GT GARDINER &THEOBALD

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TENDER PRICE **FORECAST**

for 1st Quarter 2024 is…

2.00%

Annual UK Average

▼ compared to 3.00% Annual UK Avg. for 2023

With market activity slowing in some sectors and deflationary pressures mounting, contractor pricing is expected to be more competitive in 2024. Although procurement conditions may become more favourable, interest rates and the high cost of debt remain a key pressure on viability. Pockets of the industry will remain busy, but signs point to an easing in the rate of tender price inflation in 2024.

KEY CONTACTS

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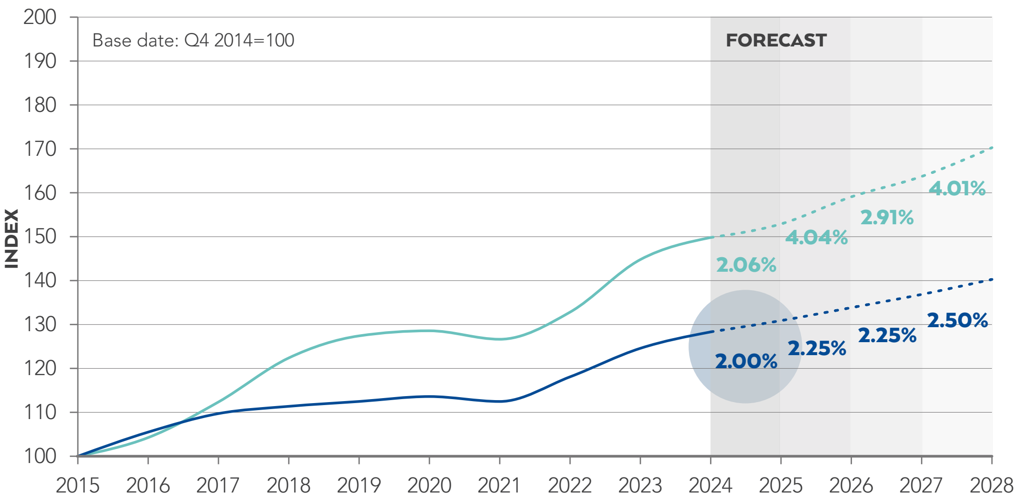
TENDER PRICE ANNUAL PERCENTAGE CHANGE Q1 2024

%	2024		2025		2026		2027	
Regional forecasts	**Now**	**Last***	**Now**	**Last***	**Now**	**Last***	**Now**	**Last***
Greater London	2.00	2.25	2.25	2.50	2.50	2.50	2.50	N/A
South East	2.00	2.25	2.25	2.50	2.50	2.50	2.50	N/A
South West	2.25	2.25	2.50	2.00	2.25	2.25	2.25	N/A
East (Anglia)	2.50	2.50	2.50	2.50	2.50	2.50	2.50	N/A
Midlands	2.00	2.00	2.00	2.00	2.00	2.25	2.00	N/A
Wales	2.00	2.25	2.00	2.50	2.25	2.50	2.50	N/A
Yorks & Humber	2.00	2.00	2.25	2.50	2.50	2.50	2.50	N/A
North West	2.00	2.00	2.00	2.50	2.00	2.50	2.50	N/A
North East	2.00	2.00	2.00	2.00	2.00	2.00	2.50	N/A
Scotland	2.75	2.50	2.50	2.50	2.25	2.25	2.25	N/A
Northern Ireland	2.25	2.25	2.00	2.00	2.50	2.50	2.50	N/A
UK Weighted Average	**2.00**	**2.25**	**2.25**	**2.25**	**2.25**	**2.50**	**2.50**	**N/A**

Last* **4Q 2023**

Our forward forecasts show annual tender price inflation (Jan-Dec)

TENDER PRICE TREND 'ALL UK TPI'



Our advice is to review each project on its own merits. This forecast publication must be treated as a guide only, being that it is based on averages of various types and sizes of projects across a region, ascertained through our latest market research.

HOW DO WE REACH OUR TENDER PRICE FORECAST?

We conduct a detailed industry survey and consider factors including…

INPUT COSTS

- ▲ 7.1% ● BCIS Labour Cost Index, Nov 22 – Nov 23
- ▼ -0.9% ● BCIS Plant Cost Index, Nov 22 – Nov 23
- ▲ 3.2% ● BCIS M&E Cost Index, Nov 22 – Nov 23
- ▼ -25.1% ● Fabricated Structural Steel, Oct 22 – Oct 23
- ▼ -24.8% ● Concrete Reinforcing Bars (Steel), Oct 22 – Oct 23
- ▼ -11.7% ● Imported Sawn or Planed Wood, Oct 22 – Oct 23
- ▲ 16.8% ● Ready Mixed Concrete, Oct 22 – Oct 23
- ▼ -7.6% ● Oil Prices (Brent Crude), Jan 23 – Jan 24

KEY

Input to tender price movement of a typical project has a range of contributory impacts from:

● *High Cost Driver* ● *Medium Cost Driver* ● *Low Cost Driver*

MACRO ECONOMICS

Unless otherwise indicated, figures show annual growth rates. Arrows indicate direction of movement over a one-year period.

