UK Construction Forecast

A 2020-2022 construction industry forecast

June 2020

About the authors

Allan Wilen BSc (Hons),
Glenigan Economics Director

Rhys Gadsby Bsc Econ,
Glenigan Economic Analyst

Allan heads up Glenigan's Economics Unit and has over 30 years' experience in providing insightful market analysis and forecasts on UK construction and the built environment. Following 20 successful years as Economics Director at the Construction Products Association, Allan joined Glenigan 12 years ago. During this time Allan and his team have helped hundreds of businesses confidently develop their market strategies.

Allan sits on the Consulting Committee on Construction Industry Statistics for the Dept for Business (BEIS), is member of a Construction Leadership Council working group and is a guest lecturer in construction at the University of Reading.

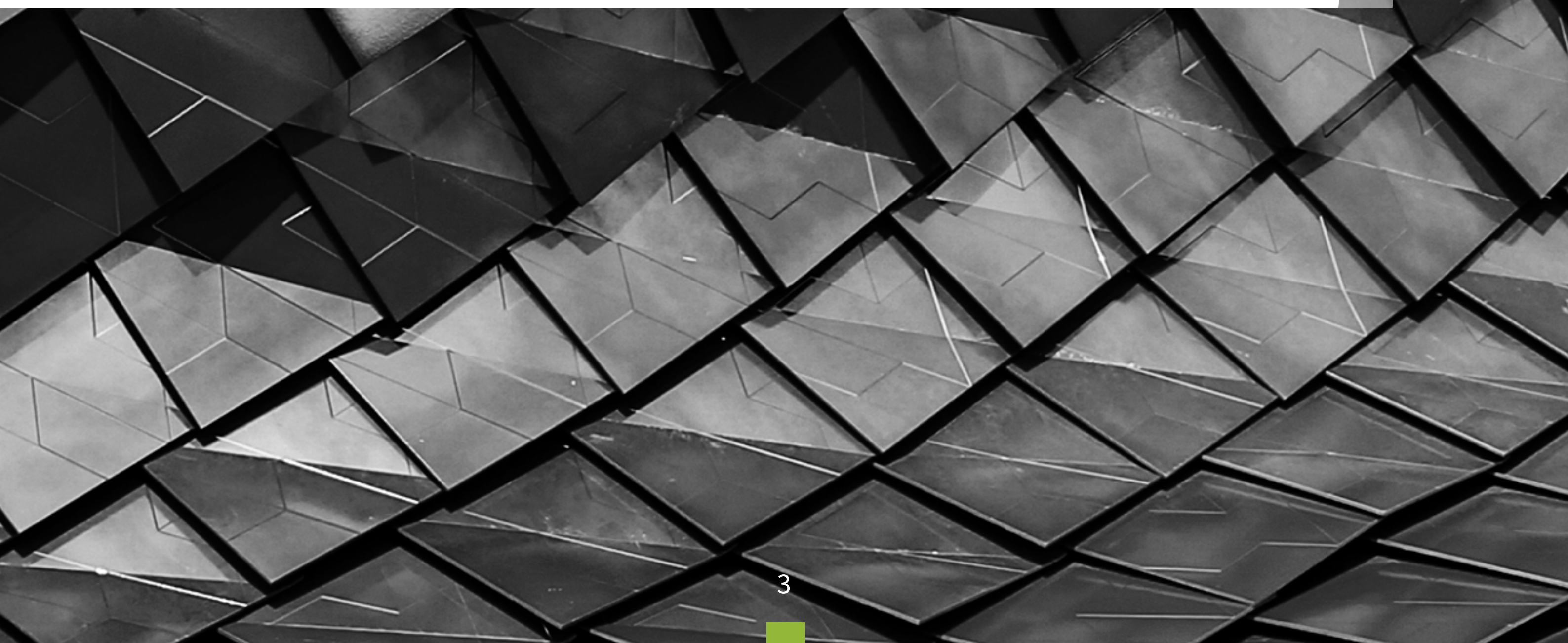
Rhys joined Glenigan in 2019 and is responsible for the research behind the Glenigan Index, sector analysis for the Glenigan Construction Review, and is a regular contributor to bespoke reporting for customers.

Business intelligence from Glenigan

The Glenigan economics team are experts in delivering tailored construction insight, analysis and recommendations to companies just like yours. Our key planning and construction industry insight has been built up over years of impartial data gathering and our economics team combine this with their commercial expertise to provide in-depth strategic analysis and statistics to give you the insight you need to make key budgeting and statistical planning decisions.

Contact us today with your requirements:

Call **0800 060 8698**
Email **info@glenigan.com**
Visit **www.glenigan.com**
80 Holdenhurst Road,
Bournemouth BH8 8AQ



Contents

Tables

Charts

Assumptions and Scenarios

The COVID-19 pandemic has dramatically reshaped the outlook for UK construction activity, as it has for the UK and world economies. The Glenigan summer forecasts take stock of the immediate impact of the pandemic upon the industry and assess the industry's expected path to recovery.

The summer forecasts are built upon the analysis of Glenigan's database of current and planned construction projects which are modelled with other market and economic variables. The modelled data has then been further analysed to take account of the potential change in historic trends and relationships in light of the pandemic.

Construction industry growth over the forecast period will be shaped by the path of the pandemic itself as well the response by the private sector and in particular the Government.

The key assumptions around which the forecasts have been based include:

> **Reduced staffing levels on site slow the pace of development activity and temper the progressive recovery in project starts during the second half of this year.**

> **The UK avoids a 'second-wave' of COVID-19 infections and the accompanying restrictions on construction activity.**

> **Weak UK growth and the disruption to UK business revenues and confidence deter private sector investment in most non-residential sectors.**

> **Rising unemployment and weak earnings growth slow housing market turnover and private housebuilding activity.**

> **Increased public sector investment is forecast to drive the recovery in construction activity as the Government seeks to offset the disruption to the economy from the pandemic and the UK's exit from the European Union.**

> **The UK completes the Brexit transition period at the end of the year, with a limited treaty with the EU in place and a framework for further negotiations of other areas. The limited agreement hampers UK exports to the EU single market and increases UK manufacturers' costs.**

Given the exceptionally high level of uncertainty over the outlook for the UK economy arising from both the pandemic and the UK's future relationship with the EU, Glenigan has prepared two alternative illustrative scenarios in addition to our central forecast.

The assumptions behind these two scenarios are summarised below:

BEST CASE

> Rapid adjustment to COVID-19 site working practices enables improved site productivity and enables a faster recovery in construction output and project starts.

> Brexit: Political flexibility enables continued UK access to the single market while negotiations are completed on a more comprehensive trade agreement.

> Faster delivery of anticipated government investment across key areas including social housing, infrastructure and health sectors.

> Stronger rise in consumer confidence supports a faster recovery in the UK housing markets and private housebuilding.

> Earlier upturn in business investment including in the office and hotel & leisure sectors

WORST CASE

> Second wave of COVID-19 infections and partial reintroduction of lockdown restrictions over the winter months disrupts work on-sites and the recovery in project starts.

> Brexit: Very limited or no trade agreement in place as the UK completes the transition phase at the end of the year. Trading with the EU reverts to World Trade Organization (WTO) rules with significant disruption to supply chains, addition to inflationary pressures and weakening economic growth.

> Weaker economic performance is reflected in the wider housing market and curbs private housing starts.

> Public sector investment in the built environment is more limited and Government departments are slow to implement their capital expenditure plans, dampening the recovery in social housing, health and infrastructure sectors.

> Weaker UK economic performance depresses private sector investment in industrial and commercial buildings.

Executive Summary

2020 -31% 2021 +37% 2022 +5%

The COVID-19 pandemic and the lockdown of much of the UK economy from late March have inflicted a massive external shock to UK construction. The value of underlying project starts fell by an estimated 62% during the second quarter.

The second quarter is expected to mark the low point for the industry. A sharp rebound in construction output and project starts is forecast for the third quarter following the lifting of lockdown restrictions. A more gradual, but sustained recovery is anticipated for the remainder of the forecast period. By 2022, the value of underlying project starts is forecast to total £52.4 billion, just 1% below 2019 levels.

> **COVID-19 safe-site working practices temper recovery in project starts**
>
> **Commercial sector development activity hit by UK recession and fall in business revenues**
>
> **Weak average earnings and rising unemployment hold back private housebuilding**
>
> **Online sales-boost to investment in logistics facilities**
>
> **Greater public sector investment fuels recovery in social housing, health, schools and civil engineering**
>
> **Major projects boost civil engineering workloads**

However, the recovery in construction activity will be greatly influenced by the course of the COVID-19 pandemic. The two alternative scenarios illustrate the potential divergence of project starts from our central forecast.

