate (Sep-Nov 2020) *Rate edged higher in latest three-month period.* OBR estimate rate to peak at **7.5%** by mid-2021

3.6% **Average weekly earnings** *(Y-on-Y three month average)* **rose in Nov 2020**

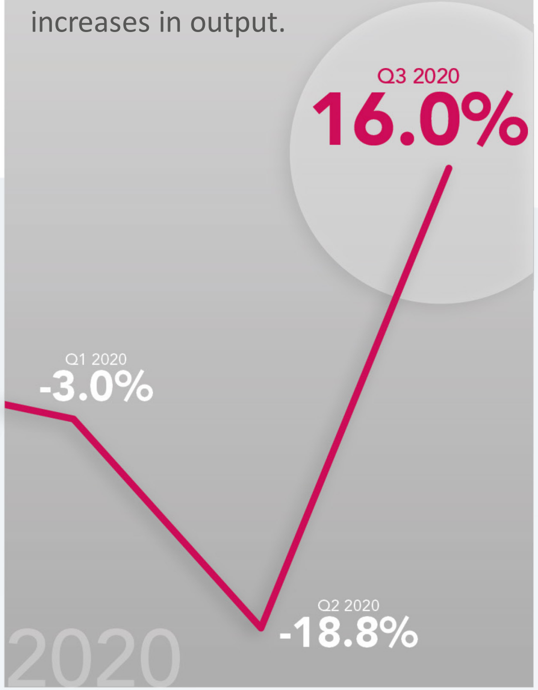
UK Economy

Overview	Latest	Forecast Q1/21	Q2/21	Q3/21	Q4/21	Units
GDP Growth Rate	16.0	-2.6	2.1	1.6	1.0	%
Unemployment Rate	5.0	7.8	8.1	7.9	7.4	%
Inflation Rate (CPI)	0.3	0.9	1.6	1.5	1.9	%
Interest Rate	0.1	0.1	-0.1	-0.1	-0.1	%
GDP from Construction	28,813	28,242	23,975	30,974	29,735	GBP Million
Government Debt to GDP (the ratio between a country's government debt (cumulative amount) and its GDP)	99.5	110	110	110	110	%

Source: *Trading Economics and ONS*

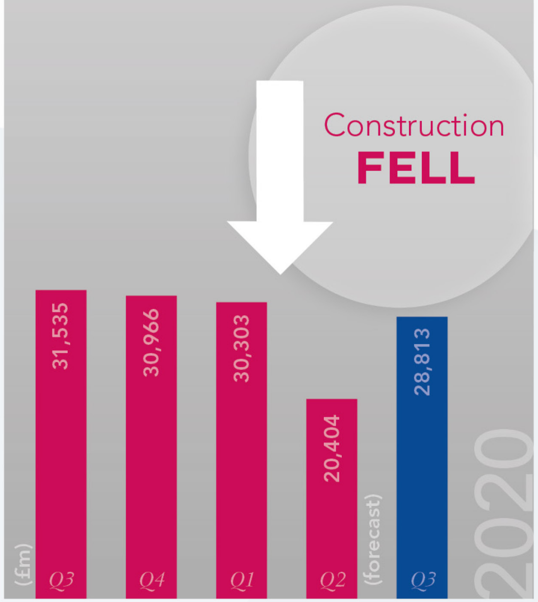
Please note: *The economic forecasts provided above have been sourced from Trading Economics. These forecasts are updated periodically and do not necessarily reflect G&T's UK economic outlook.*

After an unprecedented **18.8%** fall in Q2 2020, UK GDP rose by **16%** in Q3. All three major drivers of growth – services, manufacturing and construction – saw quarterly increases in output.



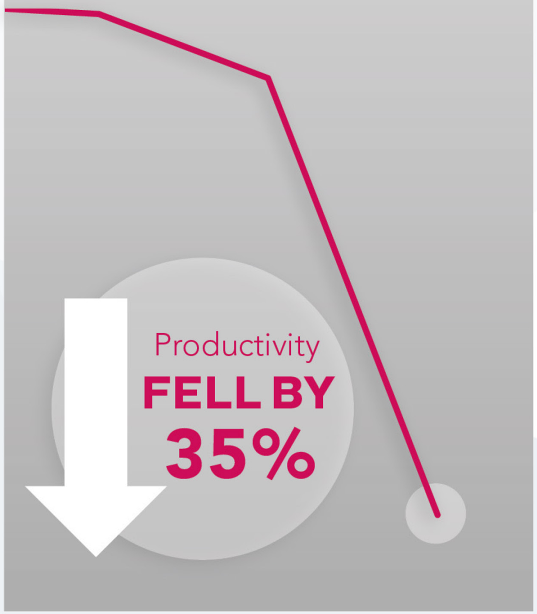
GDP: Quarter on Quarter Growth: Chained Volume Measure* Seasonally Adjusted

GDP from Construction in the UK fell by **33%** in Q2. The latest data shows a partial recovery was made in Q3, however GDP from construction still remains some **8.6%** lower than it was one year ago.



UK GDP From Construction

Construction productivity fell by nearly **35%** in Q2 2020 as many contractors closed sites or paused work on-site at the end of March.



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

Please note *– Chained Volume Measure (CVM) means that data from successive years have 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

Eurozone economy expanded by **12.7%** in Q3 2020 as demand rebounded – the sharpest increase since records began.

Productivity increased, household spending rose and export volumes jumped but output remained well below year-on-year levels.

Recent reintroduction of strict containment measures across the bloc is likely to push the recovery into reverse and GDP to shrink in Q4.

Eurozone industrial production has remained strong, with factory output cushioning the economy in recent months.

ECB expects GDP to grow by **3.9%** in 2020 (downgraded from a forecast of **5%** made in September). Near-term outlook has deteriorated but vaccines will re-establish normal conditions for most services.

US

US GDP expanded at an annual rate of **33.4%** in Q3 2020 but GDP is still **3.5%** below its pre-pandemic level.

Personal consumption expenditure and investment recovered strongly in Q3, fuelled by more than $3 trillion in pandemic relief.

Further fiscal stimulus package on the horizon in 2021 after a winter surge of the coronavirus. Federal Reserve intends to continue large-scale bond purchasing to aid the recovery.

Second stage of new economic agenda expected to call for longer-term spending on infrastructure, green energy and education.

The FED raised its 2021 GDP forecast from **4.0%** to **4.2%**. The forecast signals the country will fully recover to pre-pandemic levels by the end of 2021.

China

China's year-on-year GDP growth in Q4 2020 was **6.5%** – the highest of any quarter since 2018.

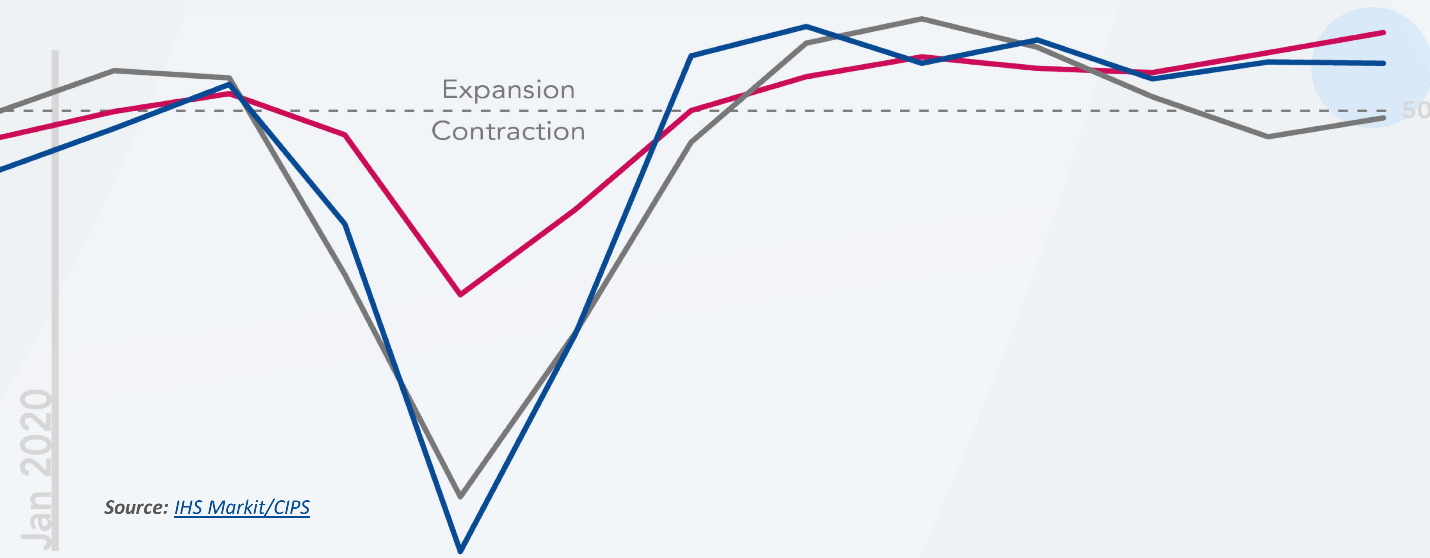
China's economy grew by **2.3%** in 2020 – the slowest pace in more than four decades but making it the only major economy to register positive growth in 2020.