- ▲ 0.3% UK GDP Annual Growth Rate, Q3 2022 – Q3 2023
- ▲ 3.9% CPI November 2023, 12-month rate
- ▲ 5.3% RPI November 2023, 12-month rate
- ◀▶ 5.25% UK Base Interest Rate, January 2024
- ◀▶ 4.3% UK Unemployment Rate, May 2023 - Jul 2023*
- ▲ 7.2% UK Wage Growth, Average Weekly Earnings (Total Pay), Y-on-Y three-month average to Oct 2023
- ▲ 4.0% UK Construction Wage Growth, Average Weekly Earnings (Total Pay), Y-on-Y three-month average to Oct 2023

* The ONS has not published updated unemployment figures due to issues with its Labour Force Survey).

GT

Our Tender Price Inflation report looks at the movement of prices in tenders for construction contracts in the UK. The report examines a number of contributing factors and is further informed by our market survey and supply chain consultations. This forward forecast illustrates our view of annual tender price inflation from January to December 2024 and beyond.

OUR FORECASTS

With market activity slowing in some sectors and deflationary pressures mounting, contractor pricing is expected to be more competitive in 2024. Although procurement conditions may become more favourable, interest rates and the high cost of debt remain a key pressure on viability.

Despite forecasts that workload, output and new orders will contract overall in 2024, the picture is more nuanced. Pockets of the industry will remain busy and some sectors are expected to buck the broader trend. Retrofit work and commercial refurbishments will continue to grow, supporting workloads, while residential new starts remain stalled and the sector subdued.

In a continuation of last year's emerging trend, all signs point to a further easing in the rate of tender price inflation in 2024. Key input cost pressures have eased following a rebalancing of supply and demand. Even labour, the key cost driver of 2023, is starting to normalise towards more typical inflationary growth. Although skills shortages remain in many specialist trades, contractor capacity has improved and vacancy levels have dipped, slowing earnings growth in the industry.

As we explore in this report, the market is still relatively busy delivering existing orders and workload commitments. Contractors are not yet being compelled to chase turnover. Input cost inflation has eased but labour-related elements and overhead costs are still putting upward pressure on tendering. The heightened risk of supply chain insolvencies will only increase risk aversion among contractors, leading to greater caution when pricing work and agreeing contract terms for profitable work.

We have lowered our previous tender price inflation forecast for 2024 from 2.25% to 2% following some minor adjustments to our regional forecasts. We subsequently anticipate a period of below-average annual inflationary rises, with G&T's cross-sector, UK average forecast remaining at 2.25% until the end of 2026.

All forecasts in this report take account of all sectors and project sizes as a statistical weighted average, indicating an overall trend in pricing levels. It should be remembered that individual projects may experience tender pricing above or below the published average rate, reflecting the project specific components and conditions.

THE ECONOMY

The UK economy shrank by 0.1% in the third quarter of last year, putting it on the cusp of a technical recession. Rising interest rates and elevated price levels weighed on consumer spending, which slowed over the period, impacting economic growth. However, the Office for Budget Responsibility, the Government's official economic forecaster, expects growth of 0.1% for the final three months of the year.

Forecasters expect the UK economy to grow by around 0.5% in both 2023 and 2024. We are entering a period of subdued economic growth, as was the case in 2023, however economists' downbeat outlook may turn out to be overly pessimistic.

Consumer prices rose by 3.9% in November – far lower than the 4.4% annual increase predicted by economists in a Reuters poll, and indicating inflation has fallen faster than expected. Unemployment data has also surprised many, not surging as predicted.

To a certain extent, the UK will remain at the mercy of global economic conditions and geopolitical events, but the shift towards calmer domestic waters could appeal to investors. The prospect of interest rates cuts could also improve the business environment and bolster near-term economic activity. The central bank kept the base rate on hold at 5.25% at December's meeting, explaining that monetary policy is "likely to need to be restrictive for an extended period of time." However, the latest slowdown in the rate of inflation has fuelled bets in financial markets that the Bank Rate could fall to as low as 3.75% by the end of 2024, with the first cut speculated to be in the late spring.