Chart 1: Value of Underlying Project Starts

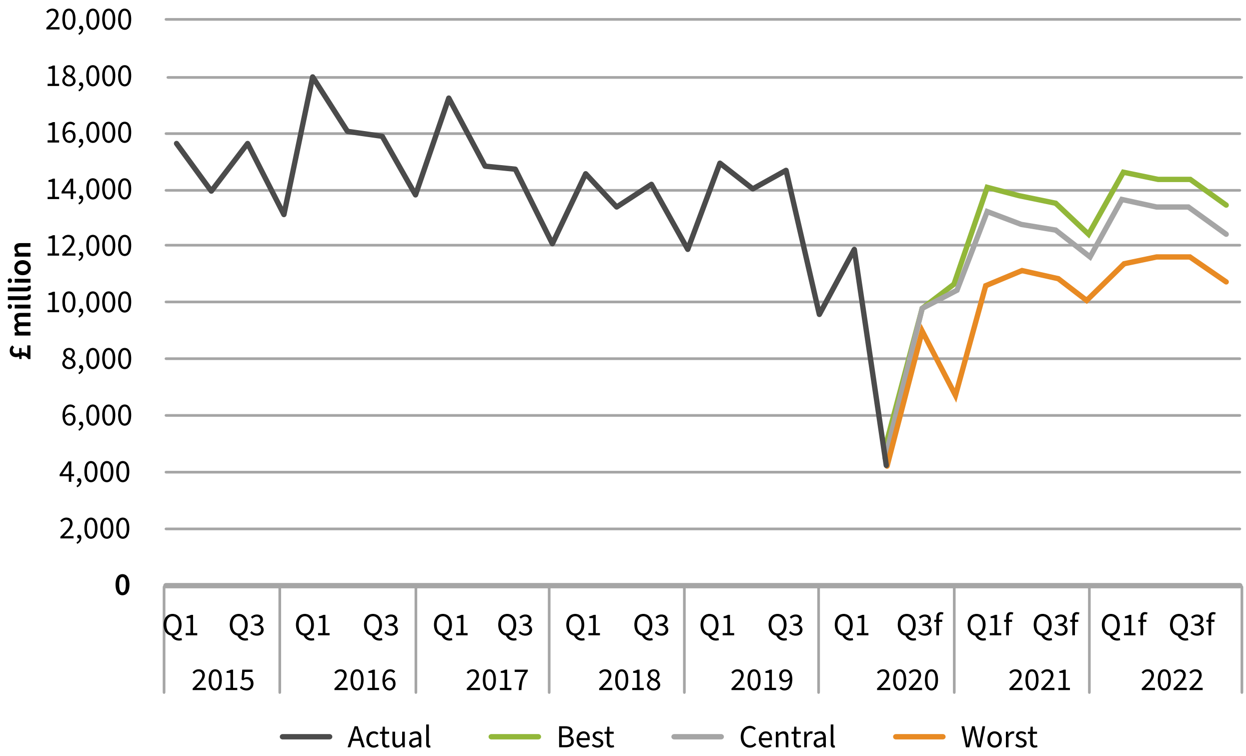


Table 1: Value of Underlying* Project Starts by Sector

£ Million	2019	2020f	2021f	2022f
PRIVATE HOUSING	17,489	10,099	14,333	16,426
SOCIAL HOUSING	6,271	4,069	6,594	6,908
INDUSTRIAL	4,380	3,689	4,765	4,152
OFFICES	4,669	3,282	3,821	3,764
RETAIL	2,125	1,417	1,847	1,749
HOTEL & LEISURE	3,645	2,503	3,176	3,540
EDUCATION	5,534	3,695	5,652	5,883
HEALTH	1,930	1,969	2,504	2,599
COMMUNITY & AMENITY	811	825	1,108	1,136
CIVIL ENGINEERING	6,399	4,951	6,468	6,737
TOTAL	**53,254**	**36,500**	**50,266**	**52,893**

Source: Glenigan
** Excludes projects over £100m*

DEPRESSED ECONOMY DAMPENS PRIVATE NON-RESIDENTIAL WORK

A weak UK economy is expected to constrain construction activity over the forecast period, with private sector workload particularly weak.

UK manufacturing faces weak domestic and overseas demand. In addition, UK manufacturers have less favourable access to the EU single market and potential disruption to EU sourced supply chains from next year. Against this background we anticipate a continued weakening in manufacturing investment over the forecast period.

In contrast, warehousing & logistics premises are forecast to remain a growth area, bolstered by long-term growth in online retailing which is driving the demand for logistics space. Although growth in this area has been disrupted in the short term by the lockdown, warehousing and logistics activity is forecast to grow strongly during 2021 and 2022.

In the retail sector, activity is forecast to decline over the forecast period as weak consumer spending and the growth in online retailing accelerate the restructuring of the retail industry and depress the demand for retail premises.

Office starts are forecast to decline sharply this year as the lockdown exacerbates a cyclical downturn in sector activity. Project starts are forecast to recover during 2021 and 2022, supported by a rise in refurbishment projects as tenants and landlords adapt premises to accommodate changing working practices. New-build office projects are likely to be slower to recover, as tenants and developers assess the impact of rising unemployment and the potential structural shift in remote working on the long term demand for office accommodation.

The COVID-19 pandemic has hit private housing activity hard. As suspended sites are re-opened, housebuilders are prioritising sites that are close to completion. With homebuyers confidence dented by the poorer economic outlook, the recovery in project starts is expected to be gradual over the forecast period.

INCREASED GOVERNMENT INVESTMENT

Social housing activity picked up during 2019. Whilst the pandemic has caused a short-term hiatus in starts this year, renewed growth is anticipated from 2021. In contrast, student accommodation work faltered during 2019 and a further marked contraction in student accommodation work is expected this year, with only a limited recovery in this sub-sector during 2021 and 2022.

An increase in school building projects is forecast to drive a recovery in sector activity during 2021 and 2022 as local authorities tackle a shortage of secondary school places. A fall in universities capital spending is expected to temper the overall growth in education sector work.

The outlook for the health sector is brightening, with promised increases in NHS capital funding expected to lift project-starts over the next two years. The Nightingale temporary hospital programme has bolstered project starts this year. Starts are subsequently forecast to gather momentum during 2021, rising by 27%, as NHS trusts develop and implement their investment programmes.

While civil engineering project starts, along with other sectors, have been disrupted and delayed by the lockdown, the sector is set to recover strongly over the forecast period. The government has pledged to significantly increase investment in the UK's infrastructure. In many areas such as energy and broadband, such investment will be delivered by the private sector.

Where additional public sector funding is potentially available in areas such as roads, it may take time before additional projects are 'shovel-ready'. Therefore, we anticipate that initially, additional funding will be directed at areas such as tackling the maintenance backlog on the nation's roads.

Existing major infrastructure schemes, including Thames Tideway, HS2 and Hinckley Point, are also forecast to lift civil engineering output over the forecast period. The £1.4 billion Stonehenge Tunnel is currently scheduled to start in 2021, but important planning and contracting hurdles have yet to be cleared.

Table 2: Growth in the value of Underlying* Project Starts by Sector

Change on a previous year	2019	2020f	2021f	2022f
PRIVATE HOUSING	-4%	-42%	42%	15%
SOCIAL HOUSING	0%	-35%	62%	5%
INDUSTRIAL	-1%	-16%	29%	-13%
OFFICES	2%	-30%	16%	-1%
RETAIL	-9%	-33%	30%	-5%
HOTEL & LEISURE	-3%	-31%	27%	11%
EDUCATION	-10%	-33%	53%	4%
HEALTH	-21%	2%	27%	4%
COMMUNITY & AMENITY	-7%	2%	34%	3%
CIVIL ENGINEERING	27%	-23%	31%	4%
TOTAL	**-1%**	**-31%**	**38%**	**5%**

Source: Glenigan
** Excludes projects over £100m*

Private Housing

2020 -42%   2021 +42%   2022 +15%

The COVID-19 pandemic has hit private housing activity hard. As suspended projects are re-opened, housebuilders are prioritising sites that are close to completion. With homebuyers' confidence dented by the poorer economic outlook, the recovery in project-starts is expected to be gradual over the forecast period.

PRIVATE HOUSING STARTS

	2019	2020f	2021f	2022f
£ million	17,489	10,099	14,333	16,426
Growth	-4%	-42%	42%	15%

- **> Strong potential development pipeline**
- **> Weak household earnings and rising unemployment overshadow housing market**
- **> Housebuilders prioritise existing sites near term**
- **> Gradual recovery in private housing starts during 2021 and 2022**
- **> Help to Buy will continue to support new house sales and new site developments over the forecast period**

The value of private housing projects starting on site declined for a second consecutive year during 2019, falling by 4% as housebuilders prioritised building-out existing developments and opened fewer new sites. The COVID-19 pandemic prompted an additional, sharper retrenchment in new project starts during the second quarter of this year as housebuilders temporarily suspended work on current sites and postponed new project starts.

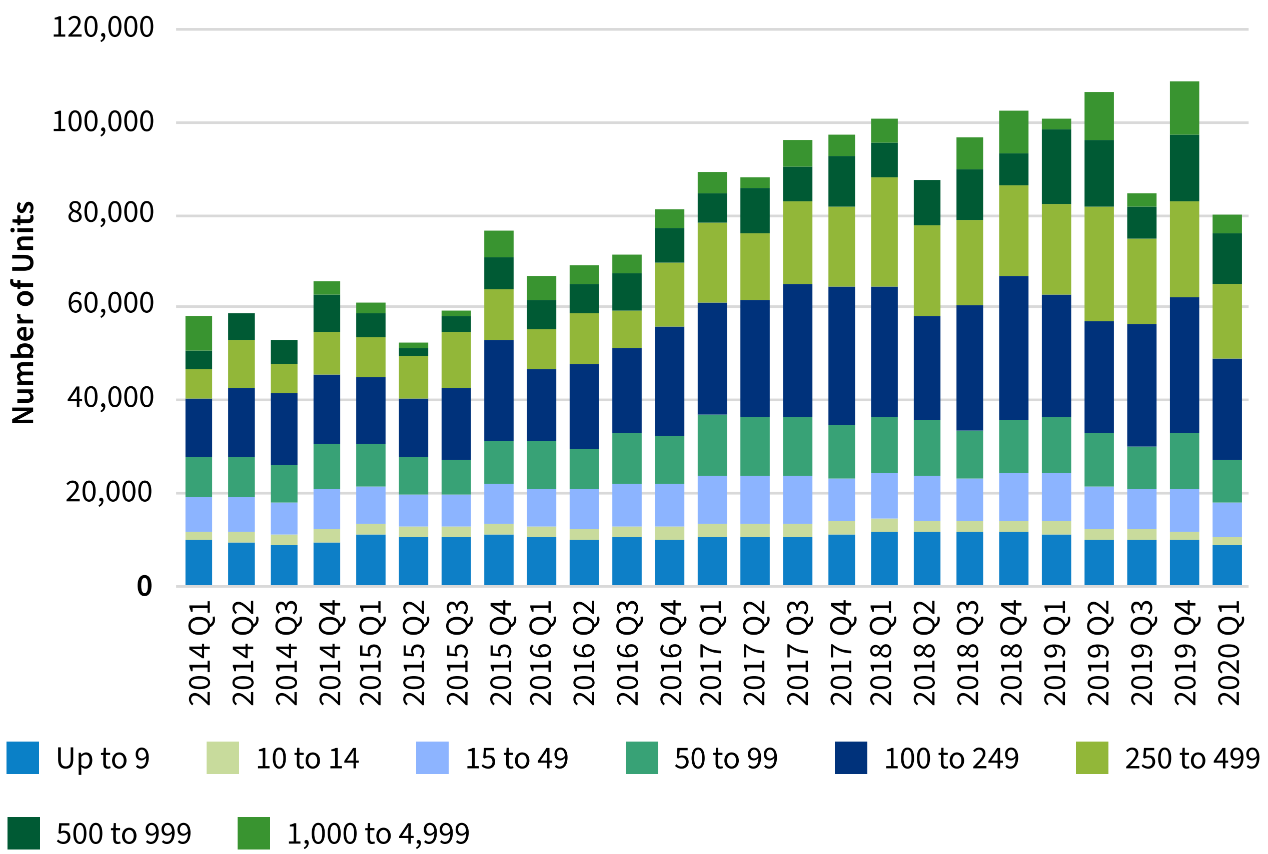
As existing sites have been reactivated, housebuilders have prioritised sites nearing completion, as such sites require fewer people on-site and provide a more immediate source of revenue as completed homes are sold.

