

Construction Market Review and Forecast: Monthly Summary

September 2014

Prepared by Glenigan





A 4C Service

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This report is a monthly summary of our full Construction Market Review and Forecast report produced quarterly. The full report is available to purchase for £595 (ex. VAT).

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Summer slowdown hits non-residential starts

The growth in the value of the Glenigan index is beginning to stall as public sector work declines and a dip in office projects emerges. In the three months to August 2014, the Glenigan index was just 2% higher than at the same point a year ago.

The growth in the index has been held back by weak activity in the public and office sectors. Glenigan's non-residential index crept up just 2%, as an earlier strong run of rises in the underlying value of new office projects was capped this summer.

Table 1: Underlying construction starts and planning approvals

| | Planning Approvals (£ millions) | Planning Approvals (Change yoy) | Project Starts (£ millions) | Project Starts (Change yoy) |
|---------------------|---------------------------------|---------------------------------|-----------------------------|-----------------------------|
| Private Housing | 3,860 | 43% | 2,680 | 11% |
| Social Housing | 610 | -27% | 1,459 | -13% |
| Industrial | 1,195 | 30% | 778 | 27% |
| Offices | 936 | 70% | 617 | -23% |
| Retail | 643 | -3% | 547 | 29% |
| Hotel & Leisure | 821 | 17% | 812 | 18% |
| Education | 1,243 | 27% | 1,557 | -9% |
| Health | 738 | 82% | 509 | 6% |
| Community & Amenity | 122 | -39% | 319 | 9% |
| Infrastructure | 298 | 5% | 1,000 | 1% |
| Utilities | 677 | -20% | 789 | 2% |

Note: Starts and Planning Approvals - 3 months to August 2014, yoy – year-on-year. **Source:** Glenigan

Key Points

- In contrast construction activity was at its strongest level for seven months during August according to the latest purchasing managers' index from Markit and the Chartered Institute of Purchasing & Supply. The rise in output was one of the sharpest since 2007 but the CIPS warned about the potential impact on further growth of skills shortages as the strain on supplier capacity grew in August.
- The number of private residential units proposed in planning applications submitted in the year months to Q2 2014 rose by at least a double digit percentage rate in 10 out of the 12 economic regions in the UK according to Glenigan. Only one region, the East of England, recorded a significant fall in proposals for new homes entering the planning system.
- Office of National Statistics figures for Q2 2014 show no growth in construction output against the preceding three-month period but a rise of 4.8% in comparison with the same quarter a year earlier. In June 2014, output was up 5.3% on the same month a year ago with increases in both new work and repair & maintenance of 5.4% and 5.0% respectively.



Source: Glenigan

Regions



Northern English construction catching up fast

Over the past year, the underlying value of construction starts has grown in every region of the United Kingdom. Although over the latest quarter to August 2014, the value of project starts is down in the East of England, London and Scotland, on an annual basis every UK region shows a rise.

In the East of England, project starts are up 13% annually and by 7% in Scotland. In London, private residential work continues to buoy workloads and the value of starts in the year to August 2014 has risen by 17%. There is also a rise of 15% in the neighbouring South East, which along with London, has experienced the largest amount of project starts by value over the past year.

On a quarterly basis, Yorkshire & the Humber experienced the largest annual rise with an increase of

82%. Over the past 12 months, the value of projects rose 28% in the region and by 20% in the North East, which is the next fastest growing region.

The biggest annual rise in construction workloads is outside Britain. The turnaround in Northern Irish construction work continues. Glenigan's research shows in that in the year to August 2014, the underlying value of project starts was up by 38%. This was the largest increase in any of the 12 economic regions of the United Kingdom, but is from an exceptionally low base.

The most recent data from Northern Ireland's Department of Finance & Personnel on construction output dates back to Q1 2014 and this does not yet reflect this recent rise, but Glenigan's planning data suggests that private residential work is also resurgent in Ulster too.