CONSTRUCTION OUTPUT AND NEW ORDERS

Construction output – a measure of the value of work being completed on site – has now grown for eight consecutive quarters on the back of post pandemic demand. The rate of growth has slowed in recent quarters due to the increasingly uncertain economic outlook, but managed to rise 0.1% in Q3, reaching a record quarterly high.

The Construction Products Association (**CPA**), in its latest set of industry forecasts, expect total output across all sectors to contract by 6.8% in 2023 compared to 2022 once official ONS figures have been released. A smaller contraction of 0.3% is forecasted for 2024, driven by slow economic growth hitting the industrial sector and pushing back a recovery in private housing new build and repair and maintenance & improvement. However, according to the CPA, fortunes across different sectors in 2024 will be mixed, with the potential for surprises to the upside if borrowing costs fall and economic growth prospects improve.

New order growth – a measure of the value and volume of new orders received by main contractors – ended its three-month losing streak and rose 3.9% in Q3. However, new orders can be a volatile series and the uptick is unlikely to mark the start of a sustained reversal to the recent downward trend.

Just one sector – Private Industrial – experienced a quarter-on-quarter contraction in Q3 last year (-7.8%), but there was zero growth in both the Commercial and Public Housing sectors, while the Private Housing sector only rose by 0.8% compared to the previous quarter. Infrastructure (+14.2%) and Public Other New Work (+23.7%) experienced the largest rises.

Although bottlenecks, cost pressures on site and supply shortages have eased in recent months, tougher borrowing conditions and access to credit are deterring some clients from committing to new projects. Others are progressing with projects in pre-construction phases, slowing down their progress until market conditions improve in their favour.

G&T TPI SURVEY FEEDBACK

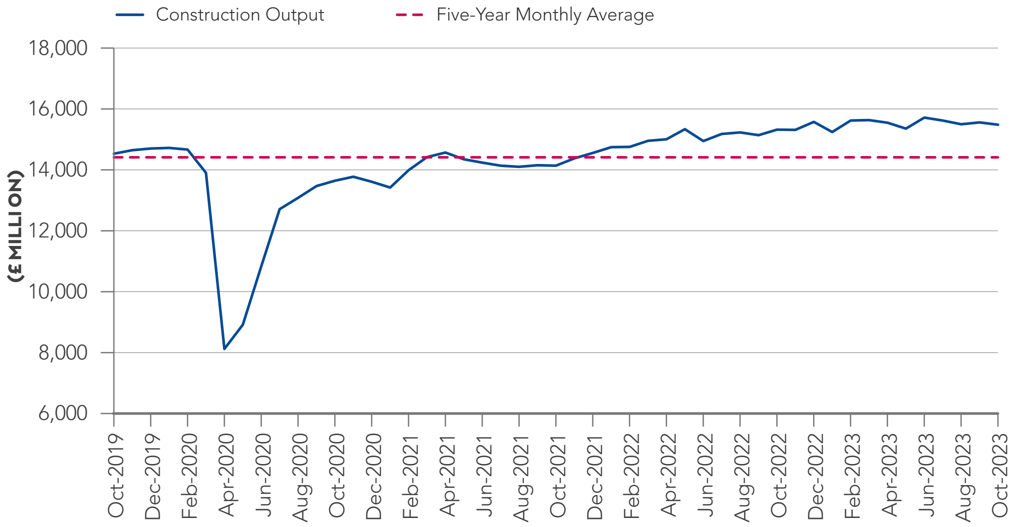
Workload

Based on our latest TPI survey, workloads are generally expected to remain consistent over the coming year, but the challenges of high interest rates, a volatile economy and a general election may impact market activity. While the residential market is slowing due to regulatory and viability challenges, activity in the commercial office sector remains buoyant and is showing few signs of slowing down.

Workloads in 2024 and beyond will largely be determined by the availability of funding and the viability results of feasibility studies. Some projects are unlikely to move forward into procurement whilst interest rates remain high. Clients will also want to see greater certainty on regulatory issues (eg regarding Gateways two and three of the Building Safety Act, the second staircase rule etc) before progressing schemes.