Housebuilders will continue to prioritise existing sites during the second half of this year, limiting the recovery in project starts.

The number and value of projects securing planning approval has weakened over the last 2 years. However, this decline follows five years of progressive growth in approvals between 2013 and 2017 and the development pipeline remains firm.

Demand, rather than supply, will be the principal constraint on new private housing activity during the forecast period.

Chart 2: Private residential projects

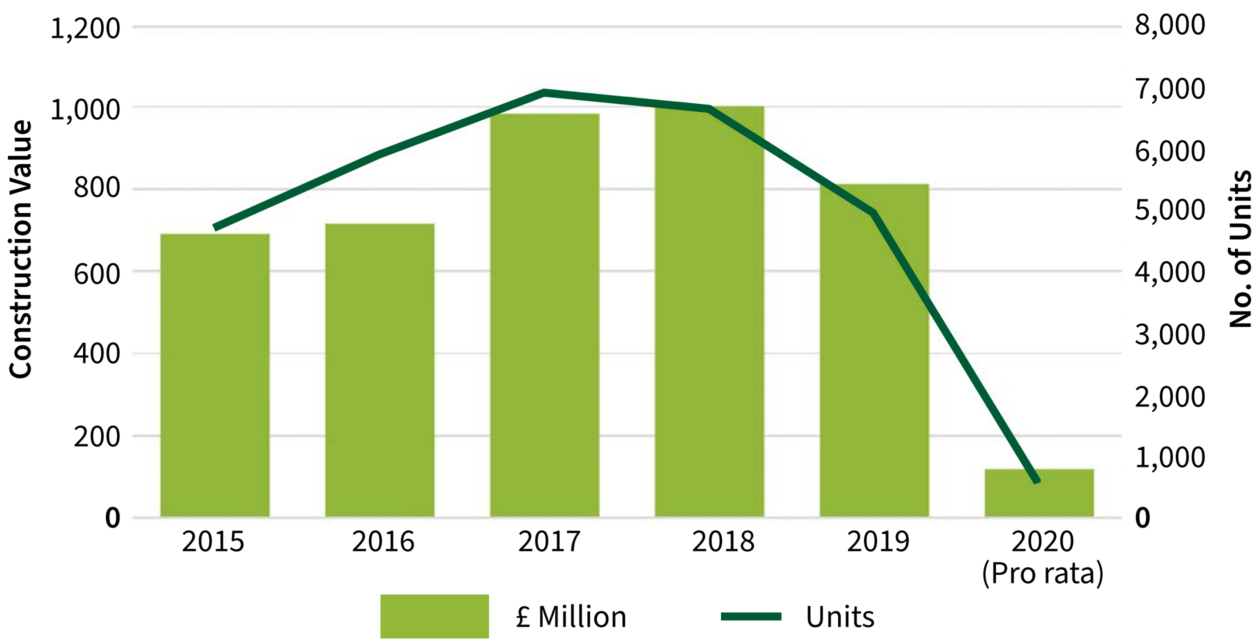


Source: Glenigan

The wider housing market was effectively frozen during April and May and the number of property transactions and house prices are expected to be extremely weak during the remainder of 2020, with potential sellers nervous of opening their homes for viewing and as purchaser confidence is dented by fears over rising unemployment and weak earnings growth. Low turnover in the wider housing market is expected to dampen new house sales especially to existing homeowners, although new home sales are likely to gain market share among first time buyers.

Improved trading conditions in the wider housing market from next year are expected to help lift new house sales and support a recovery in private housing starts during 2021 and 2022.

Chart 3: Private Rented Sector projects starting on-site



Source: Glenigan
N.B. 2020 based on January to May -pro rata

Until last year, the private rented sector had been a small, but fast growing source of work within the private housing sector. However, the flow of Build for Rent schemes starting on-site faltered during 2019, amid Brexit uncertainty and the perceived political risks ahead of last December's General Election. At £800 million the value of Build for Rent schemes started during 2019 was 20% down on the previous year.

The pandemic has prompted a further contraction in Build for Rent starts during the first half of this year. Landlords face the prospect of increased risk of rent arrears and weak rental growth as unemployment rises and household income growth stalls. Near-term the decision to protect tenants from eviction during the COVID-19 crisis has also transferred risks and liabilities to landlords. Against this background, we anticipate Build for Rent starts will remain weak for much of the forecast period, with investors returning to the sector from 2022 once the recovery in the UK economy becomes more established.

Social Housing

2020 -35% 2021 +62% 2022 +5%

Affordable housing activity picked up during 2019. Whilst the pandemic has caused a short-term hiatus in starts this year, renewed growth is anticipated from 2021.

In contrast student accommodation work faltered during 2019, having been an important growth area for the sector in recent years. A further marked contraction in student accommodation work is expected this year, with only a limited recovery in this sub-sector during 2021 and 2022.

SOCIAL HOUSING STARTS

	2019	2020f	2021f	2022f
£ million	6,271	4,069	6,594	6,908
Growth	0%	-35%	62%	5%

> Housing associations better-placed to finance new developments

> Increased support for shared ownership developments

> Contraction in student accommodation development pipeline

Housing associations are now better placed to finance and take forward new developments. Government requirements limiting association's rent increases to 1% below the rate of inflation have ended. This will provide associations with greater flexibility to increase their borrowing to fund new developments.

In addition, the Government is expected to increase sector investment as it seeks to both honour its election commitments and to kick-start the UK economy. While it is currently unclear how much of the additional funding is to be directed to improving social housing provision, the Government is already fully-funding the replacement of unsafe ACM cladding on social sector properties. It has also promised increased support for shared ownership developments.

The value of affordable housing projects started on site grew by 17% last year. Affordable housing starts are forecast to plunge by 29% this year following the suspension of work on existing sites for much of the second quarter and an accompanying 80% drop in starts during the second quarter.

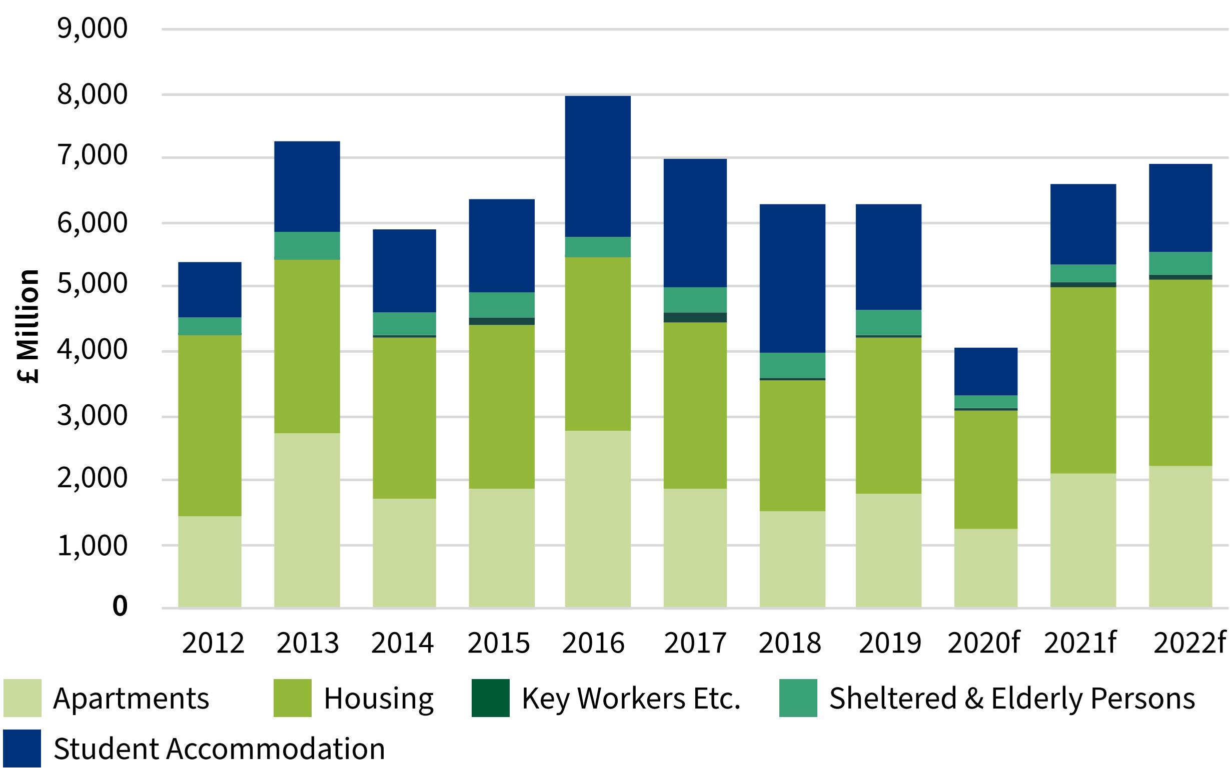
However, a sustained recovery in affordable housing activity is expected to lift sector-starts during 2021 and 2022.

Student accommodation work had been the bright spot within the social housing sector, with starts growing by 65% over the five years to 2018. After such rapid growth, student accommodation starts slipped back last year.

As with affordable housing projects, student accommodation starts have been disrupted in the near term by the Covid lockdown. However the pandemic is also expected to have longer term implications for the purpose-built student accommodation market, which is disproportionately dependent upon lettings to overseas students. Whilst overall student numbers are projected to decline over the medium term, overseas students are widely expected to be especially vulnerable.