Table 2: Underlying construction starts and planning approvals

| | Planning Approvals (£ millions) | Planning Approvals (Change yoy) | Project Starts (£ millions) | Project Start (Change yoy) |
|------------------------|---------------------------------|---------------------------------|-----------------------------|----------------------------|
| East Midlands | 975 | 9% | 786 | -16% |
| East of England | 672 | -5% | 660 | 2% |
| London | 1,804 | 57% | 1,931 | -12% |
| North East | 365 | 38% | 457 | 51% |
| Northern Ireland | 1,078 | -9% | 1,042 | 13% |
| North West | 398 | 44% | 215 | 36% |
| South East | 819 | -2% | 1,054 | -20% |
| South West | 1,682 | 38% | 1,671 | 5% |
| Scotland | 912 | -6% | 1,182 | 1% |
| West Midlands | 545 | 116% | 402 | 27% |
| Wales | 1,042 | 53% | 811 | -1% |
| Yorkshire & the Humber | 852 | -14% | 857 | 82% |

Note: Starts and Planning Approvals - 3 months to August 2014, yoy – year-on-year. **Source:** Glenigan

For more detailed regional data and analysis, please consult our website.

Sectors



Private Housing

Private residential work continues to expand at a strong rate with Glenigan's index showing an annual 18% rise in the value of work starting on site in the year to August 2014 and an 11% in the last quarter. Only industrial work has grown more over the past year, and then from a very low base.

The private residential boom looks likely to continue as Glenigan's research also shows that there has been a major upswing in the level of planning applications for private residential schemes over the past year.

Glenigan's data shows that planning applications to build 114,875 units were submitted by private housebuilders in the year to Q2 2014. This is an overall rise of 47% on the preceding 12 months. Although London and the South East have experienced the largest level of project starts by value, the rest of the UK looks likely to experience the next flow of work.

Ten of the dozen regions experienced a major rise in the number of units being proposed through the planning

system over the past 12 months. That increase illustrates a groundswell of support for private housebuilding that has seen the North West over-take the South East as the region experiencing the largest number of new homes proposed in the latest planning pipeline.

The only parts of the UK to record a decline was Wales, where the drop was marginal, and the east of England, where the planning pipeline shrank 15% against a strong total a year ago.

All the major privately-owned housebuilders are planning significant expansion and this rise in submissions has been driven as much by the major housebuilders as by an increase in the number of applications being submitted.

In the year to Q2 2013, 1,297 planning applications for private housing schemes of 10 or more units were submitted according to Glenigan's research; in the most recent 12 month period, that figure had surged to 1,614.

Community & Amenity

The underlying value of community & amenity project starts over the year to August 2014 was the second lowest of the 10 sectors covered by Glenigan, rising just 7%. Only health experienced worse growth.

In the most recent quarter, there was a 9% rise in project starts but the value of work in the pipeline over the last quarter fell 39% on a year ago. The prospect of any increase appears to be fast diminishing as local authorities, a key driver of work in this sector, are under more budgetary pressure than ever.

Research from the Chartered Institute of Public Finance & Accountancy (CIPF&A) shows that local authorities are struggling to cope with budget cuts of almost a third over the last five years. Councils' spending per head of population will have fallen by nearly 30% in real terms over the course of this parliament according to the CIPF&A, as spending on housing, leisure services, libraries and roads are all dramatically reduced.

Spending on housing saw the biggest fall over in the past year, dropping 7.8% between 2013/14 and 2014/15. Culture expenditure fell by 6.3% and spending on highways and transport fell by 6.2% in the same period. Not all of this spending is on capital works. In addition some areas fall under other sectors, such as roads which comes under civil engineering, but there can be no doubt about the pressure that councils are under when commissioning major construction work.

The CIPF&A's analysis claims that councils' total spending on services will fall by three times more in this financial year than during 2013/4 with a drop of 3.1% in 2014/15 after a 1% fall in the previous year.

In response to these cuts, a Local Government Association survey suggests that 22% of councils took money from building programmes to help cover a 'black hole' in school funding estimated by the LGA to total £1 billion.