Industrial production and strong export growth driving China's recovery. However, consumer spending is still weak, coinciding with the lowest rates of inflation in more than a decade.

The IMF trimmed back its 2021 growth projection for the Chinese economy from **8.2%** to **7.9%** to reflect an increasingly hostile geopolitical climate and challenging global economic conditions.

December's construction PMI survey revealed…

- Output expanded for the seventh consecutive month with increased activity primarily reflecting another sharp rise in house building.
- Commercial activity expanded but growth eased to its lowest since the recovery began last June while civil engineering works contracted.
- Total new orders also increased for a seventh straight month with respondents noting improving client demand and business wins from deferred projects.
- Rising workloads contributed to a sharp increase in purchasing activity at the end of 2020 as some companies brought forward input buying due to concerns about longer lead times among suppliers.
- Input cost inflation quickened to the highest since April 2019, reflecting supply shortages and strong demand for construction inputs.
- Stretched supply chains and delays at UK ports resulted in longer delivery times.
- Slight rebound in employment numbers reflecting forthcoming new projects and improved business outlook.
- Business activity growth expectations were the strongest since April 2017 with only 10% of the survey panel anticipating a decline in activity in 2021.

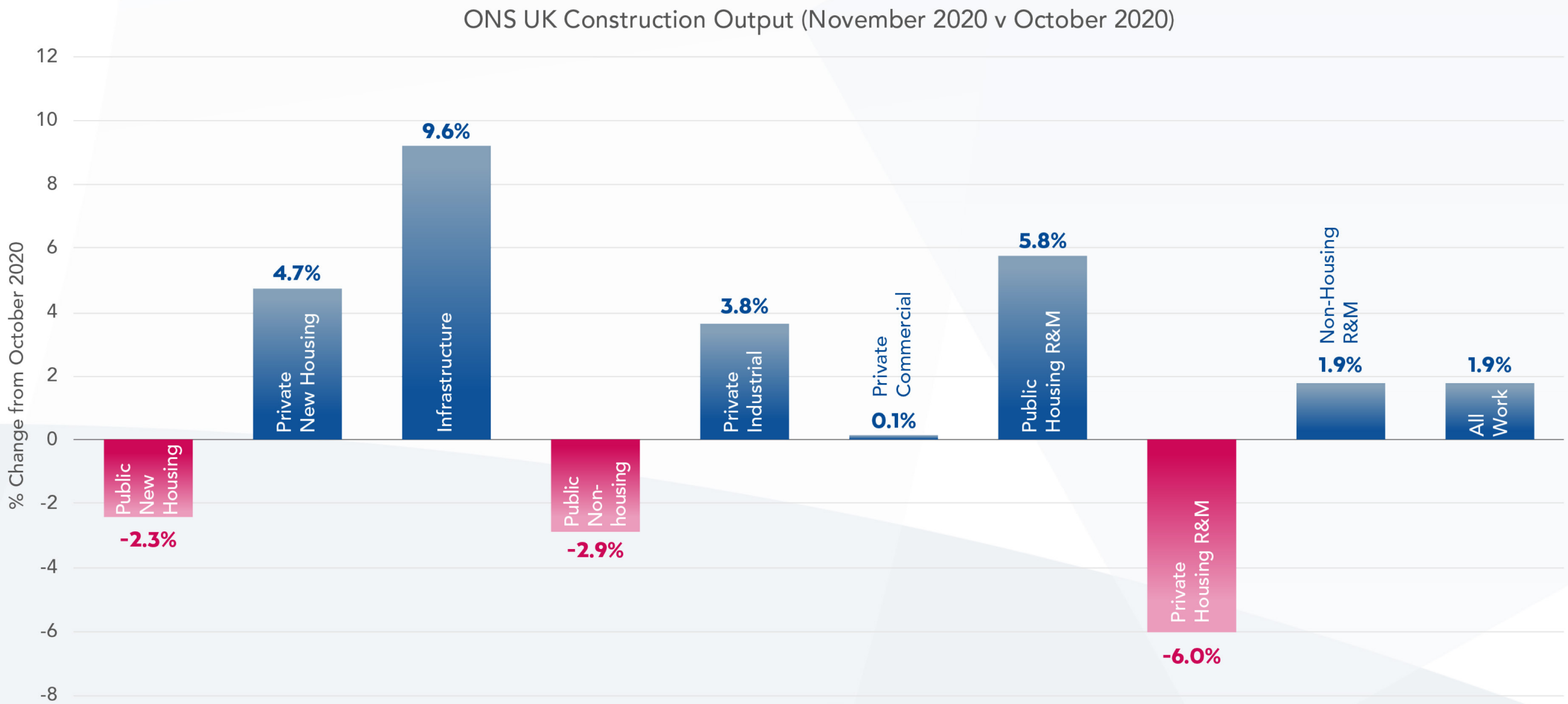


Services **49.4**

Manufacturing **57.5**

Construction **54.6**

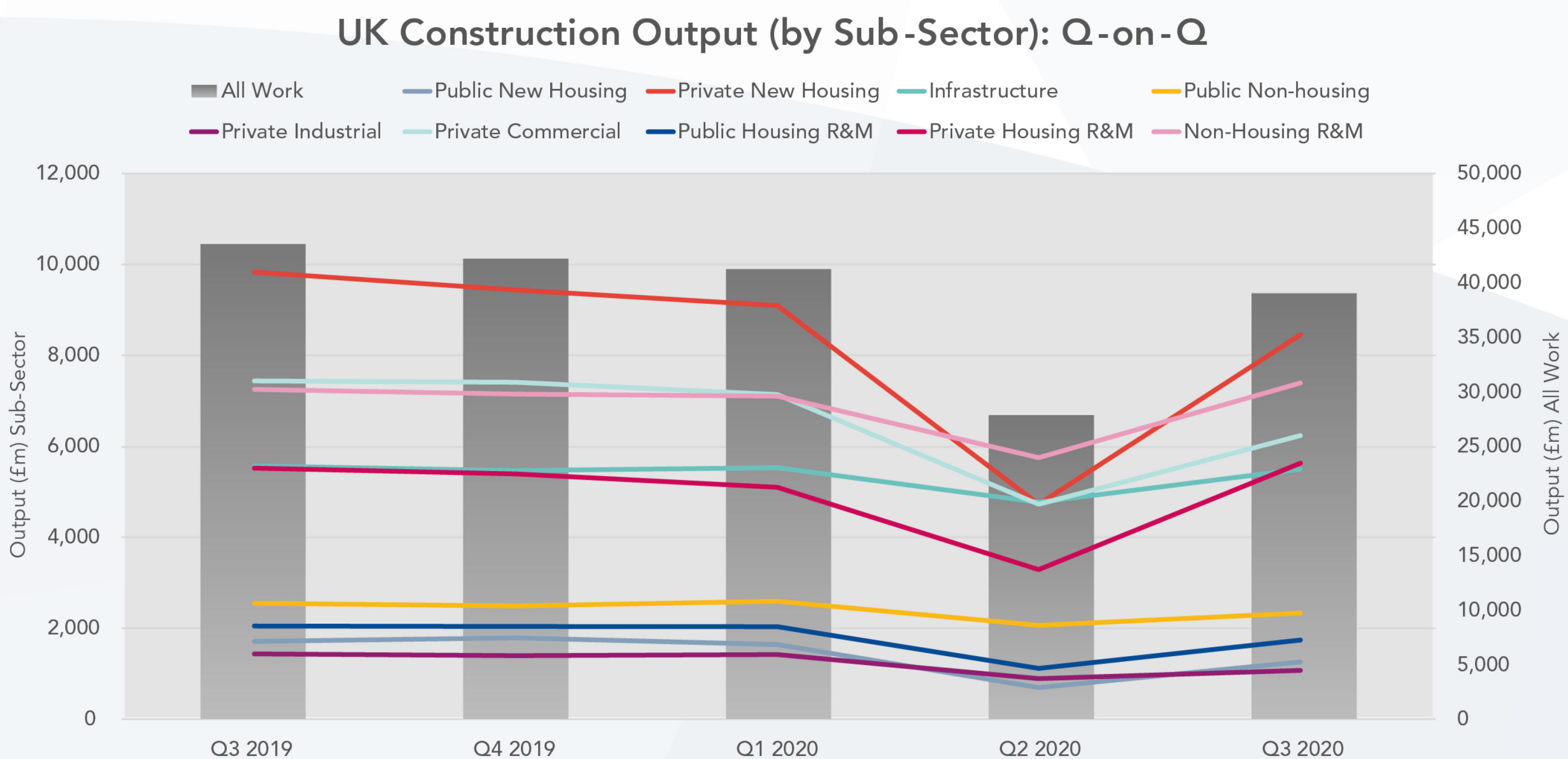
Source: *IHS Markit/CIPS*



- Construction output ('All Work') rose by **1.9%** in November 2020 compared to the previous month.
- Output has now grown for seven consecutive months and in November 2020, construction output was just **1.4%** lower than it was in the same month in 2019.
- The infrastructure sector led output growth in November **(+9.6%)** as the industry got stuck into a series of major public infrastructure programmes. Meanwhile, private housing R&M work, although providing a relatively consistent source of fuel for recovery since June, fell by **6%.**
- Private new housing was another strong sub-sector, with output growing by **4.7%** in November and contributing in excess of £3bn worth of output to the £14bn UK construction sector. Higher demand for private new housing has helped underpin the recovery in output and also led to a rise in employment numbers.
- Private commercial output growth remained suppressed as clients and developers struggle to decide on a long-term strategy for commercial office occupation post COVID-19 and determine what the 'office of the future' might look like.