The value of student accommodation work started is expected to halve this year, having dropped by 29% last year. While the value of student accommodation starts are forecast to improve over the next two years, starts in 2022 will still be 40% below their 2018 peak.

Chart 4: Social housing starts by type of development



Source: Glenigan

Industrial

2020 -16% 2021 +29% 2022 -13%

Strong demand for logistics space is supporting sector activity, but recession and Brexit are set to disrupt manufacturing investment.

Industrial project starts fell an estimated 70% during the second quarter of 2020 against a year earlier as the lock down disrupted work on-site and delayed project starts. However, driven by the demand for logistics space, the sector is forecast to recover quickly during the second half of the year, limiting the annual decline to 16%.

INDUSTRIAL STARTS

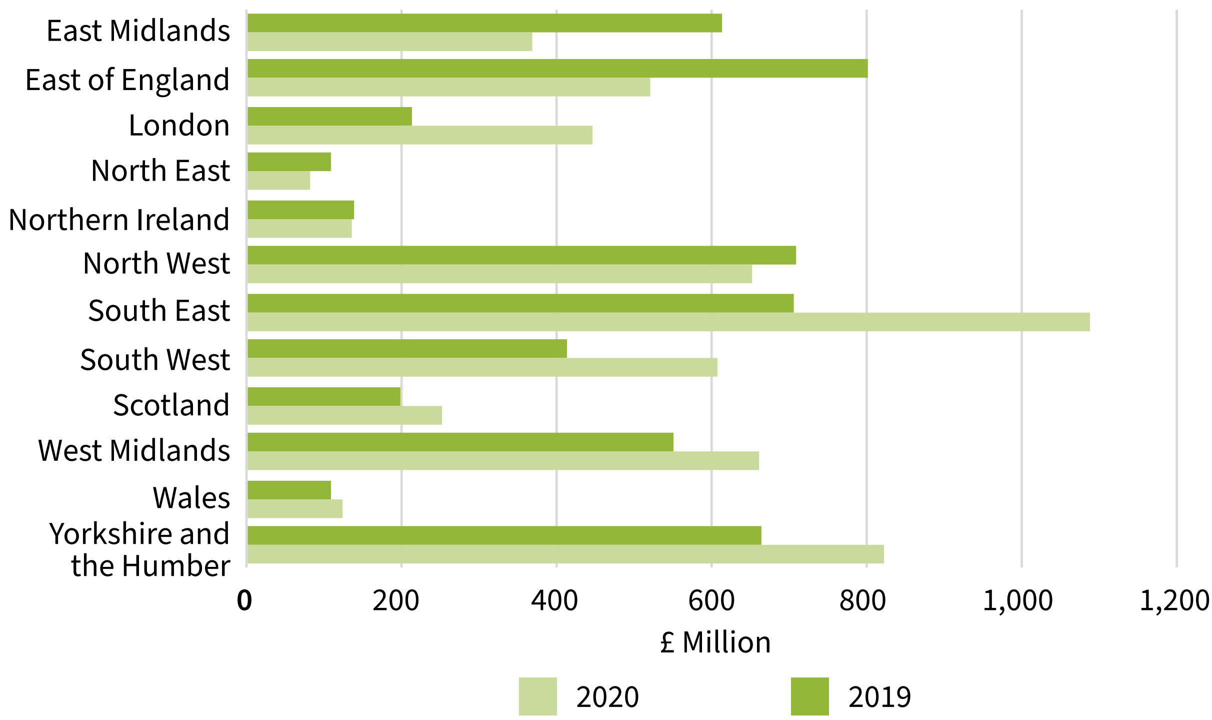
	2019	2020f	2021f	2022f
£ million	4,380	3,689	4,765	4,152
Growth	-1%	-16%	29%	-13%

- **Manufacturers' investment in additional capacity and manufacturing premises is deterred by weak domestic and overseas demand and reduced access to the European Single Market**
- **Demand for logistics space is lifting investment in warehousing and distribution facilities**
- **Midlands and North West are prime areas for sector growth**

Manufacturers' investment in capacity and premises will be determined by their long term growth prospects. Weak UK economic growth is expected to dampen domestic demand for manufacturers products, and with most major economies falling into recession, overseas demand has also weakened. In addition, manufacturers are also likely to face reduced access to EU markets and disrupted supply chains from 2021.

Against this adverse economic background, manufacturers' investment in new premises is expected to be weak over the forecast period as manufacturers prioritise efficiency improvements over additional capacity.

Chart 5: Detailed planning approvals for industrial projects



Source: Glenigan
N.B. 2020 data is based on Jan to May pro rata

Warehousing and logistics have been the fastest growing segment within the industrial sector in recent years.

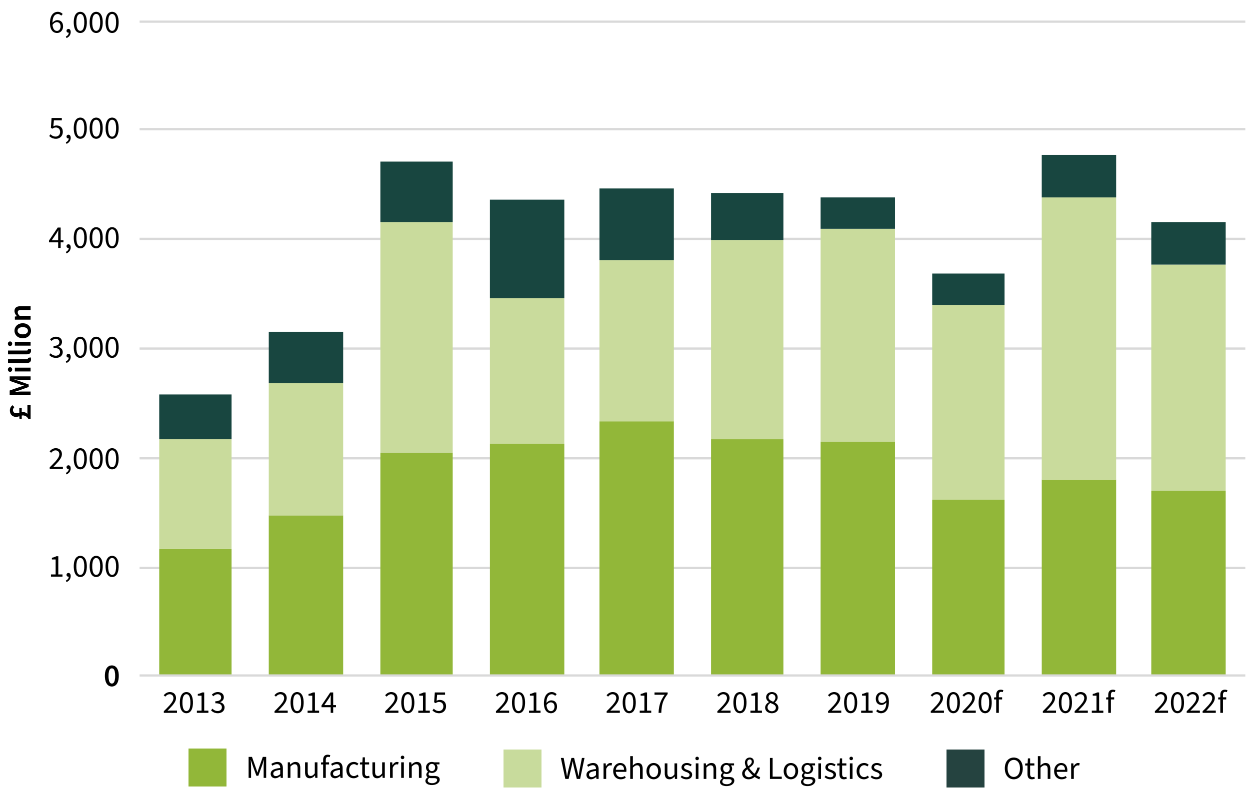
Investor confidence and project-starts have recovered after a sharp fall in project-starts in the immediate aftermath of the EU referendum. The value of starts grew a third consecutive year in 2019, increasing by 6% last year to £1.9 billion.

Demand for logistics space is being principally driven by structural change in the retail sector, with the relentless growth of online retailing, 'click & collect' and home deliveries fuelling demand for warehousing and distribution premises. Online retailing has surged during the lockdown, with many consumers becoming regular online shoppers for the first time and retailers and logistics firms increasing their home delivery capacity. Online purchases accounted for 30% of all retail sales in May. Although shops are now re-opening, we believe that the lockdown has accelerated the long-term structure trend towards online retailing.

Investment in warehousing and logistics facilities has remained strong throughout the pandemic. Work is due to start on-site in September on a £200 million distribution centre in Dartford for Amazon, while Segro has raised £650 million in order to increase its investment in the sector. Warehousing and logistics projects are expected to remain the main driver behind the strong growth forecast for industrial starts during 2021 and 2022.

The Midlands, North West and parts of the South East of England are favoured locations for such facilities, offering good access to national transport networks and the UK's major population centres. However, there is also growing demand across the UK for smaller distribution facilities to service the 'final mile' delivery of products to the customer.

Chart 6: Value of Underlying Industrial Starts by Category



Source: Glenigan

Offices

2020 -30%   2021 +16%   2022 -2%

Recent development activity has been driven by a shortage of quality office space, especially outside of London. The increase in available office accommodation as projects are completed, coupled with a bleak outlook for UK unemployment following the COVID-19 pandemic, is forecast to temper the flow of new project starts over the forecast period.