Sectors



Industrial

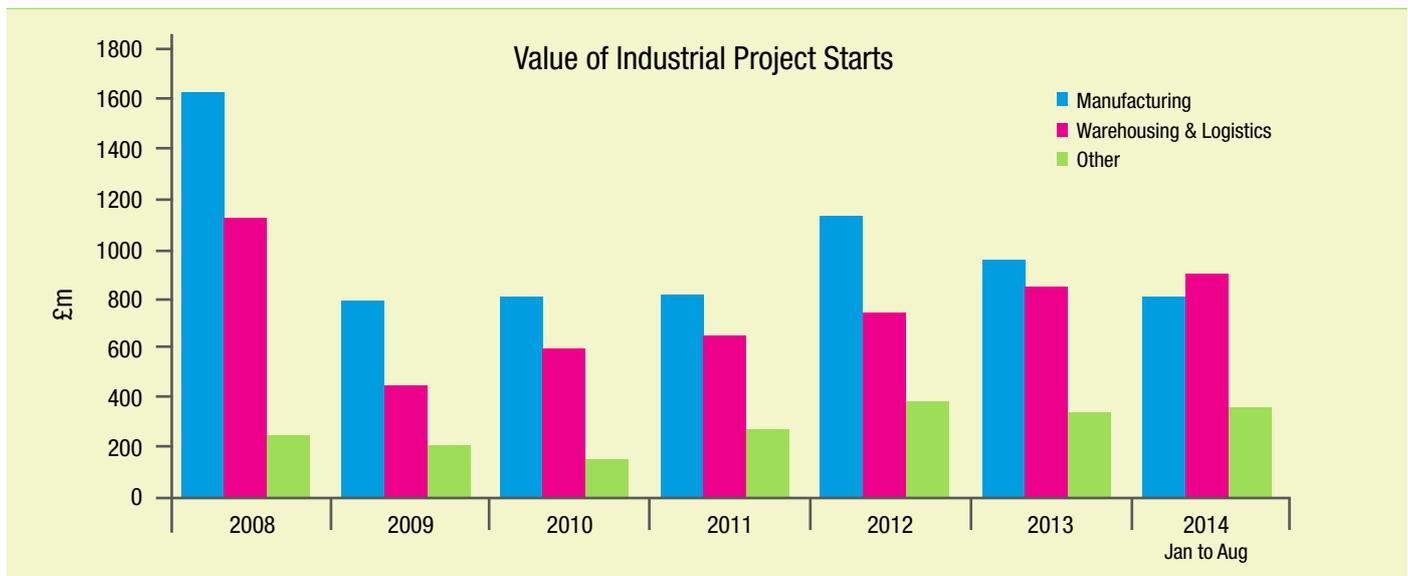
After years of lack of investment, workloads in the industrial sector are beginning to boom as retailers shift investment from the high street and public facing stores and into distribution hubs.

In the year to August 2014, the underlying value of industrial project starts ballooned by 53%. Of the 10 sectors tracked by Glenigan, this was by some distance the biggest increase. In the three months to August 2014, the underlying value of project starts in this sector leapt 27%. This surge in industrial workload is reflected on the latest, but slightly more historic, figures on private industrial output from the Office of National Statistics. The ONS data shows that private industrial output in the three months to Q2 2014 was up by 16.7% compared to the same period a year

earlier and by 9.6% on the preceding three-month period to Q1 2014.

The ONS notes: “The growth in private industrial work on the year, quarter and month, is on the face of it, substantial. However, the weight of private industrial work in all construction is small (3%) and thus does not contribute much towards the overall performance of the construction sector.”

However, with the major retailers increasingly cutting capital spend in favour of building distribution hubs for online retailing and, more recently in building ‘dark stores’ where the public can collect shopping, this sector’s proportion of overall construction output and activity looks likely to continue to increase.



Note: Underlying projects - excludes projects with a construction value of £100m or more. **Source:** Glenigan

Hotel & Leisure

In the year to August 2014, the underlying value of project starts in the hotel and leisure sector rose by 15% according to Glenigan. In the latest three months to August 2014, there was an increase of 18% on the same period a year earlier.

The value of hotel & leisure work in the planning pipeline in the three months to August 2014 rose 17%, but this remains a relatively small sector. With no major client such as a government department or an external stimulus to drive hotel upgrades such as an Olympic Games or other

mega-event, work is reliant on the seven-year cycle of hotel room upgrades.