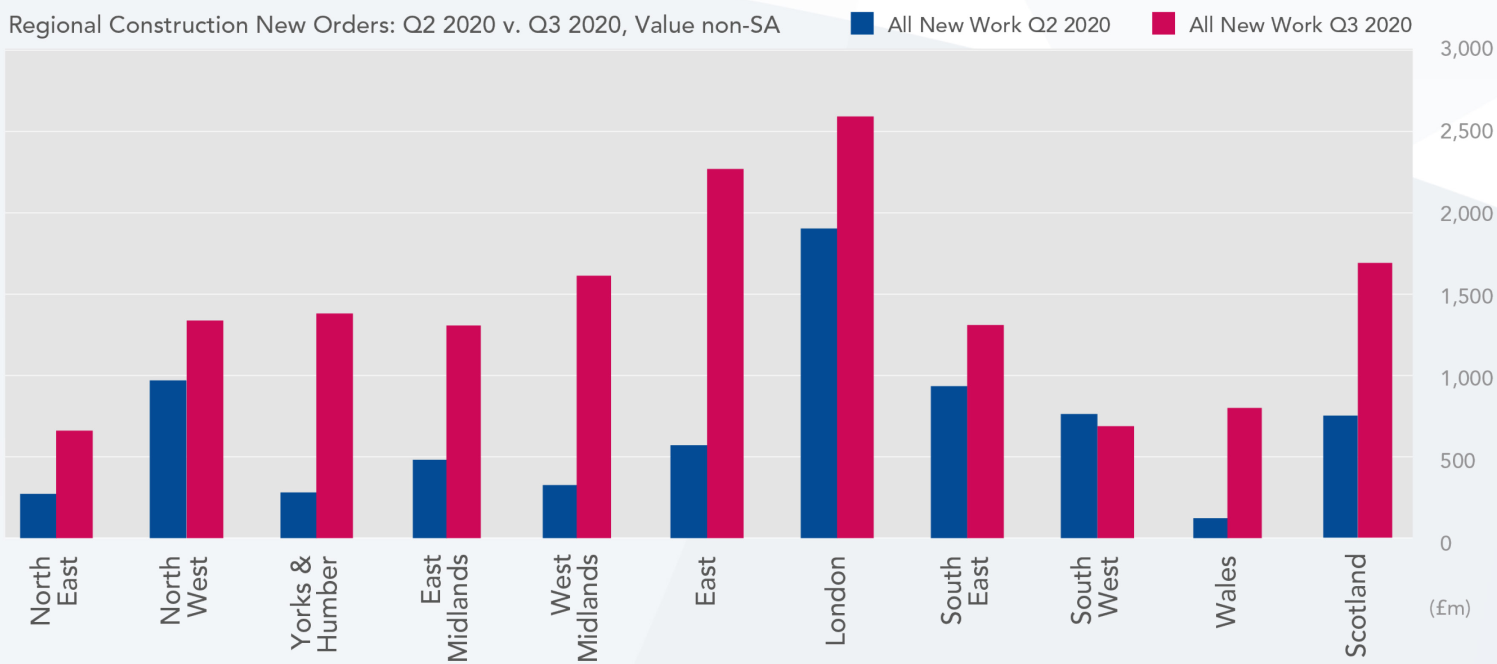
Source: *ONS*

- After dropping by a record **33%** in Q2, construction output made a partial but strong recovery in Q3. Output rose by more than **41%** across all sectors but despite the strong performance in Q3 2020, output was still **8.6%** adrift of its pre-pandemic level in Q3 2019.
- From the low Q2 base, output saw a near V-shaped recovery in Q3 2020 as economic conditions began to improve and productivity returned to near-normal levels. The quick recovery can largely be attributed to the Government putting construction at the front and centre of its recovery plan.
- Reduced planning applications and weak order pipelines in some sectors (eg retail and hospitality) will dent output growth in 2021. However, a handful of key sectors (eg healthcare, senior living, logistics and infrastructure) should more than offset lower output levels in these sectors.
- Output for the whole of 2020 is still expected to be around **15%** lower than it was in 2019. Looking ahead, the CPA forecasts that output will grow by **14%** in 2021 and **4.9%** in 2022. However, there is a risk that output could slump lower if unemployment rises later on in the year. The CPA notes the delivery of major infrastructure projects will be crucial to output growth in 2021.



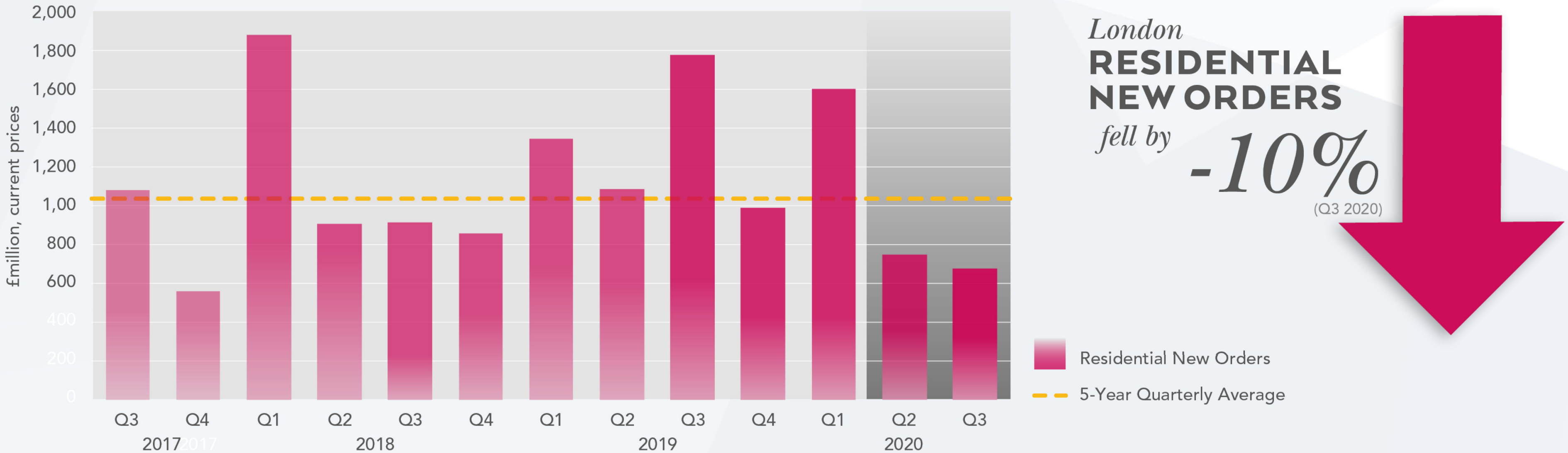
Source: ONS

- Construction new orders rose by **89%** in Q3 2020 compared to the previous quarter - the highest quarterly growth rate since new order records began in 1964.
- All sectors, other than public new housing, experienced record quarterly new order growth rates. However, new private industrial work led the recovery, rising by nearly **140%** between Q2 and Q3 2020 due to the increased need for logistics, distribution and warehousing facilities.
- On a regional level, the South West was the only region to see a fall in new orders (**-10%**). All other regions experienced double or triple-digit quarterly growth.
- The Q3 recovery in new order growth was sharper in regions outside of London and the South East.
- PMI survey data towards the end of 2020 points to a sustained recovery in new order growth. IHS Markit's December report, for example, reveals improving client demand and workloads. New wins from deferred projects helped order book growth to remain close to November's six-month high.
- However, there is a lack of long-term commitment in certain sectors and a question mark remains over how the latest national lockdown will affect the speed at which future projects are brought forward and how they will impact decisions on private investment.