OFFICE STARTS

	2019	2020f	2021f	2022f
£ million	4,669	3,282	3,821	3,764
Growth	2%	-30%	16%	-2%

> UK recession and spike in unemployment to impact demand for office space

> Opportunities for refurbishment and conversion of secondary office accommodation

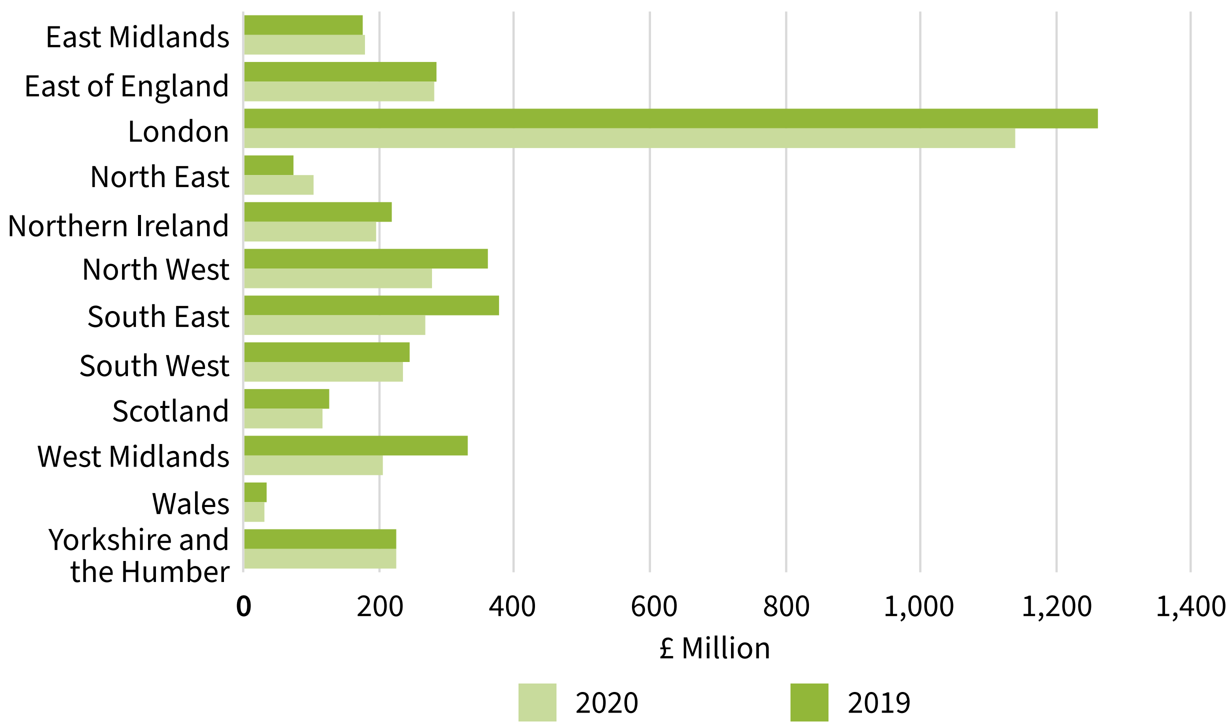
Regional centres, rather than the Capital, have been the recent focus for development activity. Demand for high-quality office space has been growing in the UK's 'core' cities. This rising demand for office accommodation and a previous lack of development activity tightened the supply of available office space in Manchester, Birmingham, Leeds and other major regional centres and has spurned on development activity. Recently completed projects and those currently under construction are now improving the supply of available floorspace. This is expected to dampen new-build project starts during the forecast period, although it may spur the refurbishment and upgrading of existing premises as leases come up for renewal.

The value of underlying project starts in London declined between 2015 and 2018 as Brexit concerns dampened development activity in the capital's financial quarters. Those concerns continue with uncertainty surrounding trade negotiations throughout 2020, nevertheless, the Capital still accounts for around half of all activity.

Despite a significant slowdown towards the end of last year amidst the snap general election, London office starts increased by 4% in 2019, following a marked rise in detailed planning approvals in 2018. Detailed planning approvals increased by a further 29% in 2019, which will contribute to the sector's recovery following the COVID-19 pandemic.

Uncertainty surrounding Britain's trade negotiations with the European Union and the impact on demand for office space following the economic impact of the COVID-19 pandemic is likely to result in a decline in the value of office starts over the forecast period. Despite growth in detailed planning approvals climbing over the last couple of years, we anticipate project starts to fall 30% in 2020, with growth of 16% in 2021. We do not expect project starts to return to pre-COVID-19 pandemic levels during the forecast period.

Chart 7: Detailed planning approvals for office projects



Source: Glenigan
N.B. 2020 data is based on Jan to May pro rata

OFFICES RETAIL HOTEL & LEISURE EDUCATION HEALTH CIVIL ENGINEERING KEY RECOMMENDATIONS

Retail

2020 -33% 2021 +30% 2022 -5%

New retail development activity is subdued as retailers close stores in the face of faltering consumer spending and the growth of online retailing.

RETAIL STARTS

	2019	2020f	2021f	2022f
£ million	2,125	1,417	1,847	1,749
Growth	-9%	-33%	30%	-5%

- **Demand for retail space hit by weak household earnings and growth of online retailing**
- **Retailers rationalising their estates as costs rise and in-store sales volumes falter**
- **Refurbishment of retained premises to attract customers and support online offering**
- **Pandemic has intensified the squeeze on 'bricks & mortar' retailers from weak consumer spending and growing online sales**

Retailers face challenging market conditions. Overall consumer spending is growing, but slowly. Before the COVID-19 pandemic, the OBR estimated consumer spending would grow by just 1.5% this year before strengthening to 1.6% in 2021. This compares to an average rise of 2.3% per annum over the last five years. This is reflected in weak retail sales growth, with online sales taking an ever-growing proportion of sales. The COVID-19 pandemic accelerated this trend, with online sales as a proportion of all sales rising from 18.9% in February 2019 to 32.8% in May 2019 according to the ONS.

Against this backdrop, the retail property market faces weakening demand for retail space and softening rental values as many retailers look to rationalise their existing estate and renegotiate rental terms.

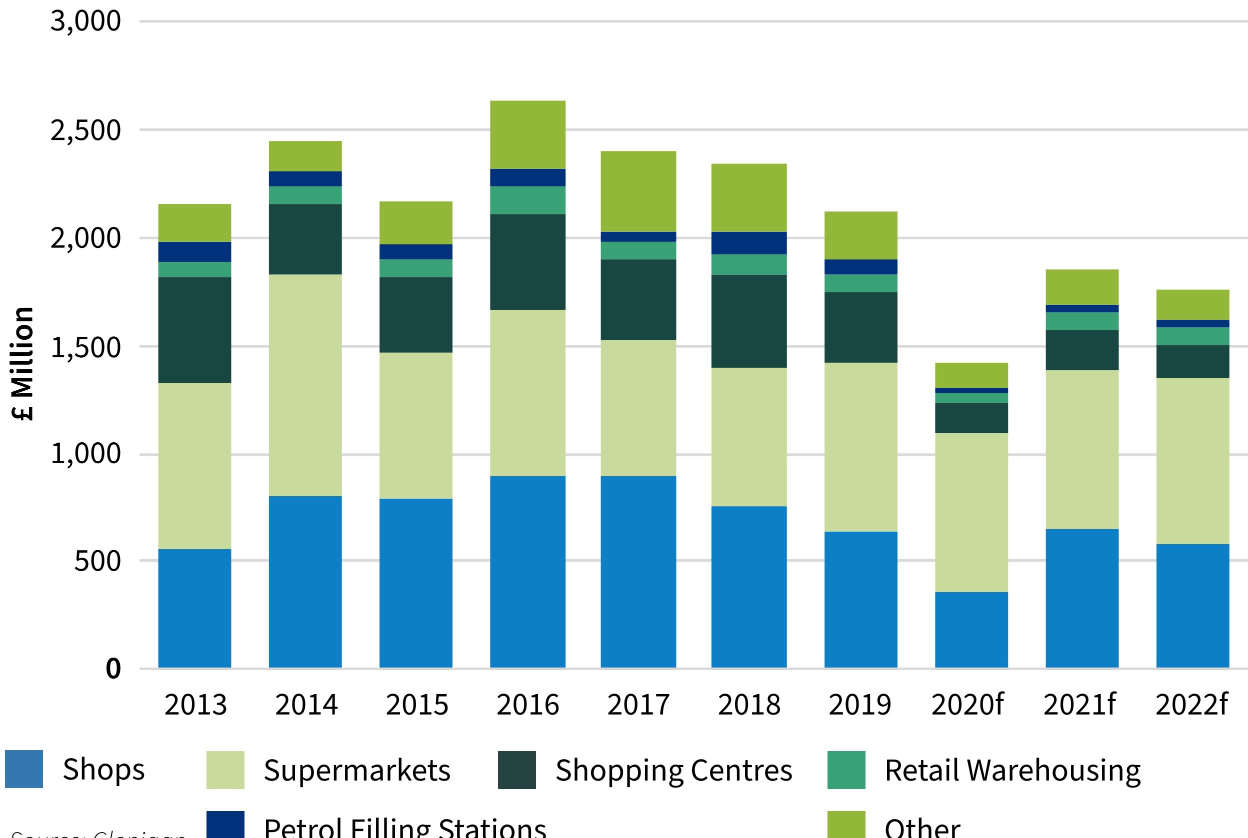
A number of well-known high street names have failed over the last few years, a trend that appears to have accelerated in recent months. Other retailers, driven by declining in-store sales and efforts to accommodate click & collect services have rationalised their estate, closing stores and seeking rent reductions and re-modelling their retained stores. The latest BRC/ Springboard's retail survey reports that 10% of UK retail premises were vacant prior to the pandemic.

Three of the UK's leading shopping centre owners have recently reported falling rental incomes and asset values as vacancy rates have risen and retailers have sought rent reductions.

The leading supermarket chains have scaled back and focussed their investment programmes towards the convenience store format. This often entails the conversion of existing high street premises rather than the construction of new stores. Only the deep discounters, Lidl and Aldi, have substantial new store development programmes.

These have helped to stabilise the value of project starts this year as Lidl and Aldi progress their development programmes. However, the upturn is forecast to be short-lived given weak market conditions and a shrinking development pipeline.