Outside of the hotel sector, local authority clients are increasingly cutting back on work as the Chartered Institute of Public Finance & Accountancy (CIPF&A) research shows. What little local authority work there is will be tied up with private sector partnerships funded through the sale of public sector assets, or acting as a guarantor/joint client on mixed-use developments that will ensure the underlying value of project starts in this sector is prone to spikes and dips.

Sectors



Retail

The decision by ailing supermarket giant Tesco to reduce capital spending looks set to have a major impact on the underlying value of project starts in this sector. Britain's largest grocery chain issued a profit warning in eight months in August and also informed the City that overall capital expenditure will be 'no more than £2.1 billion' in the current financial year.

This figure is £0.4 billion less than anticipated and down from £2.7 billion in the preceding financial year. There will clearly be a knock-on effect in terms of the underlying value of project starts going forward as Glenigan's data shows that in the year to March 2014, Tesco was the only grocery chain to increase spending on construction starts.

Over the past year, retail spending on construction work has held up well compared to the other nine construction sectors tracked by Glenigan on an annual basis. In the three months to August 2014, the underlying value of retail project starts did rise 29%. Year-on-year the underlying value of project starts in the 12 months to August 2014 is up 18%.

This level of growth has been equalled by the private residential and civil engineering sectors but only outstripped by industrial project starts. The industrial sector has been buoyed by retailers spending more money on distribution hubs, but overall capital spending by retailers is diminishing; in particular construction spending on stores.

Retail Project Starts

| | 2010 | 2011 | 2012 | 2013 | 2014 ytd* |
|------------------------|------|------|------|------|-----------|
| East Midlands | 122 | 95 | 133 | 93 | 155 |
| East of England | 123 | 138 | 150 | 192 | 95 |
| London | 85 | 124 | 225 | 289 | 279 |
| North East | 69 | 113 | 166 | 104 | 19 |
| Northern Ireland | 38 | 41 | 22 | 14 | 68 |
| North West | 294 | 341 | 278 | 163 | 166 |
| South East | 133 | 251 | 409 | 209 | 189 |
| South West | 148 | 188 | 129 | 240 | 69 |
| Scotland | 143 | 226 | 109 | 192 | 81 |
| West Midlands | 151 | 165 | 323 | 336 | 84 |
| Wales | 70 | 108 | 69 | 77 | 105 |
| Yorkshire & the Humber | 124 | 137 | 120 | 208 | 81 |

*August 2014 **N.B.** Excludes projects with a construction value of £100 million or more

Offices

In the year to August 2014, the underlying value of office construction starts rose by 13% according to Glenigan but in the three months to August 2014, there was a 23% fall.

Office of National Statistics data on private sector commercial new-build work shows some improvement in the three months to Q2 2014 against the same quarter a year earlier with output edging up 0.5%, although compared to the preceding quarter

the ONS statistics show a 4.3% drop in new-build output.

However, the latest state of trade survey from the Construction Products Association suggests a better picture going forward. According to the CPA, the private commercial sector enjoyed a significant rise in activity in Q2 2014 with 37% of contractors reporting that commercial output rose in Q2 compared with a year ago.