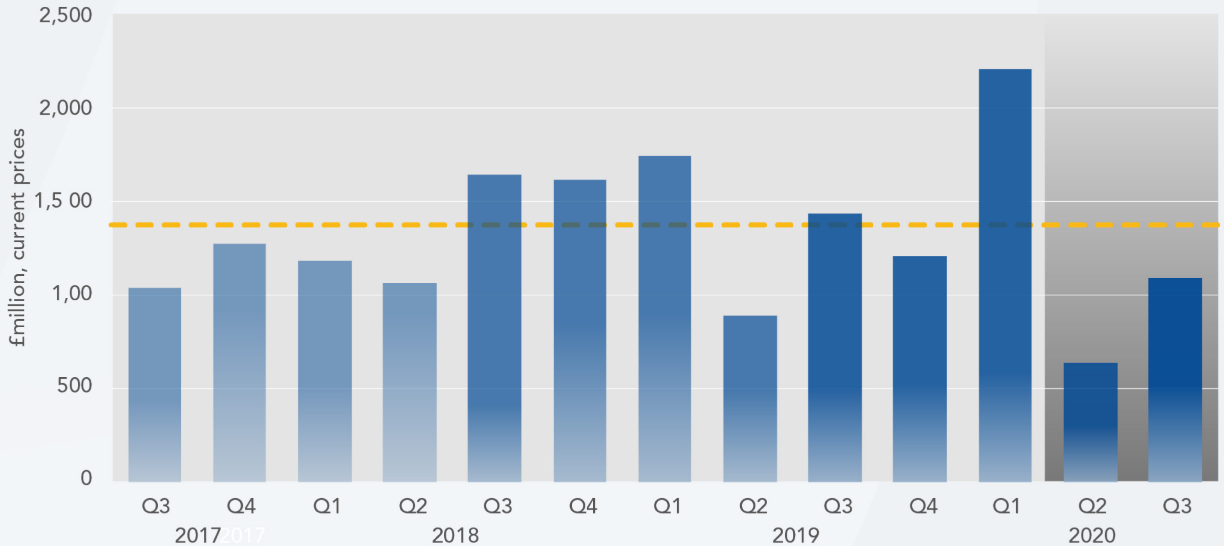
Source: ONS

- London Residential new orders fell a further **10%** in Q3 2020 to **£679m** – well below the five-year quarterly average of **£1.04bn**.
- Housing completions returned to more normal levels in Q3 2020. Completions jumped from **3,000** in Q2 to **5,300** in Q3, putting total completions in the year to Q3 2020 at **21,598**. However, this represents an annual fall of **-11%** and is still well short of the draft London Plan's identified need of **66,000** homes per annum.
- COVID-19 has had a significant short-term impact on London residential construction. Continuing the longer-term downward trend, the number of new starts on site fell by a further **16%** in the year to Q3 2020. However, a significant pipeline remains of over **61,000** private units under construction (on sites with more than 20 homes) in London. This should translate into increased delivery in the medium term.
- The mainstream market (below £1,000/sq ft) has recovered more strongly than the prime market. This has been driven by need for home-working and leisure space, Help to Buy and the recent stamp duty holiday. However, the greatest demand is for more affordable homes and local authority run housing companies have significant development pipelines in place to combat the shortfall.
- According to BCIS' Private Housing Construction Price Index (**PHCPI**), construction costs have risen by around **2.7%** in the year to Q4 2020. This has largely been fuelled by supply shortages and rising material prices.

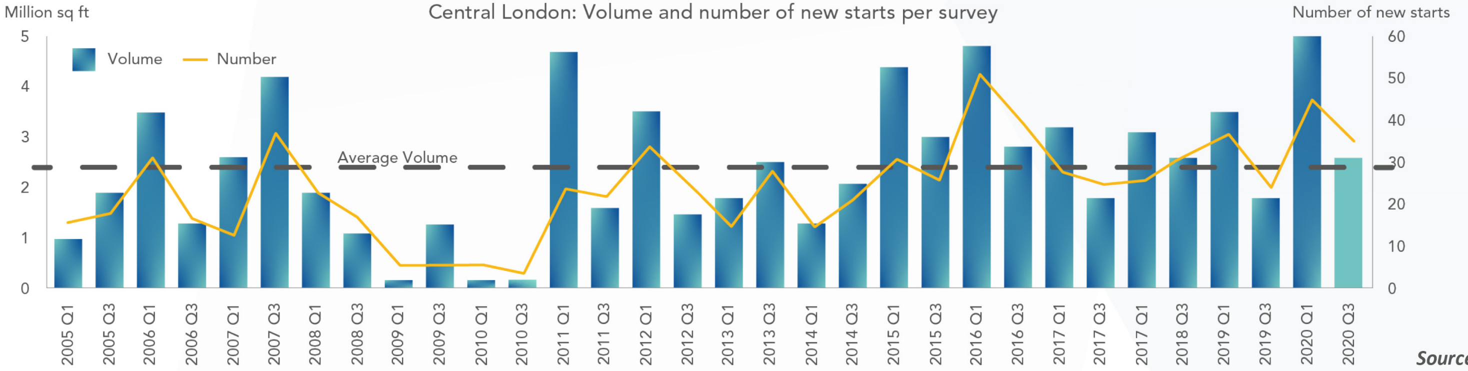


Source: *ONS, Molior*

- London Commercial new orders rose by **72%** in Q3 2020 from **£628m** to **£1.08bn** but were still well below the five-year quarterly average of **£1.4bn**.
- The total amount of office space under construction remains close to its all-time high (15.1m sq ft across 117 schemes in Q3 2020). There is still a strong central London office pipeline for 2021 but it has been boosted by a significant number of delayed schemes, shifting many completions to 2021 (Deloitte).
- Developers and clients have been delaying decisions on further speculative developments, waiting for further clarity in the market and on future working practices before deciding on a long-term occupier office strategy.
- Around two-thirds of new starts on site in the six months to September 2020 were refurbishments. Businesses are increasingly reviewing their footprints and releasing existing space that is being adapted, refreshed or repurposed.
- Commercial new order growth is likely to remain suppressed in 2021 but high quality office products may still go ahead as these offer better sustainability as well as health and wellbeing features (ie a 'flight to quality').
- Sentiment has shifted with COVID-19, temporarily reducing demand for commercial space and leading to a fall in new starts. In the short term, we're more likely to see price drops, delayed decisions, extended feasibility review of schemes and perhaps more phased starts with limited commitment.

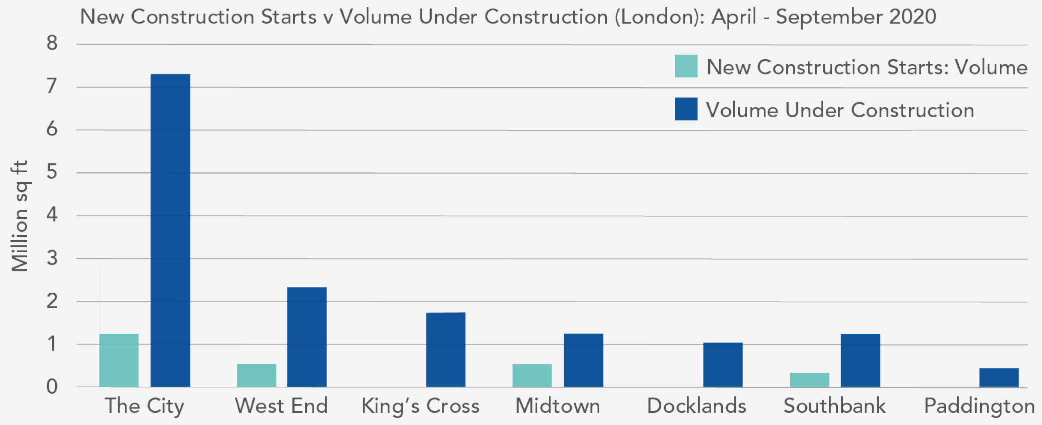


Source: ONS



Source: [Deloitte Real Estate]

- **50%** decline in the volume of new construction starts compared to the six-months to March 2020.
- However, 2.6m sq ft of new London office projects started in the six months to September 2020 – broadly in line with the long-term survey average and exceeding new starts in the corresponding period in 2019.
- 35 separate schemes broke ground during the survey period – significantly higher than the long-term average of 24 but the typical size of new developments shrank by a third to an average of 70,000 sq ft.

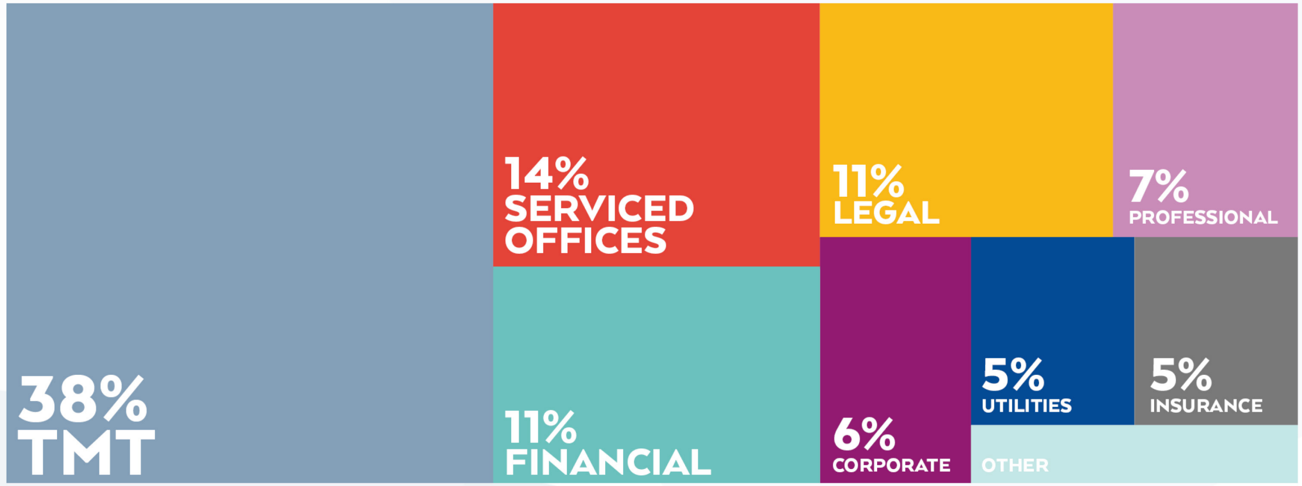


- The largest new start between April and September was 20 Ropemaker (447,000 sq ft) in the City. The building is expected to complete in early 2023.
- The West End had the highest number of new starts (12) but the City saw the highest volume of new construction starts (1.2m sq ft).
- Volume of space under construction in the City was unchanged from the previous survey (7.3m sq ft accounting for **48%** of all volume).