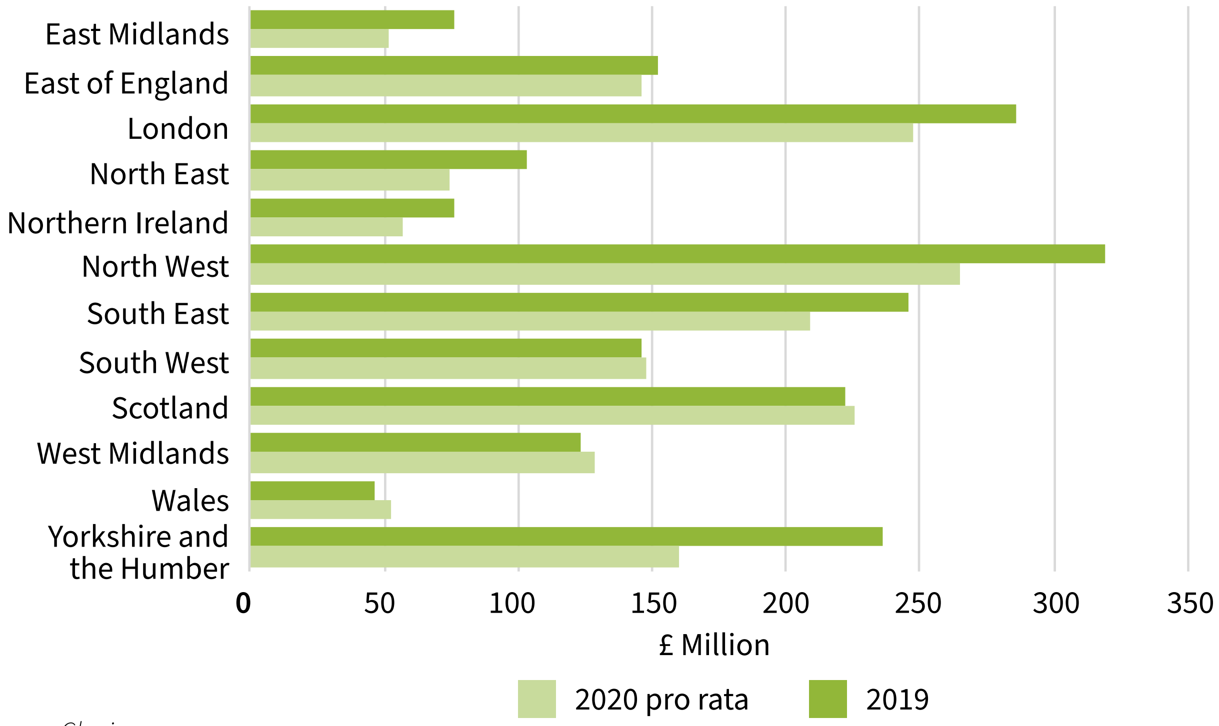
Chart 8: Value of Underlying Retail Starts by Category



Source: Glenigan

Slower retail sales growth and the rise of online sales are forecast to feed through to a decline in the value of retail starts over the forecast period. Despite the value of projects securing detailed planning approval climbing 6% last year, we expect project-starts to fall by a third this year, with growth of 30% in 2021.

Chart 9: Detailed planning approvals for retail projects



Source: Glenigan
N.B. 2020 data is based on Jan to May pro rata

Hotel & Leisure

2020 -31%   2021 +27%   2022 +12%

Sector activity stabilised in 2019 after the retrenchment seen in 2018. Investors and operators remain cautious as UK consumer spending weakens and earlier increases in overseas visitors is reversed.

We forecast a gradual strengthening in project starts over the forecast period as investor confidence improves longer-term.

HOTEL & LEISURE STARTS

	2019	2020f	2021f	2022f
£ million	3,645	2,503	3,176	3,540
Growth	-3%	-31%	27%	12%

- **Strong development pipeline, but investors cautious**
- **More UK residents expected to holiday in the UK with weaker consumer spending and fears of travelling far from home**
- **Hotel chains have significant expansion plans**

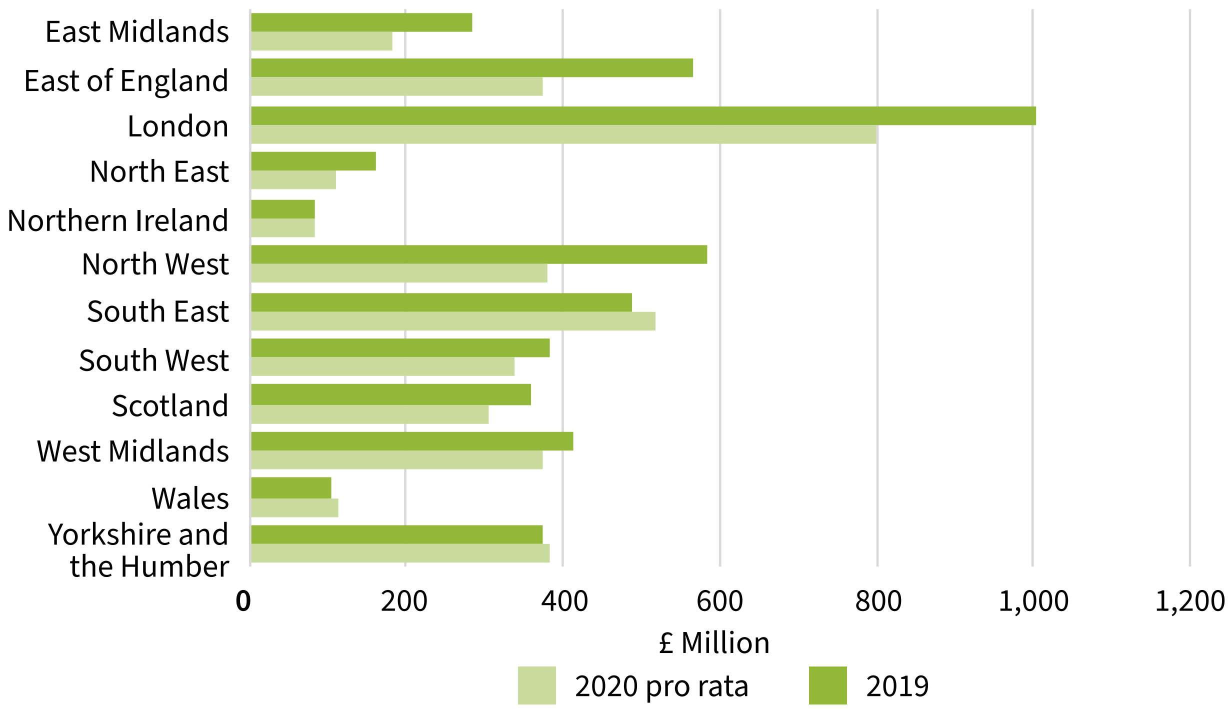
Before the COVID-19 pandemic hit the UK, the hotel & leisure sector appeared to be strengthening. According to Visit Britain, the number of overseas visitors to the UK increased by 1.4% last year and related expenditure rose by 7.3%. The rise in overseas visitor numbers in 2019 may have prompted increased confidence among investors.

As a result, the value of sector detailed planning approvals rose 15% on the previous year. The value of projects commencing on-site remained largely unchanged, dropping 3% last year. The five months to May 2020 saw the value of projects commencing on site fall 27% due to many sites shutting as a result of the UK lockdown.

However, throughout the forecast period, the hotel & leisure sector should be able to take a greater share of discretionary spending by UK households as the weaker pound and economic effects of the COVID-19 pandemic prompts more UK consumers to holiday in the UK. Weak confidence in travelling far from home, as well as rising unemployment and weak consumer spending, should boost the UK hotel & leisure sector in the short-term.

Near term, investors and operators remain cautious. The sector has a strong pre-construction development pipeline of projects that have secured detailed planning consent over the last three years, with that remaining the same throughout the five months to May 2020. A more certain political and economic outlook is expected to encourage investors to bring forward more projects longer-term, especially in 2021. We therefore anticipate that sector starts will recover towards pre-COVID-19 pandemic levels by the end of the forecast period.

Chart 10: Detailed planning approvals for hotel & leisure projects



Source: Glenigan
N.B. 2020 data is based on Jan to May pro rata

Education

2020 -33% 2021 +53% 2022 +4%

Increase in secondary school building projects forecast to drive sector activity longer term, as universities scale back their capital spending.

EDUCATION STARTS

	2019	2020f	2021f	2022f
£ million	5,534	3,695	5,652	5,883
Growth	-10%	-33%	53%	4%

> New and expanded secondary schools needed as pupil numbers rise

> Universities moderating investment plans

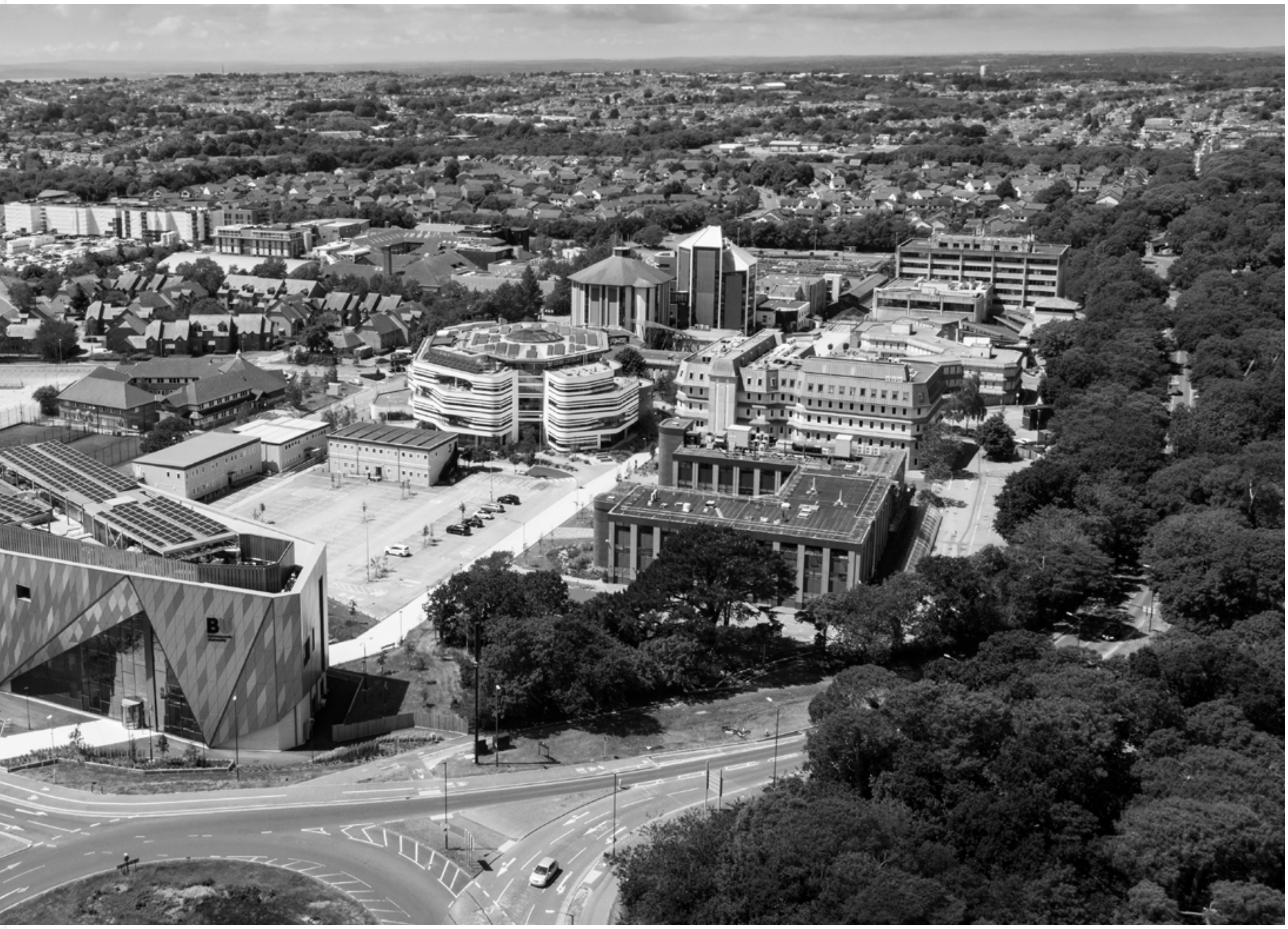
The number of secondary school-age children in England is projected to rise by 13.6% over the five years to 2022. Cash-strapped councils have sought to accommodate the initial rise in pupil numbers through the expansion of existing schools. However, new schools will also be required, especially in areas of high growth such as London and other major metropolitan areas.