Sectors



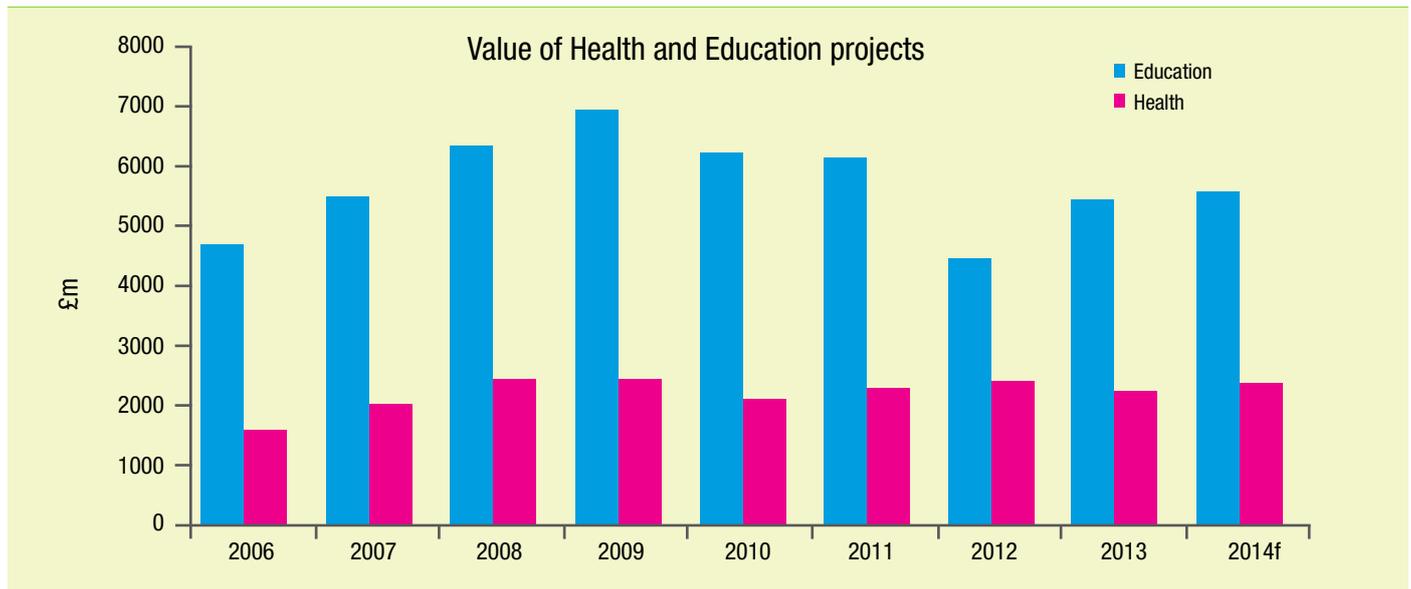
Health

Health construction growth ground to a halt this summer. Glenigan’s research shows that in the year to August 2014, the underlying value of project starts was completely static on a year ago.

In all the other nine construction sectors tracked by Glenigan on an annual basis, there was an increase. Only in health was there no growth. In the quarter to August 2014, there was a 6% rise but the prospects for any sustained recovery in workloads in this sector do not look promising.

In their latest statistical release covering the more historic year to Q2 2014, the Office of National Statistics noted that: “those sub-components of construction that are not consumer facing have performed less strongly.”

While this covers other sectors where the bulk of funding comes from the private sector, this is particularly apposite for the health sector. Over all new work in the year to Q2 2014 is down 19.2% on its pre-downturn peak in Q1 2008.



Note: Underlying projects - excludes projects with a construction value of £100m or more. **Source:** Glenigan

Education

In the latest state of trade survey from the Construction Products Association covering Q2 2014, 46% of building contractors reported that work in publicly-funded education and health construction saw a return to growth.

The CPA says this reflects the recovery in capital investment during 2014/15 and suggests this is politically motivated by noting that there is ‘less than a year to go to the next election.’ Glenigan’s information suggests education is more likely to experience this stimulus but in the three months to August 2014 the underlying value of project starts in this sector fell 9%.

In the year to August 2014, the underlying value of education project did rise 9% but of the 10 sectors tracked by Glenigan, only community & amenity and health have experienced lower growth over the past year.

This sector has been helped to some degree by local authorities diverting funds from other areas in order to enable schools to meet targets on supplying school places, but the state of public sector spending is having some impact. Office of National Statistics on public sector new-build work in the three months to Q2 2014 shows a 2.6% drop on the same stage a year ago. The fall compared to the preceding three months to Q1 2014 is less marked at 0.2%.

The ONS data suggests that more public sector work is being directed to repair and maintenance work, where the Q2 2014 year-on-year fall was just 0.7%, although the fall on the preceding quarter was slightly larger at 1.3%. This illustrates the underlying lack of investment in the public sector as a whole as belts may have been loosened slightly but remain tight.