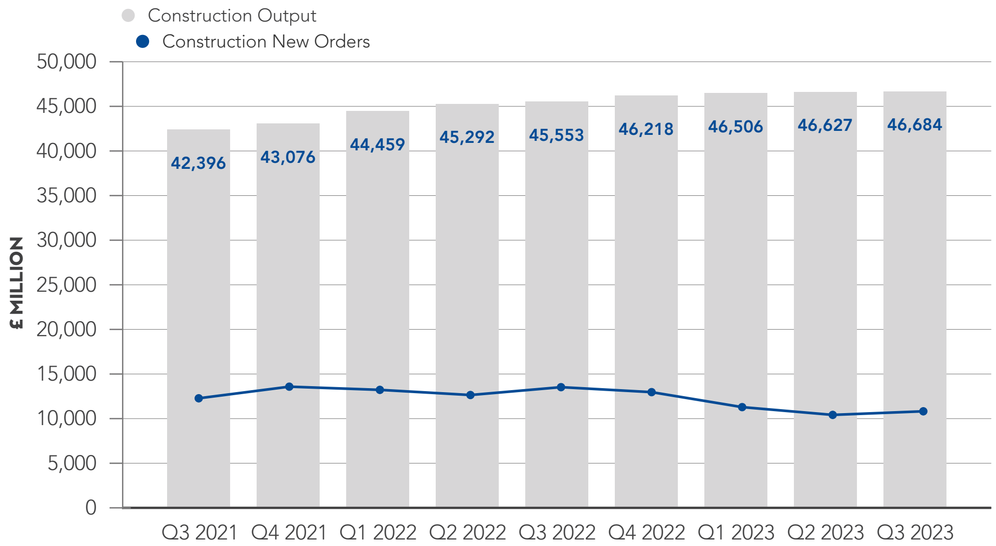
CONSTRUCTION OUTPUT: ALL WORK

Seasonally adjusted



Source: ONS

UK CONSTRUCTION: NEW ORDERS (ALL NEW WORK) V OUTPUT (ALL WORK)



Source: ONS

Market Conditions

Market conditions saw a notable shift in our previous (Q4 2023) TPI survey, with greater proportions of respondents expecting reduced market activity and greater tendering competition over the next six months. Sentiment has changed little in our latest (Q1 2024) survey.

Over a third of the respondents hold a neutral view on the current market conditions. However, a significant proportion (33.3%) anticipate that fewer tendering opportunities will lead to a slightly more competitive bidding environment.

The UK construction industry continues to grapple with uncertain demand, high construction and financing costs, as well as skilled labour shortages. However, the volatility experienced over the last year, largely due to extreme geo-political and economic factors, has eased. As stubborn material price inflation pressures receded in 2023, tender pricing started to cool and it is expected 2024 will see more modest levels of inflation.

The shortage of labour continues to be the primary driver of inflationary pressure, but this is likely to be counterbalanced by softer demand. The prospect of a general election towards the end of 2024, and potentially a new Government, could also weigh on demand in sectors where viability is finely balanced.

With the market still relatively busy with existing workloads, many contractors will focus on chasing profitable work rather than turnover in the short-term. However, with less new work coming through to tender, contractors in weaker growth sectors may start to become a little more competitive in 2024.

Prudent contractors will remain risk averse and price work carefully when faced with uncertainty. The high number of construction insolvencies is putting pressure on the supply chain. Recent high-profile administrations have elevated this to a key risk factor for contractors and project delivery. Contractors are acutely aware of these risks and are taking them into account when pricing their work.

For many, the immediate future will be one of slowing market activity and softer demand. However, a shrinking supply chain will reduce pressure on contractors to chase turnover. Those pockets of the industry that are expected to remain busy in 2024 (eg commercial fit-out and data centres) will invariably see less competitive pricing.