Growth in school building work has been slow and sporadic, reflecting local authorities' tight financial positions and the regulatory hurdles to creating a new school. The value of project starts is estimated to have slipped 10% in 2019, having risen by 8% during 2018. Largely as a result of the national lockdown, the 5 months to May saw the value of project-starts sharply fall 45% compared to the previous year.

Looking ahead, the Government's pledge to increase capital investment may help to increase the funding available to local authorities to invest in their school estate. This is expected to help accelerate the delivery of much needed school places and lift school building starts in the long term. Because of this, we anticipate the value of project starts to jump 53% in 2021, despite a fall of 33% in 2020.

Investment in higher education facilities has been a growth area as universities have competed to attract domestic and overseas students. The value of project starts grew by 28% in 2018. Investment has been undertaken by a wide range of universities with the Russell Group of Universities accounting for the lion's share of activity.

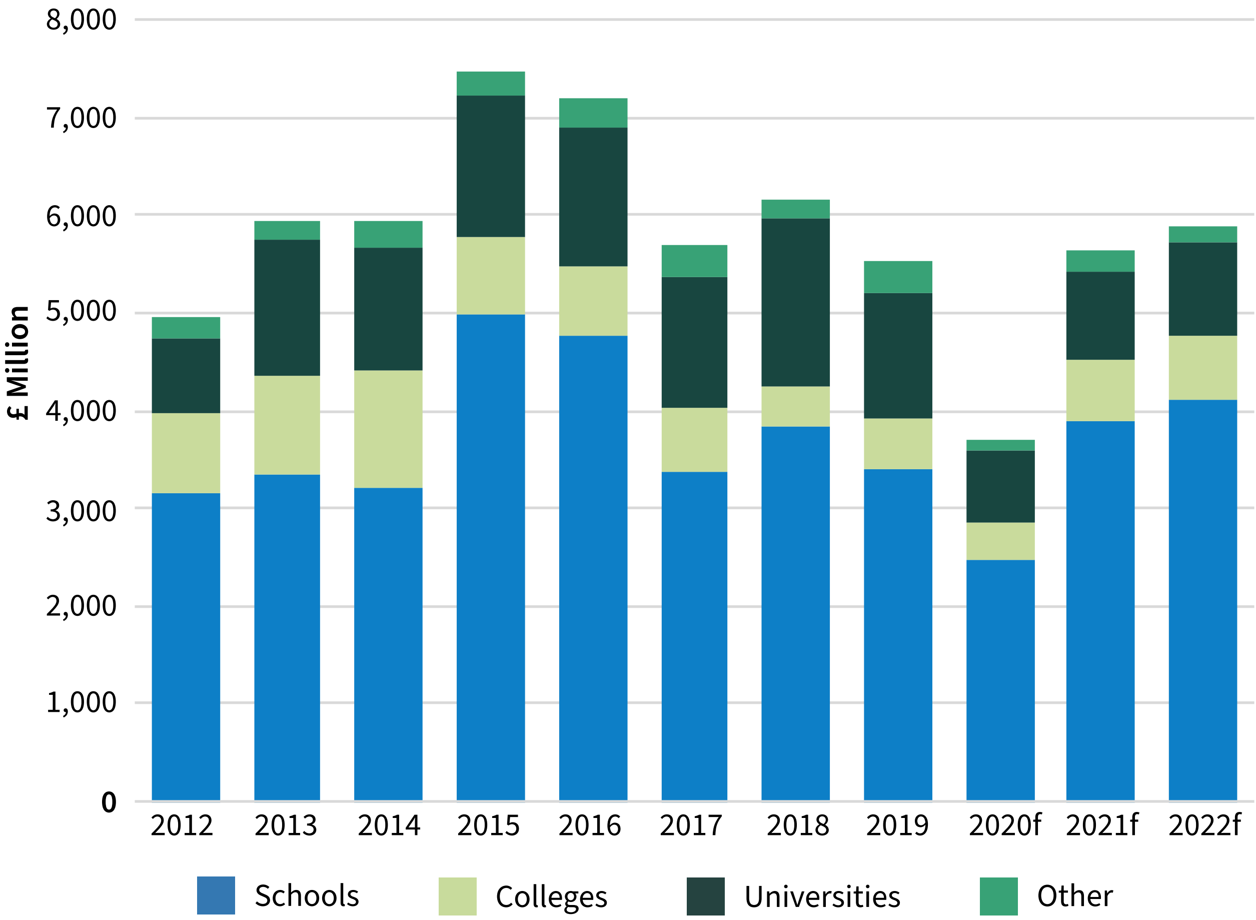
However, universities now face increasing funding pressures from a weakening in UK student numbers. In addition, the Augar Review has proposed changes to graduate funding. Against this background university project-starts fell back by an estimated 25% in 2019.



The pandemic has exacerbated the financial problems faced by universities, with the number of high-fee paying overseas students expected to fall. Higher education project starts are expected to fall back sharply this year, in part due to the disruption to planned projects directly caused by the pandemic. The subsequent recovery in university construction activity will be weak, with activity consolidating significantly below pandemic levels.

Overall, sector starts are forecast to drop by a third this year due to a fall in all education work during the lockdown period. The forecast rise in school building projects over the next two years is expected to contribute to a boost in sector starts by 53% in 2021 and 4% in 2022.

Chart 11: Value of underlying Education starts by category



Source: Glenigan
N.B Excludes projects with a construction value in excess of £100m.

EDUCATION
HEALTH
CIVIL ENGINEERING
KEY RECOMMENDATIONS

Health

2020 +2%

2021 +27%

2022 +4%

The outlook for the health sector remains bright, with promised increases in NHS capital funding expected to lift project starts over the next two years.

HEALTH STARTS

	2019	2020f	2021f	2022f
£ million	1,930	1,969	2,504	2,599
Growth	-21%	2%	27%	4%

> Anticipated strengthening in the development pipeline

> Sustained increase in NHS funding over the next two years

> Increase in NHS capital budgets in 2019/20 and 2020/21

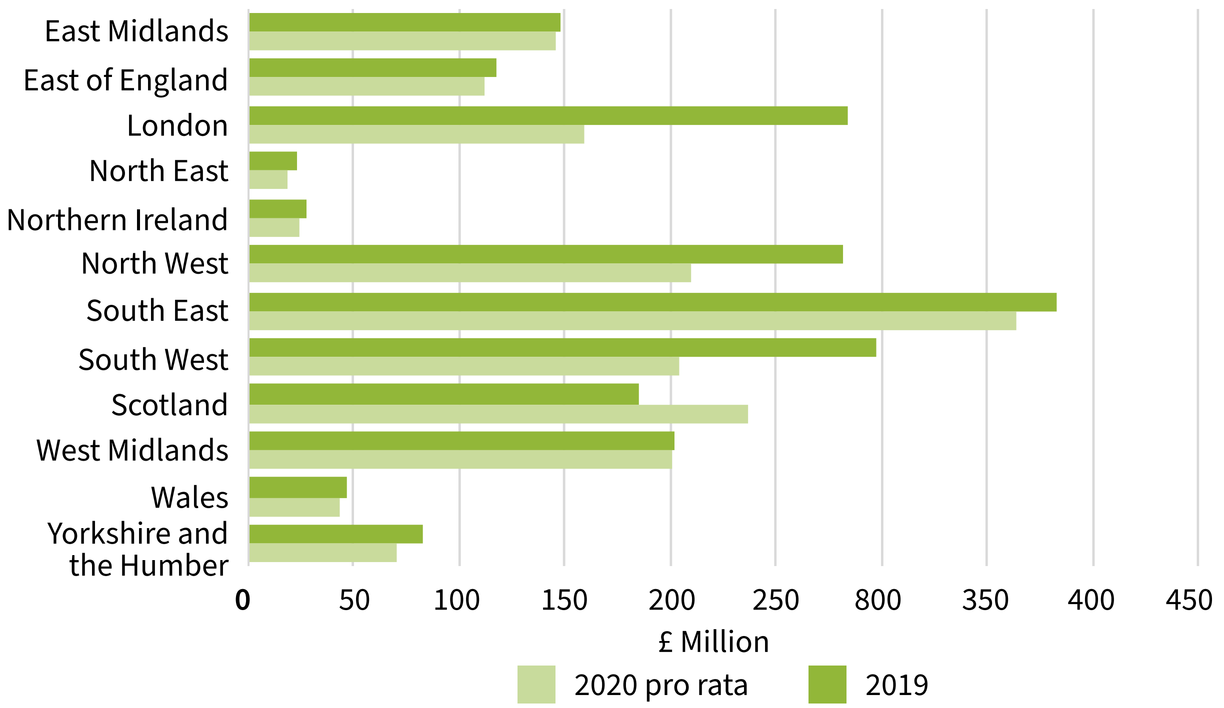
NHS funding is high on the political agenda with extra funding promised by the Government. An extra £20 billion has been committed to the NHS over the next five years. This includes a 14% rise in capital funding for the NHS in England to £6.7 billion in 2019/20.