Sectors



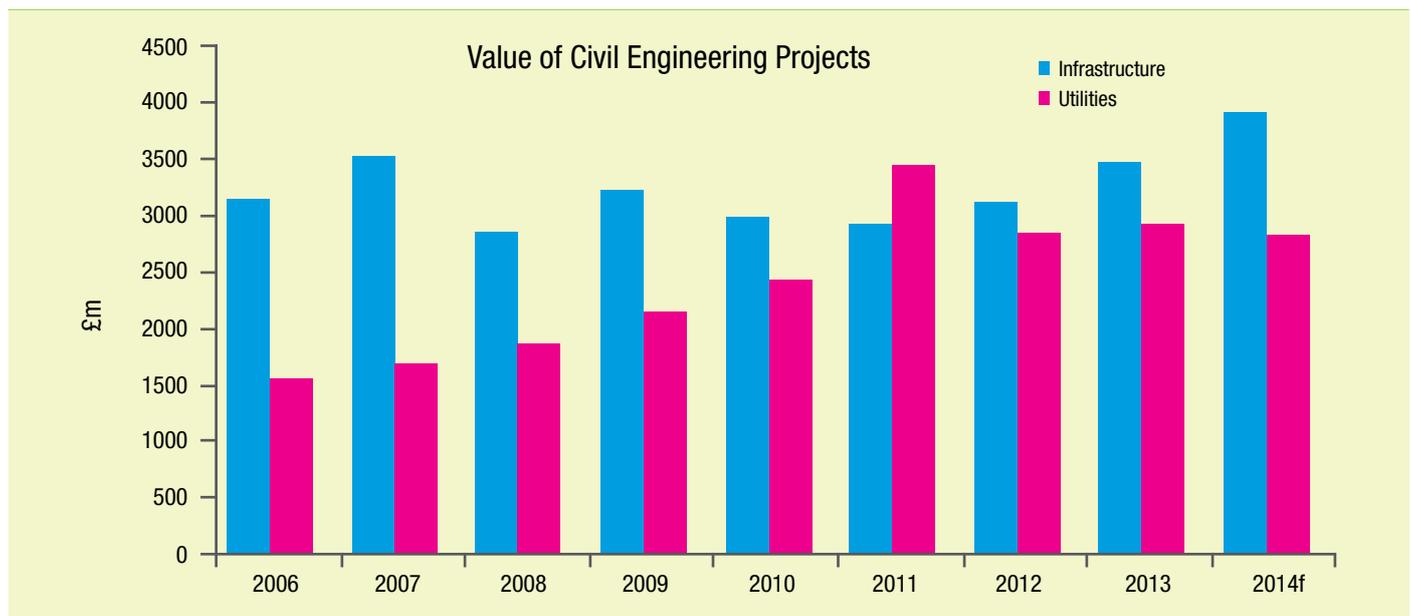
Civil Engineering

Over the past year, Glenigan’s research shows that the underlying value of civil engineering projects starts has risen by 18%. Only the industrial sector grew at a faster pace, and then from a much lower base.

However the flow of project starts has dipped over the summer months, with the underlying value of project starts in the utilities and infrastructure sectors during the three months to August only 2% up on a year ago. Office of National Statistics data for Q2 2014 shows overall infrastructure output as falling by 8.2% when compared to the same quarter a year earlier. The drop was less marked when the latest quarter was compared to the previous three months with a fall of 3.9% and elsewhere there is evidence of growth.

The latest state of trade survey from the Construction Products Association shows that civils workloads increased for a fourth quarter in a row in Q2 2014, while the most recent purchasing managers’ index from Market and the Chartered Institute of Purchasing & Supply backs this up.

The Markit/CIPS index showed a sharp rise in civil engineering activity in August 2014. The increase was the fastest rise since March 2014 and this sector experienced the second largest rise, behind private residential work but ahead of commercial activity, according to Markit/CIPS.



Note: Underlying projects - excludes projects with a construction value of £100m or more. **Source:** Glenigan

Social Housing

The underlying value of project starts in the social housing sector is up by 12% in the year to August 2014 on the same period a year earlier. However in the three months to August 2014, there is a 13% fall and the long-term prospects for social housing provision do not look good.

Private housebuilders are building fewer and fewer social housing units and government cuts are impacting planned spending by registered social landlords according to Glenigan’s data, which shows a significant slump in the

number of units being developed through the planning system.

In the year to Q2 2014, registered social landlords (RSLs) submitted 523 planning application for social housing schemes of 10 or more units. The total number of units in that planning pipeline is 17,529 homes. In the preceding 12 month period, RSLs submitted 640 applications of 10 or more units to build a total of 25,853 homes.