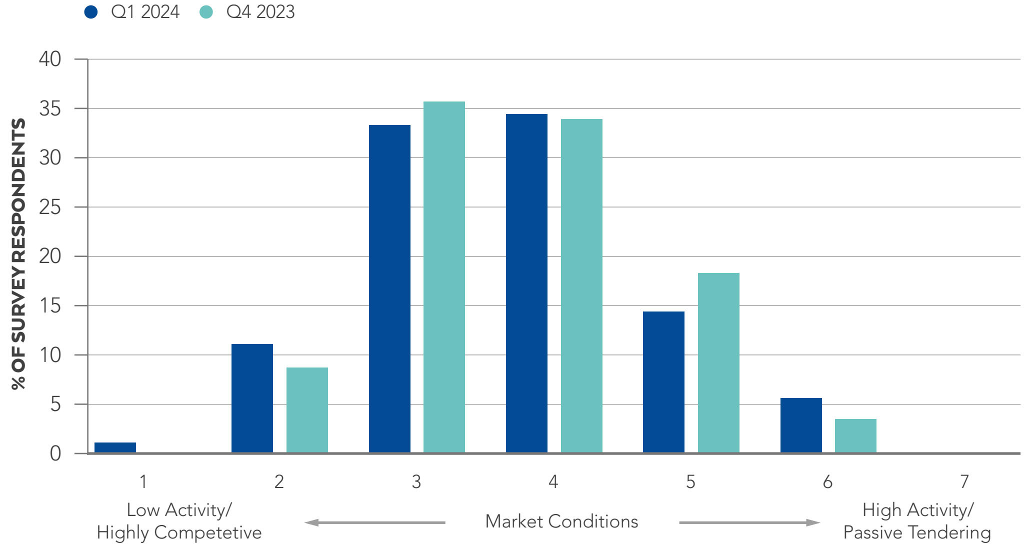
INPUT COSTS

Key Inflationary Drivers

Following COVID-19 and the war in Ukraine, double digit rises in materials prices in both 2021 (+19.8%) and 2022 (10.9%) drove the inflationary spiral. Relatively speaking, labour costs were a less important factor over this period, rising by 2% in 2021 and 4.8% in 2022. However, in 2023, the cost-of-living crisis, high demand and reduced contractor capacity meant that labour became the most prominent input cost driver, rising by 7.1%.

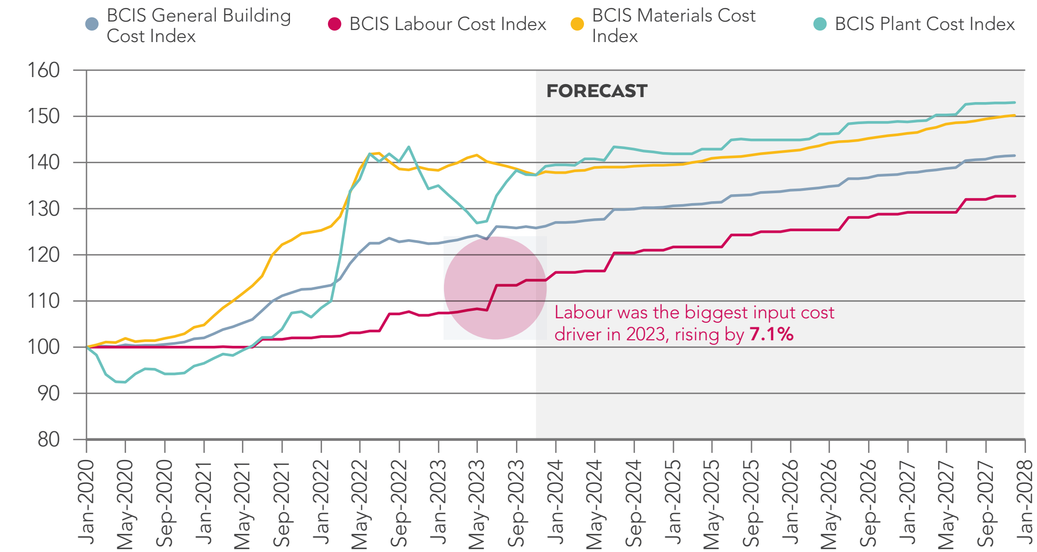
Still, wages in construction have not risen as much as previously feared. Indeed, construction earnings growth has lagged that of other sectors this year, while falling vacancy rates suggest that wage pressures will gradually recede in 2024. When considered alongside falling material prices, softer demand for construction projects and an increased appetite to win work, it is unsurprising that industry forecasters generally anticipate lower levels of tender price inflation in 2024 and beyond.

PERCEPTION OF MARKET CONDITIONS OVER THE NEXT SIX MONTHS (LONDON)



Source: *G&T Q1 2024 TPI Survery*

BCIS INPUT COSTS



Source: BCIS

Deflationary drivers are not likely to completely win out though. Above trend workload levels, a shrinking supply chain, labour pressures and contractor concerns about taking on too much risk will ensure tender price inflation continues to be positive for the foreseeable future.

Material Trends

Since July 2022, construction material price inflation has collectively stabilised and, for several materials, fallen significantly. Stagnating demand, lower wholesale energy prices and improvements in product availability following a series of supply chain disruptions have helped soften material prices.

According to the BEIS All-Work index – a basket of goods that tracks price movements for construction materials – prices in October 2023 were **2.6%** lower than they were one year ago. Additionally, October marked the fifth consecutive month-on-month contraction of the index.

The decline in the index was driven by a handful of key materials; namely structural steel, rebar, and imported timber – some of the most heavily inflated materials in 2021-2022. Prices for a small number of product categories are still experiencing marginal increases (eg insulation, concrete/cement and electrical components), but there has been a clear tapering off in the rate of inflation in recent months.