DELOITTE LONDON OFFICE CRANE SURVEY (WINTER 2020)

- Central London office take-up plummeted to 1 million sq ft in latest survey period – two-thirds down on the long-term average.
- Weaker pre-letting activity with only 0.9 million sq ft of space under construction committed to during the survey period (**41%** down on previous survey).
- TMT sector continues to drive office demand taking up **38%** of all pre-let space under construction. The sector is likely to emerge least affected by the pandemic.
- Appetite for serviced office providers has been affected by weaker demand but share of pre-let space under construction has actually risen from **12%** to **14%** as tenants take short-term space whilst assessing their accommodation needs or renegotiating lease extension terms with current landlords.
- Deloitte anticipates weaker tenant demand for office space will be a major obstacle to starting any new construction. The market is facing a 'state of suspension' as occupiers pause to reflect on their office plans.

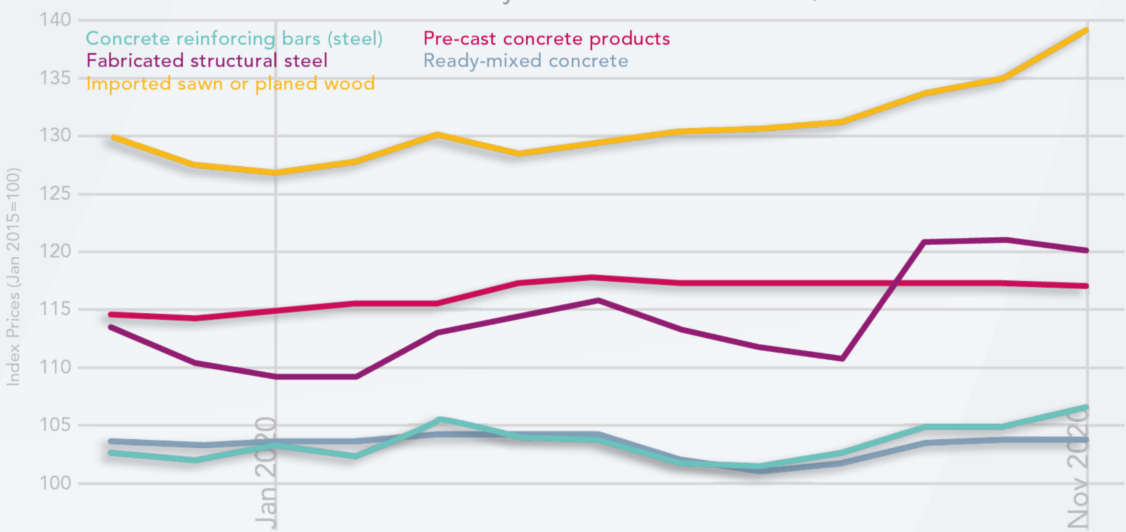
Percentage of pre-comletion space let by sector



Source: *Deloitte, Summer 2020 London Office Crane Survey*

- The ONS ‘All Work’ material price index rose by **3.1%** in the year to November 2020. After briefly falling in the summer months, the index rose sharply in the autumn.
- Shortages and supply issues helped push up prices as a whole in 2020. As site activity picked up in the second half of 2020 and demand outpaced supply, several key materials such as fabricated structural steel and imported timber experienced above-average cost inflation at **8.4%** and **5.8%** respectively in the three months to November 2020.
- Current material availability issues are largely COVID-related as factories close and re-open and container capacity is constrained.
- Low availability of finished products and raw materials led to suppliers increasing prices for goods in short supply and lengthening delivery times. The EU/UK trade deal prevented immediate price hikes at the border but the risk of supply chain disruption remains, putting upward pressure on prices.

Price Indices of Key Construction Materials, UK



Source: gov.uk

Construction Material Price Indices

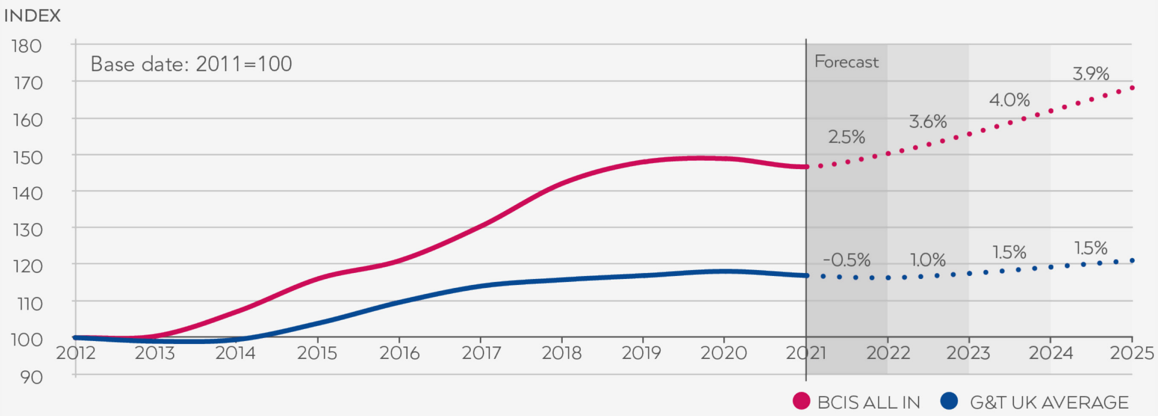
Month on Month October 20 - November 20		Year on Year November 19 - November 20
0.6%	New Housing	3.2%
0.3%	Other New Work	3.2%
1.0%	Repair & Maintenance	2.9%
0.4%	All Work	3.1%

Key Trade Analysis Likely 12-month inflationary range for key trade packages based on our Q1 2021 TPI Survey results

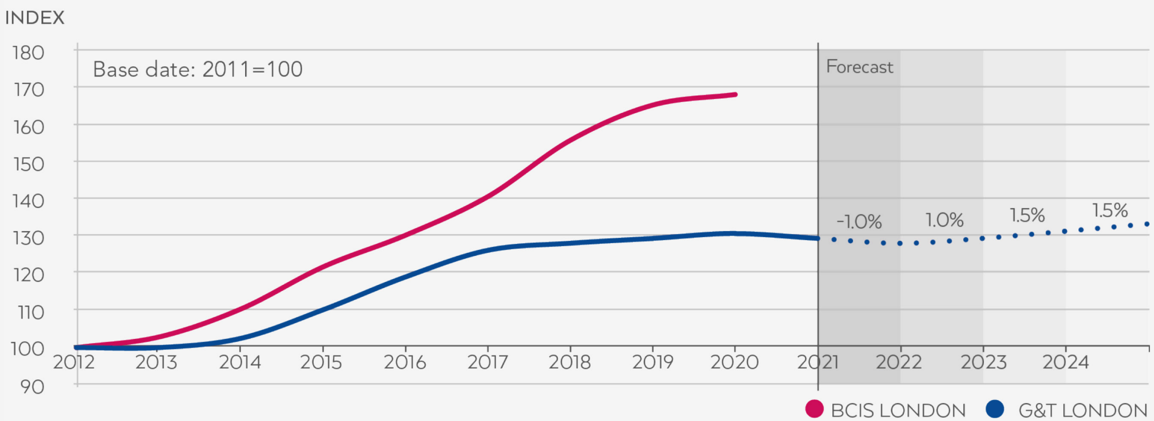
Key Trade Packages	Summary	Likely Inflation Range (Next 12 months)
Demolition	Although demolition is less exposed to the cost and productivity impacts stemming from adherence to Site Operating Procedures (SOP), early trades are often the most sensitive to lower workloads. We anticipate highly competitive tendering for demolition packages in early 2021 with pricing beginning to recover in Q2 and beyond.	**-5% to 0%**
Groundworks	Productivity levels remain strong but fewer new projects coming through will increase tendering competition on groundworks packages. Rising rebar prices are a concern but this could be offset by contractors looking to secure work.	**-2% to 0%**
Concrete	Ready-mixed concrete prices rose marginally (1.9%) in the three months to November 2020. Demand for concrete is recovering and will be boosted further by major infrastructure schemes in 2021. Bulk buying of concrete whilst supply is still constrained will drive up cost. Suppliers also remain keen to secure workload, resulting in competitive package pricing. Enquiry levels rose in H2 2020 but workloads were still down compared to pre-pandemic levels. Lead times remain at around 11 weeks.	**-1.5% to 0.5%**
Steel	With demand outweighing supply, steel prices skyrocketed from an average of £650 p/t in 2019 to £900 p/t at the end of 2020 affecting a number of different trades. Mill production slowed due to the pandemic and stocks were depleted. Resurgent demand and rising raw material costs (resulting from iron ore shortages) have also fed into higher prices, prompting contractors to warn that pre-tender quotes prices will have to rise as a result. Steel supplies are expected to catch up to demand in Q2 2021 but prices looks set to remain high and volatile in the meantime. On site, steelwork erection also continues to work significantly below normal productivity levels.	**-1% to 2%**
Facades	Supply pressure and increased cost of design, installation and materials creating uncertainty in the supply chain with bids being caveated. Speculation that some materials (eg aluminium) may increase by up to 10% in 2021. 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 are lengthening due to the closure of manufacturing facilities and suppliers increasing procurement periods. Contractors are still tendering hard with low conversion rates and pricing is fairly tight.	**0% to 2%**
Brick	Brick production and deliveries (both lead indicators of residential construction volumes) have returned to near pre-pandemic levels. Demand has recovered strongly and manufacturers have said that trading is stable with no impact on capacity under the current operating conditions. Lead times, workload and enquiries remain steady but labour availability due to COVID-19 and Brexit continues to be a concern.	**-1% to 1%**

Key Trade Packages	Summary	Likely Inflation Range (Next 12 months)
Dry lining	Shortages of skilled labour (more due to COVID-19 than Brexit) are supporting prices, particularly in residential. Costs are being pushed up by supplier stock shortages of plasterboard, plywood and insulation materials. Drylining lead times have been stretched with little-to-no manufacture of UK plasterboard but have since recovered. Rising steel costs are a concern for metal studs and lay in grids.	**-1% to 1%**
Carpentry	Demand for carpentry from the residential sector has returned and continues to stretch capacity. Imported sawn or planed wood prices rose by 7.1% in the year to November 2020 as a result of tighter supply globally and surging demand from renovation projects. Lumber prices soared in 2020 but sawmill supply is improving and expected to catch up with demand which may help soften prices in H2 2020. Labour costs remain relatively stable.	**-1% to 1%**
Joinery	Workload and enquiries are consistent and there are no issues with materials (other than the availability of veneers from Europe) or labour. No rise in lead times is anticipated.	**-1% to 1%**
Finishes	Social distancing measures impacting productivity while enquiries and workloads are rising.	**-1% to 1%**
M&E	Input costs (eg materials/key commodities, equipment and labour) all expected to rise in 2021. Copper, aluminium and steel prices are rising sharply and stock availability issues persist. Additionally, issues have been reported concerning availability of sprinklers, pumps and lighting from overseas (eg LED lights from China) contributing to increased lead times. Stock levels are not expected to be replenished until Q3 2021. Increased cost of steel will put upward cost pressure on MEP materials, particularly ductwork. Number of opportunities has stabilised but active pursuit of workload by MEP contractors is resulting in more competitive tenders, particularly in the commercial fit-out market. Size/value of projects are generally lower, increasing the number of tenderers and competition.	**-0.5% to 1.5%**
Roof	Although showing signs of improvement, shortages in roofing supplies and restrictions on labour have pushed lead times higher. A shortage of contractors/labour, as well as a volatile insulation market, continue to add upward cost pressure. Oil prices expected to rise in 2021, increasing the price of asphalt shingles and overhead cost pressure on roofing contractors.	**-1% to 1%**
Preliminaries	Compliance with SOP's and enhanced welfare provision on site continues to put upward pressure on preliminaries costs. However, upward cost pressure is being counteracted by a competitive market/desire to secure work, particularly with smaller contractors. It is expected that contractors will continue to be competitive with their direct costs in 2021 as they feel sustained pressure to price keenly and offer discounts to win work.	**Unchanged**
OH&P	Main contractor OH&P levels will largely depend on the firm, sector, project value and procurement route, but are generally expected to remain low in 2021. Tier 1 MCs working on larger schemes (under two-stage contracts) appear to be holding their pricing levels. However, lower tier contractors are tightening their bidding and reducing OH&P to secure order books. Overall, we expect OH&P to remain in the 3.5-5% range - below the pre-pandemic average of 5-6%.	**Unchanged**

*Tender Price Trend **"UK Average"** Q1 2021*



*Tender Price Trend **"London"** Q1 2021*



Note: BCIS does not publish regional TPI forecasts.

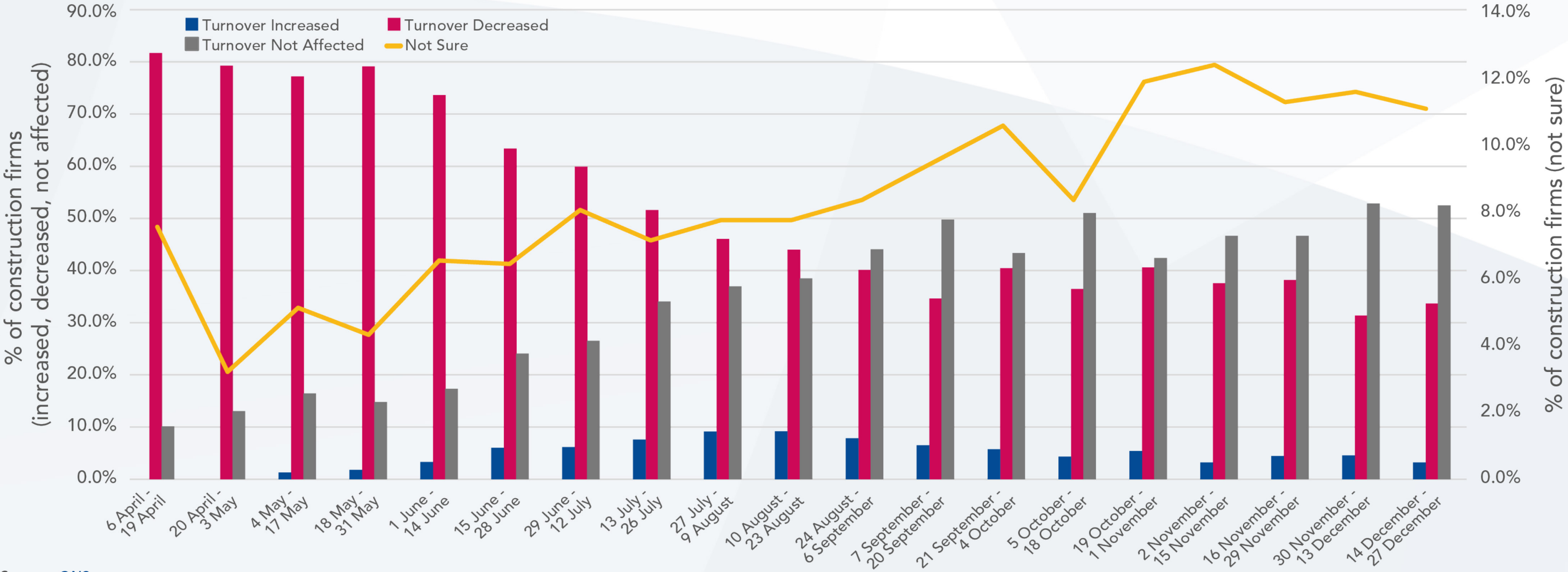
- Bumpy start to the year expected as businesses adjust to the new trading relationship and supply chains remain strained due to a slowdown in production from some factories in the EU.
- Early part of 2021 expected to be the bottom of the market, but tender pricing will remain keen in the short-term as clients cautiously hold back projects as they wait for the economy to begin to recover and normal levels of demand to return.
- We expect to see gradual inflationary rises towards long-term average levels of tender price inflation over the next two-to-three years.
- Tendering conditions will vary by sector in 2021. Healthcare, infrastructure and logistics sectors are likely to see above trend tender price inflation as capacity is limited. In other sectors, such as commercial and retail, contractors will be very keen to win work and market discounts will be prevalent.
- Two-tier tendering market with lower tier contractors more actively chasing a smaller pool of work and offering increased market discounts. Not uncommon to see tender returns 5-6% below the pre-tender estimate in H2 2020.
- Towards the end of 2020, some contractors were declining opportunities to tender on the expectation of increased tender activity in 2021 (and therefore the potential for higher pricing). Tier 1 contractors in particular were being very selective about taking on new projects.

- According to the ONS' fortnightly Business Insights and Impact on the UK Economy dataset, the number of construction firms reporting that their turnover was lower compared to what was normally expected for the time of year steadily decreased between 18th May-20th September 2020. However, uncertainty stemming from subsequent national lockdown restrictions may have acted to flatten the downward trend during the Autumn and Winter.

- Between 14th-27th December, over **52%** of surveyed construction firms said that turnover had not been affected by the pandemic. However, a substantial proportion (**33%**) said that turnover has lower than normal. Very few (**3.1%**) reported increased turnover.