The slowdown in the speculative new-build sector caused a drop in demand for heavy materials such as steel, bricks and timber. This allowed manufacturers to rebuild inventory/ stock levels for these products, improving the supply-demand balance. This may generate short-term discounting and favourable buying windows but further hikes are still possible. Some suppliers have simply deferred scheduled price increases as demand has slowed, while ongoing volatility in the energy markets presents a significant upside risk to production costs and future price movements.

Labour Trends

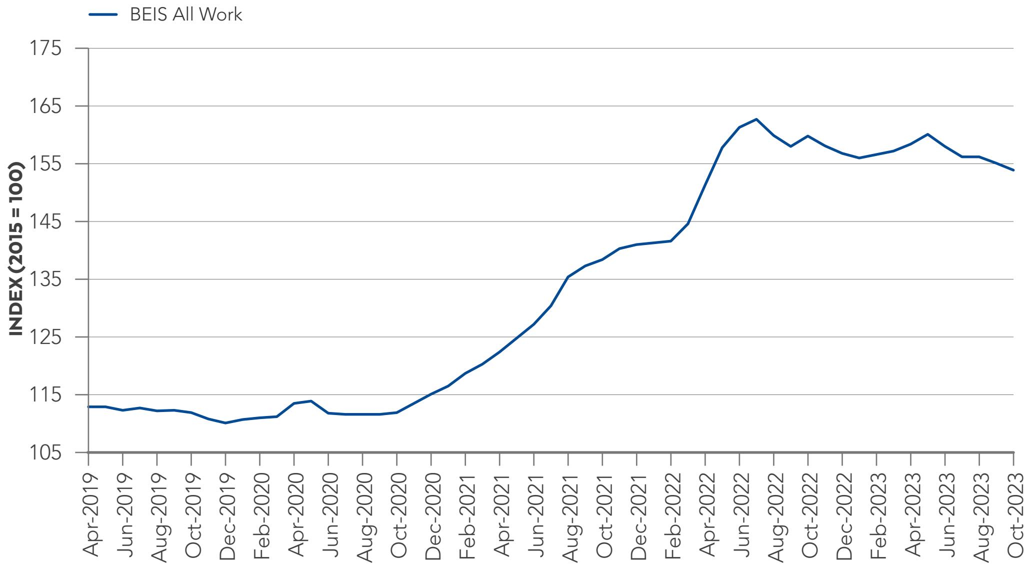
Weaker new order growth and uncertainty over the longer-term business outlook has limited appetite for additional hiring, dampening employment and recruitment activity over the past year.

According to ONS data, labour cost pressures have eased in recent months. In October 2023, average weekly construction earnings in the UK were 4% higher than a year ago (on a three-month average basis). Although still higher than the industry's long-term average annual growth rate of 3.1%, this represents a significant cooling and is far below earnings growth in the economy as a whole at 7.2%.

Construction workers have taken a larger pay cut in real terms compared to other sectors. Easing demand for construction activity and improved capacity have led industry vacancy levels to fall from their peak in Aug-Oct 2022. Lower consumer price inflation will also help to alleviate some of the pressure on earnings growth.

Against a background of falling new orders, the tight labour market may experience some relief. The latest earnings data offers some reassurance that wage growth has now passed its peak. However, we expect earnings will only ease gradually from here towards more typical growth, rather than seeing a substantial rebasing.

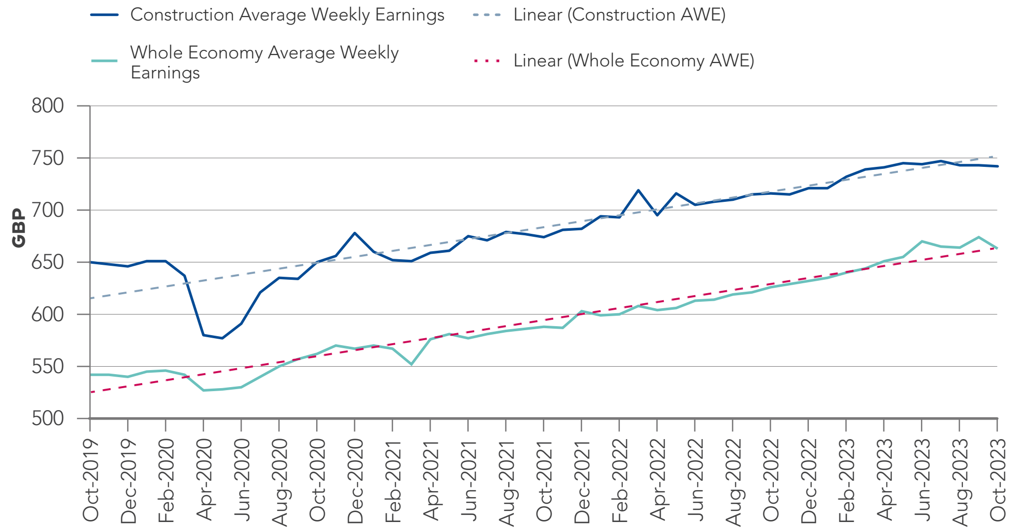
BEIS: 'ALL WORK' CONSTRUCTION MATERIAL PRICES INDEX, UK



Source: BEIS

AVERAGE WEEKLY EARNINGS (UK CONSTRUCTION)