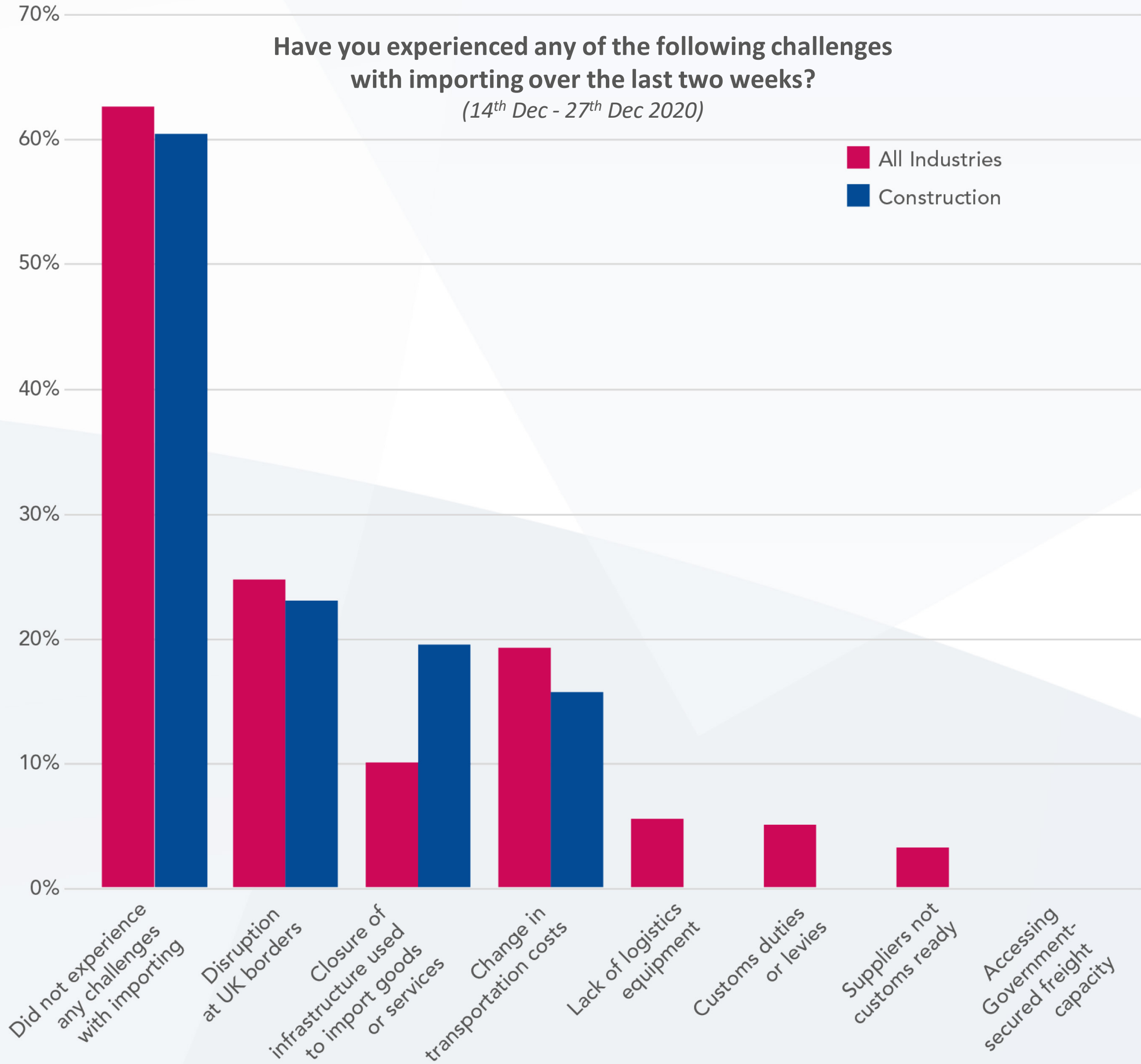
- A rising number of construction firms are also reporting that their business faces a 'severe' or 'moderate risk' of insolvency. At the end of the summer, around **10%** of surveyed businesses reported a severe or moderate risk of insolvency. By the end of 2020, this had grown to nearly **24%.**

In the last two weeks, how has the coronavirus (COVID-19) pandemic affected your business's turnover, compared to what is normally expected for this time of year?

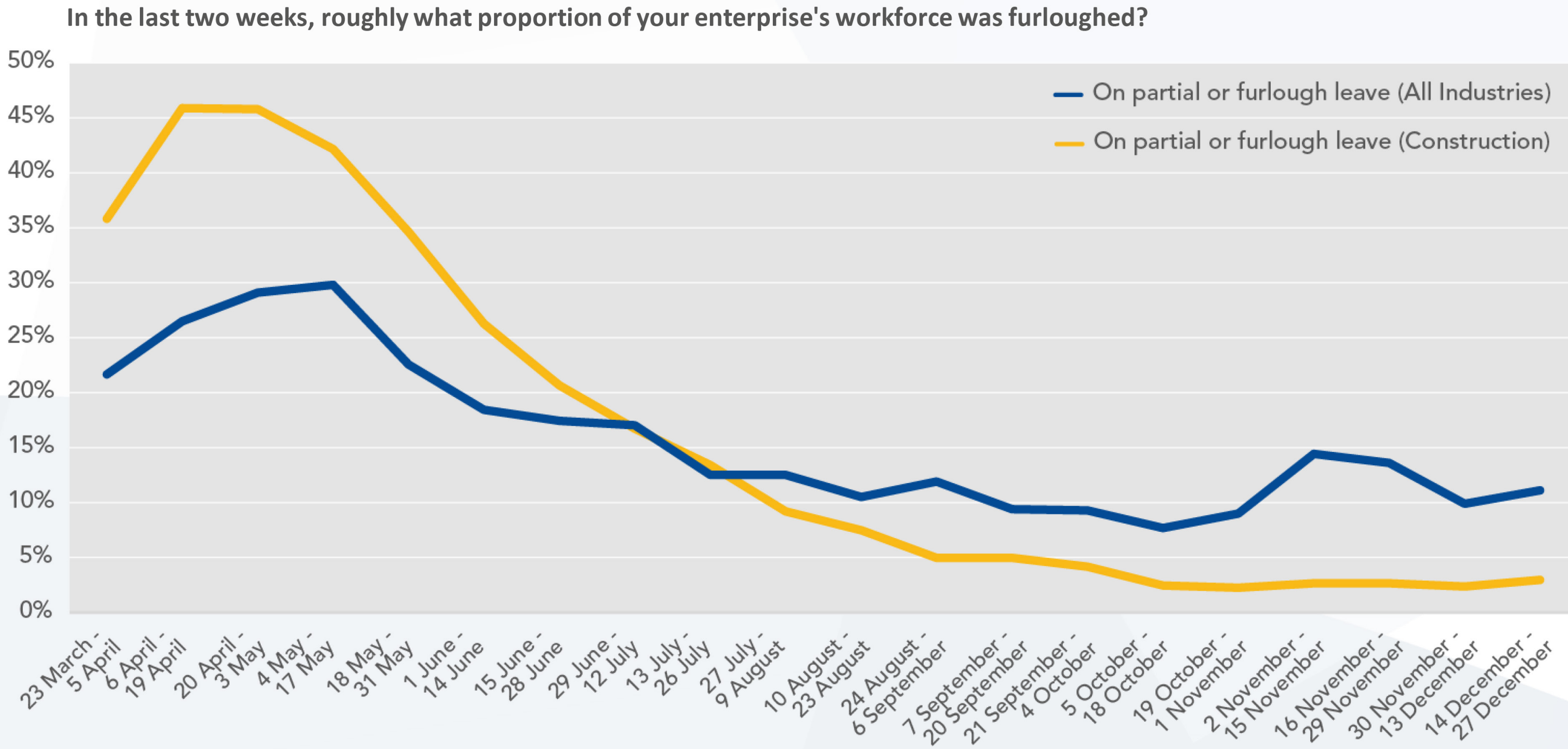


Source: ONS

- Between 14th – 27th December, most construction firms (**60.6%**) reported that they did not experience any challenges with importing.
- Nearly a quarter (**23%**) of construction firms said they experienced disruption at the border and a further **19.6%** indicated that the infrastructure used to import goods had closed (referring to the 48-hour closure of the borders between the UK and France for 'accompanied freight').
- Over **15%** of construction firms also said that a 'change in transportation costs' from importing was a challenge. Higher transportation costs were thought to have been caused by a spike in demand (front loading of orders/ stockpiling to avoid post-Brexit supply disruption), temporary border closures and disrupted container movement at ports since September resulting in logistical logjams.
- Most thought that these import challenges were mainly caused by a combination of the COVID-19 pandemic and the end of the EU transition period, but less than 1% of respondents said that the challenges caused 'severe' disruption to their businesses.



Source: ONS

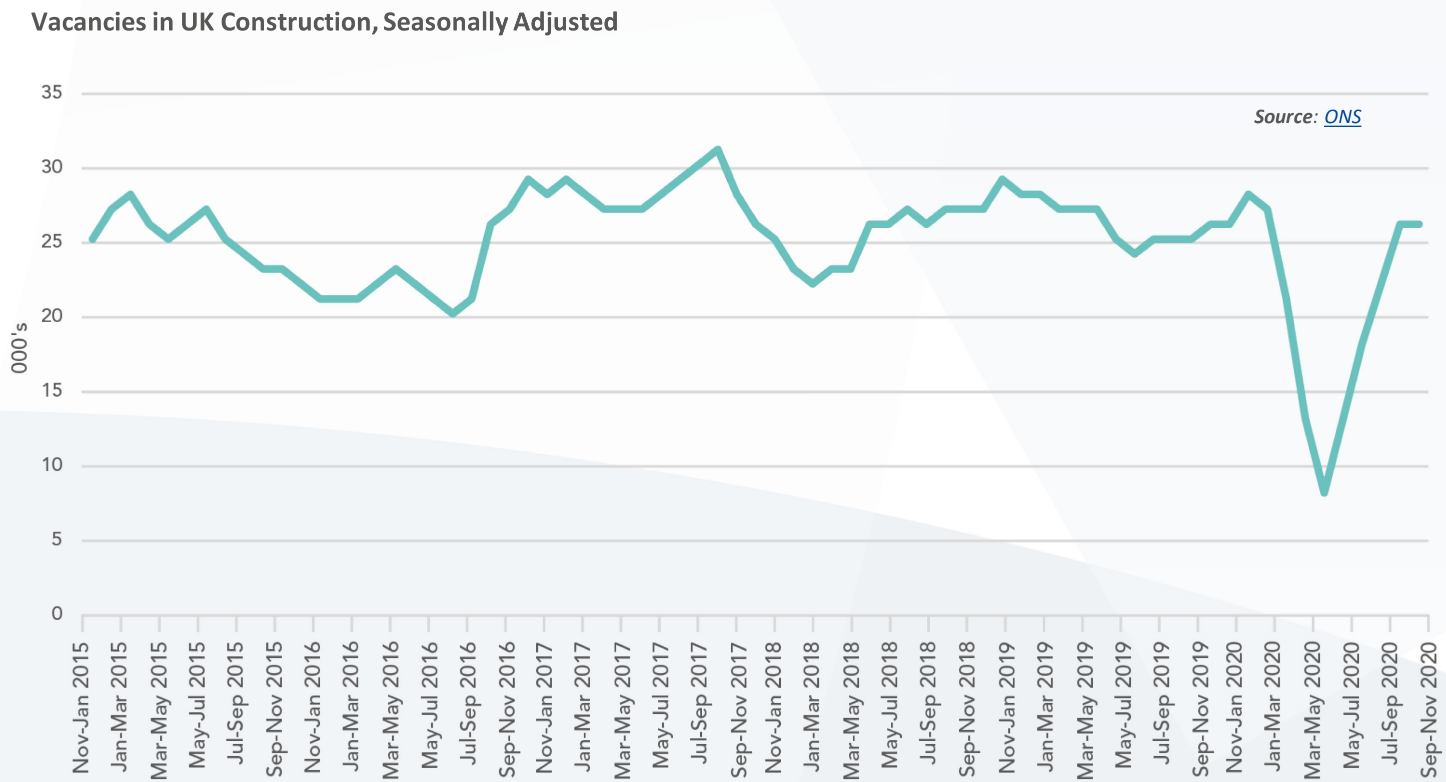


- According to the ONS, surveyed construction firms reported that, on average, the proportion of their workforce that were on furlough (or partial furlough) leave had fallen from a high of **45.7%** during 6th-19th April to just **3%** during 14th-27th December 2020.

- Since the end of July, UK construction firms reported that a lower proportion of their workforce were on furlough leave compared to the 'All Industries' sector classification.

- In construction, furloughing peaked on 14th April with 723,600 employments furloughed according to HMRC. By 31st October, employments furloughed had fallen to 130,700. This is likely to have fallen even further since then as a result of ongoing permission from the Government to keep sites open.

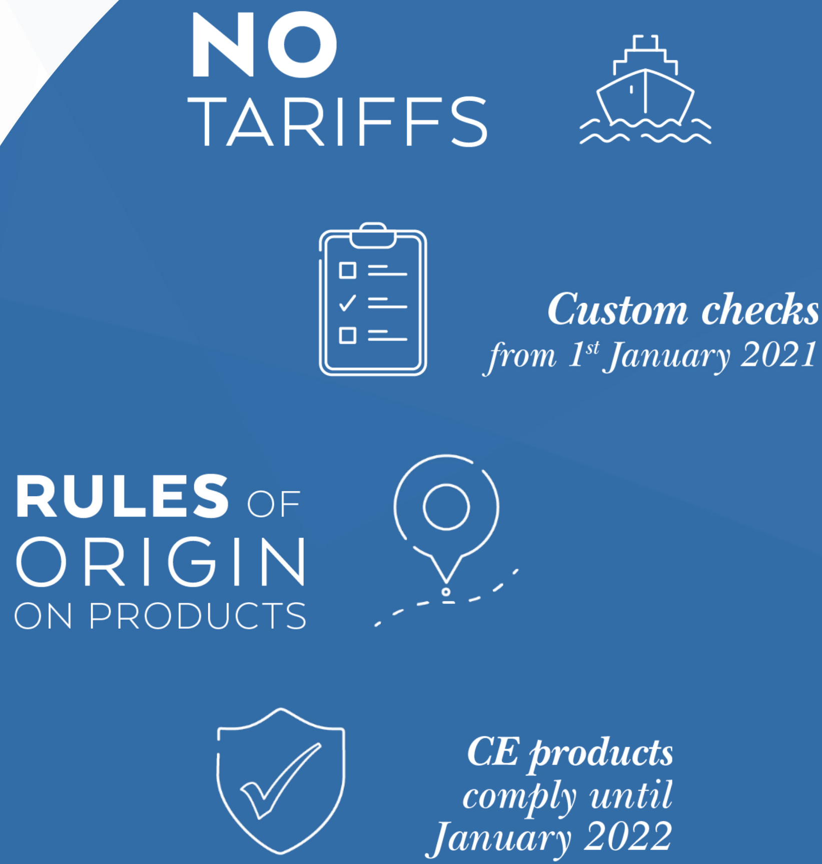
Source: ONS



- Construction vacancies in the three-month period between September-November 2020 were 26,000 - **7%** lower than the number of vacancies in the December-February 2020 period (just before the first national lockdown).
- Construction vacancies have experienced a sharp, ‘V-shaped’ recovery since late spring and are now more-or-less on par with pre-pandemic levels.
- The recovery coincides with seven consecutive periods of month-on-month growth in construction activity since June and a strong rise in new orders in Q3 2020. This has helped hiring demand to recover more quickly than other sectors of the UK economy and construction employment numbers return to growth in December.

Goods and Standards

- **Zero tariffs, quotas or customs duties** on goods imported from/exported to the EU.
- **Customs checks and controls** at borders from 1st January 2021 (although the UK has provided a transitional period until 1st July 2021 with extended deadlines for paperwork to be filed on imports to the UK).
- Traders will have to meet **'Rules of Origin'** on products and make declarations to that effect.
- Trade agreement aims to reduce **new administrative burdens and barriers** on traders where possible, including through mutual recognition of 'trusted trader' (AEO) schemes, providing a simplified/streamlined customs processes.
- **CE marked products** will still be allowed in the UK market until 1st January 2022, but the intention is to end recognition of the CE mark and introduce UKCA marking.
- Hopefully, UK Conformity Assessed (UKCA) marking will align closely to the CE marking system to ensure goods pass the equivalent CE standard without the need to carry out further testing. Otherwise, manufacturers' overheads may increase and choice of product may be reduced.
- **Additional cost and delays** involved in restrictions on product origin, double-certification and border checks will need to be factored into the pricing and programming of projects. This is likely to significantly impact 'just-in-time' procurement, slow down progression on projects and add cost.



Labour

- **Free movement ended** on 31st December 2020.
- **New global Points-based application system** excludes several roles such as general labourers and some plant operators.
- Applicants will need to:
    - Produce evidence of a job offer at the required skill level (RQF 3 or above/A-level or equivalent)
    - Meet new minimum salary threshold (£25,600, or the going rate for the role)
    - Speak English to the required standard
- Even if the relevant criteria are met (see here for full criteria), the **ongoing sponsorship costs** (£1,000 per skilled worker for the first 12 months and £500 for each subsequent six-month period) to bring workers to the UK will be prohibitive for some employers.
- **No mutual recognition of professional qualifications** under the trade deal. Architects, engineers and others holding UK professional qualifications will not be able to use that qualification to work in an EU member state and vice versa.
- However, the intention is for the **UK and the EU to agree mutual recognition arrangements** for the recognition of professional qualifications covering the UK and all 27 EU Member States.
- New system (along with job losses from COVID-19) may lead to **an increase in domestic construction labour** in the short-term. Longer term, we will continue to need access to foreign labour.

"The agreements reached will enable construction companies to continue to forecast the cost and availability of products and materials imported from the EU or comprising components made in the EU. "

-BCIS-

Public Procurement

- UK will maintain a **separate and independent procurement regime**.
- After 1st January 2021 contracting authorities will no longer be obliged to publish notices in the Official Journal of the European Union (**OJEU**). A new UK e-notification system, '**Find a Tender**' will be used.
- The trade deal provides for a framework of rules for trade in public procurement based on the WTO Government Procurement Agreement (**GPA**). GPA members commit to open up their public procurement markets to contractors from other member countries. As a result, **UK businesses will still be able to compete for public contracts across the EU**, although on a more limited basis than before.
- The **UK and EU have also agreed an extension of market access coverage beyond the GPA**, which includes: the gas and heat distribution sector, private utilities that act as a monopoly, and a range of additional services in the hospitality, telecoms, real estate, education and other business sectors. This will provide UK businesses with additional opportunities but will equally mean more competition for UK public sector contracts.

Market Update
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