Seasonally adjusted



Source: ONS

On-costs

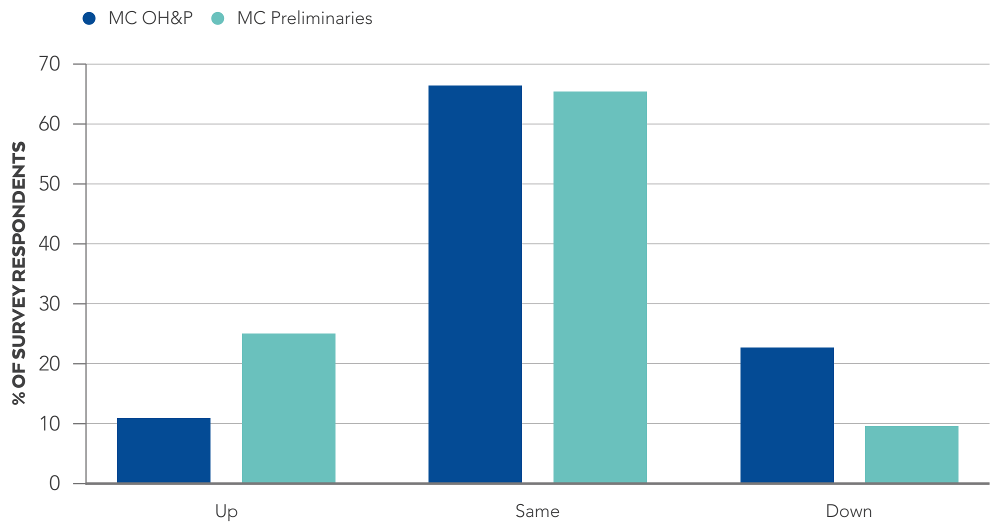
While Main Contractors are perhaps becoming keener to secure work, most respondents don’t expect to see any notable changes to preliminaries costs and overheads and profit (**OH&P**) over the next 12 months.

Staff and skilled management costs will continue to maintain or, as one third of survey respondents anticipate, increase preliminaries costs. Increased levels of tendering competitiveness will naturally drive a review of preliminaries, but with the current labour pressures, costs are unlikely to come down significantly until the second half of 2024.

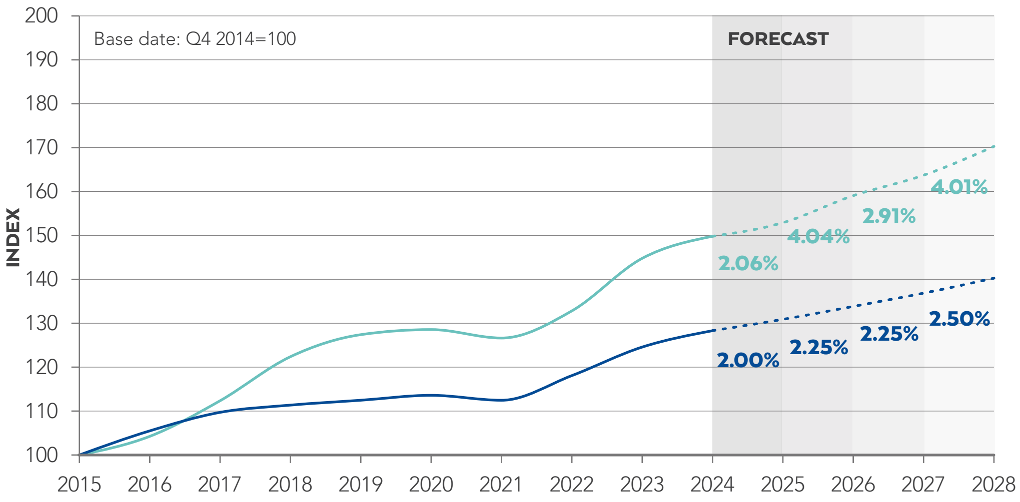
OH&P has remained broadly consistent over the past quarter as contractors have priced work prudently, with appropriate allowances for profit and risk. Over the next 12 months, if new orders continue to decline and construction activity stalls, contractors will have to compete more heavily on price and may lower their returns to secure work.

As contractors try and strike the balance between maintaining competitiveness and margin, the rising number of supply chain insolvencies is a significant risk. A return to aggressive competition on pricing, as is typical in market downturns, is therefore unlikely. Many contractors will naturally look to mitigate insolvency risk by building in higher risk allowance provisions and increasing on costs with the objective of maintaining a stable and successful business.

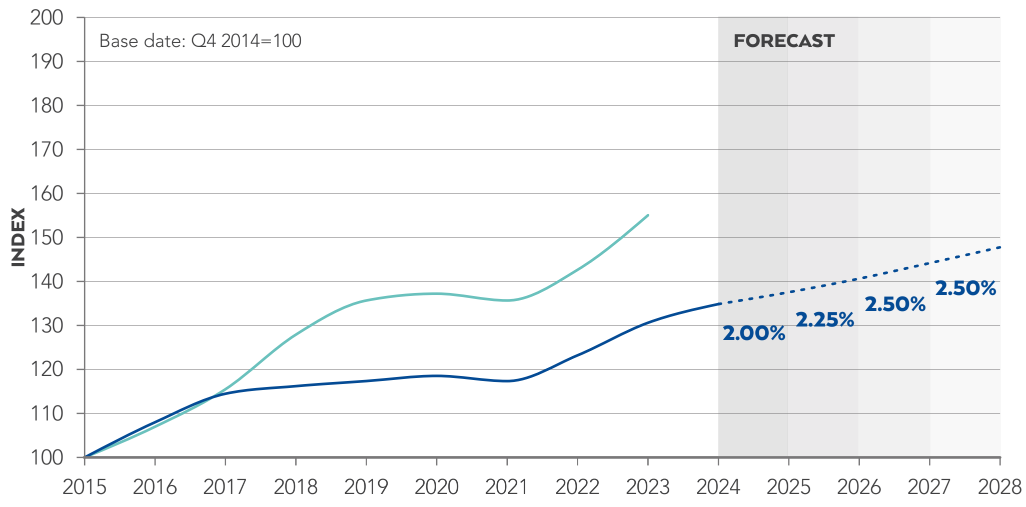
INFLATIONARY PREDICTION FOR MAIN CONTRACTOR OH&P AND PRELIMINARIES OVER THE NEXT 12 MONTHS



TENDER PRICE TREND 'ALL UK TPI'



TENDER PRICE TREND 'LONDON TPI'



Note: BCIS do not publish regional TPI forecasts.

TENDER PRICE ANNUAL PERCENTAGE CHANGE Q1 2024

%	2024		2025		2026		2027	
Regional forecasts	**Now**	**Last***	**Now**	**Last***	**Now**	**Last***	**Now**	**Last***
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Wales	2.00	2.25	2.00	2.50	2.25	2.50	2.50	N/A
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Northern Ireland	2.25	2.25	2.00	2.00	2.50	2.50	2.50	N/A
UK Average (weighted)	**2.00**	**2.25**	**2.25**	**2.25**	**2.25**	**2.50**	**2.50**	**N/A**

Last* **4Q 2023**

COMPARISON OF PUBLISHED FORECASTS FOR TENDER PRICE CHANGE

G&T UK AVER.	**BCIS** UK AVER.	**G&T** LONDON	**AECOM** UK	**ARCADIS** LONDON	
Q1 2024	Jan 2024	Q1 2024	Q4 2023	Winter 2023	
% CHANGE					
2.00	2.06	2.00	3.00	2.00	**2024**
2.25	4.04	2.25	3.00	1.00 - 2.00	**2025**
2.25	2.91	2.50	N/A	3.00 - 4.00	**2026**
2.50	4.01	2.50	N/A	4.00	**2027**
N/A	2.95	N/A	N/A	4.00	**2028**

Note: Arcadis' TPI figures are for its 'London Building Construction TPI' series.
Aecom's baseine forecasts are from Q4 2023 to Q4 2024 and Q4 2024 to Q4 2025

Our advice is to review each project on its own merits. This forecast publication must be treated as a guide only, being that it is based on averages of various types and sizes of projects across a region, ascertained through our latest market research. The quality, both of design and desired end product, procurement route (particularly ownership and transfer risk), delivery timescales, complexity of design and desire of contractors to tender should be carefully considered in project specific estimates and their outturn cost. Suitable allowances should be made for project specific designs, site conditions and local market conditions, which should be reviewed regularly with your Gardiner & Theobald team to determine the appropriate base cost.