Initially front-line services, rather than longer term investment in health facilities, will see the benefit of the additional resources. Whilst capital investment in NHS facilities can deliver efficiency improvements and better health outcomes, it will take time to bring forward new building projects.

There are currently few projects in the development pipeline. The value of health projects securing detailed planning consent fell 7% in 2018 and approvals fell by 5% during 2019. Approvals remained unchanged during the five months to May 2020. Against this background, project starts have fallen back 21% this year after a strong performance during 2018. The end of 2019 saw a fall in starts as projects were not progressing to site because of the uncertainty surrounding the result of the snap election in 2019. Project starts fell 29% during the first five months to May, largely because of the national lockdown.

Looking ahead, the sector will benefit from the promised additional government funding. Despite the scarcity of projects currently in the development pipeline and many sites shutting as a result of the UK lockdown, we expect initial sector growth of 2% this year. Starts are forecast to gather momentum during 2021, rising by 27%, as NHS trusts develop and implement their investment programmes. We forecast a further 4% rise in 2021.

Chart 12: Detailed planning approvals for health projects



Source: Glenigan
N.B. 2020 data is based on Jan to May pro rata

Civil Engineering

2020 -23%   2021 +31%   2022 +4%

Major infrastructure schemes, including Thames Tideway, HS2 and Hinckley Point, will be important drivers for sector activity over the forecast period. In addition, we anticipate a strengthening in the value of underlying project starts.

CIVIL ENGINEERING STARTS

	2019	2020f	2021f	2022f
£ million	6,399	4,951	6,468	6,737
Growth	27%	-23%	31%	4%

> Increased spending by Network Rail on maintenance and renewals

> Main works on HS2 commence on-site

> Highways England's development programme gathering momentum

> Major boost anticipated in road projects

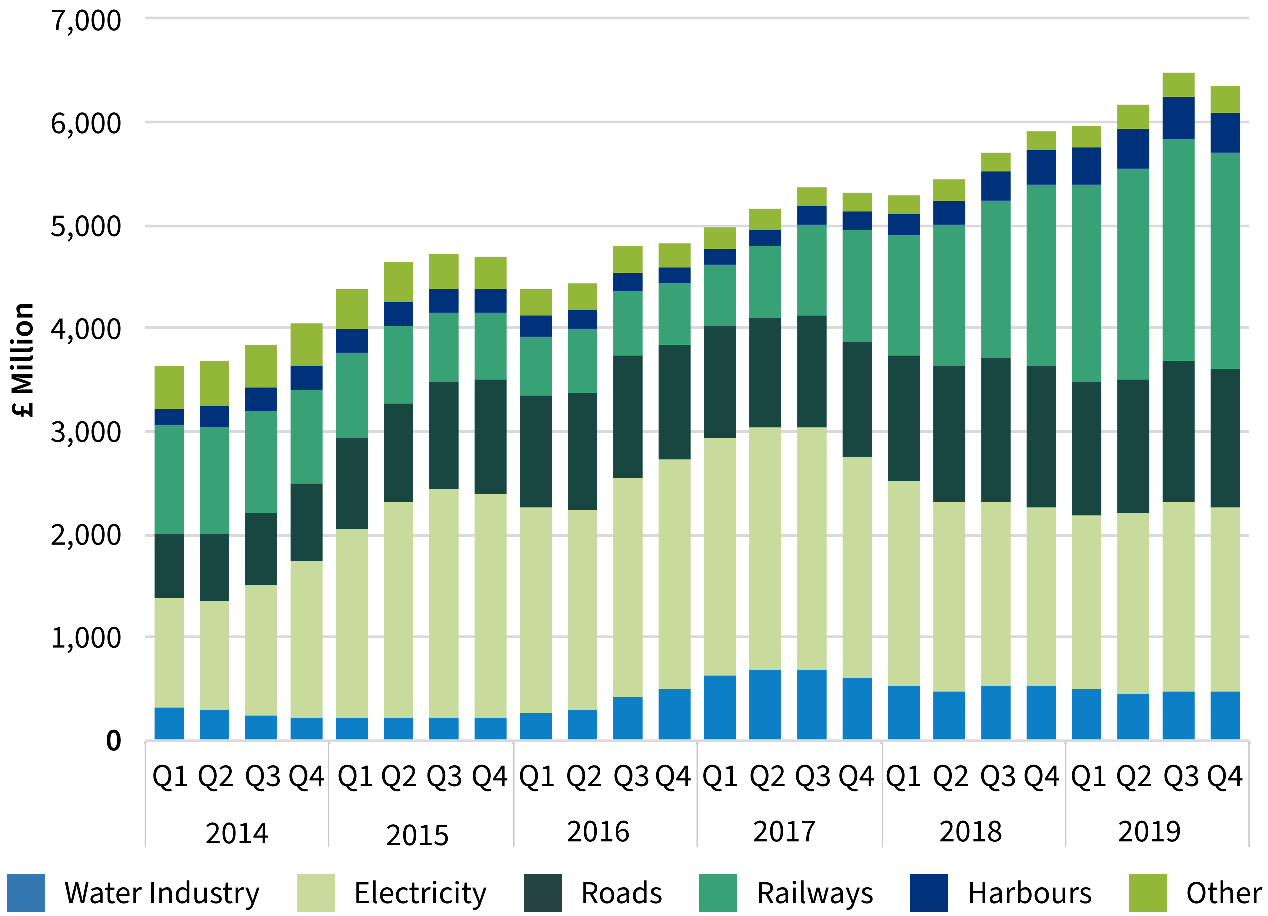
The sector grew sharply in 2019, with underlying starts rising by an estimated 27%. A further strengthening is anticipated beyond 2020 as road, rail and water industry investment programmes increase output.

The Government has pledged to significantly increase investment in the UK's infrastructure. In many areas such as energy and broadband, such investment will be delivered by the private sector. Public sector funding is potentially available in areas such as roads. The Government announced that the second Road Investment Strategy (RIS2) will spend over £27 billion between 2020 and 2025, taking forward schemes such as dualling the A66 Trans-Pennine route, and upgrading the A46 Newark bypass. These will take time to be 'shovel-ready', but may boost the sector towards the end of the forecast period.

Therefore, we anticipate that, initially, the additional funding increases will be directed at areas such as tackling the maintenance backlog on the nation's roads. A 50% increase to local road maintenance budgets in 2020-21 was announced as part of the Budget in March 2020.

Major projects make up a significant proportion of energy industry workload, with a current focus on major generation projects such as new gas-fired plants, Hinckley Point 'C' and off-shore wind farms.

Chart 13: Civil Engineering Output



Source: ONS

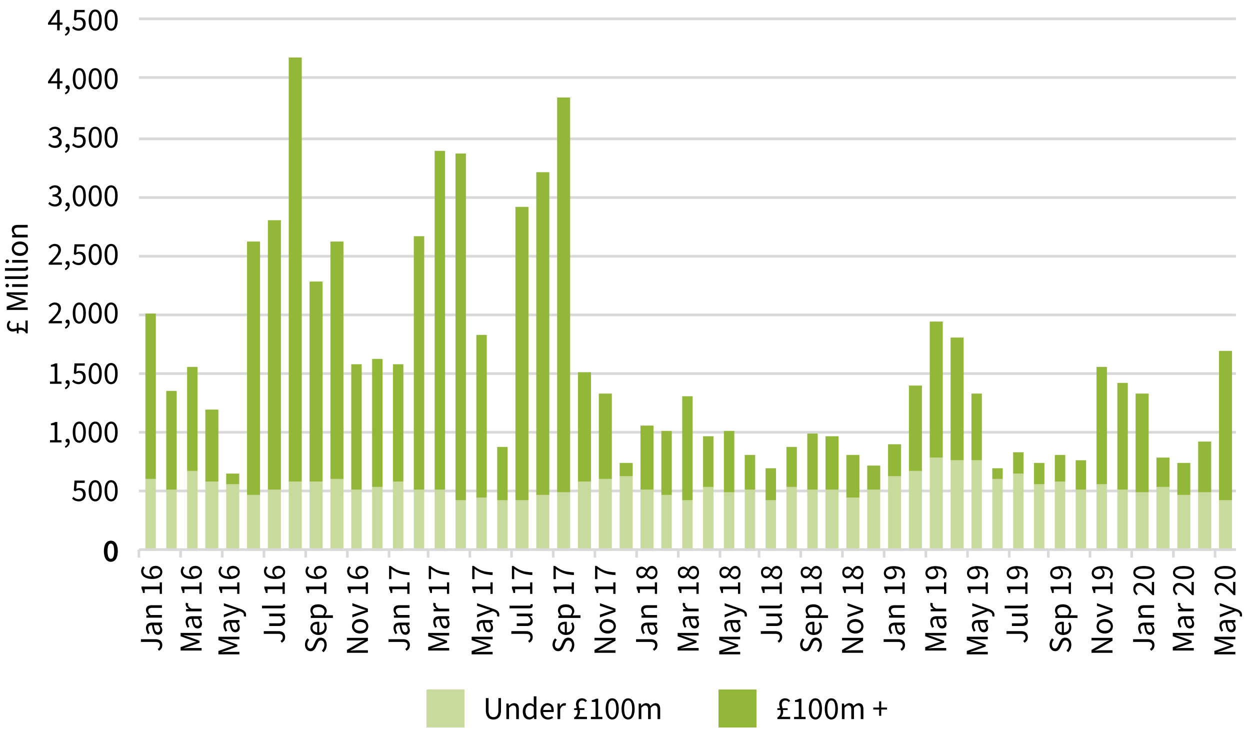
HS2 is now set to contribute to sector activity following receiving the go-ahead by the Oakervee Review. Contribution to sector output will be later than previously anticipated, however , the value of the overall development is likely to rise.

In addition, Network Rail's new five-year investment programme (CP6) is now underway. Within the programme £4.1 billion has been allocated for maintenance and renewal work during the current financial year, a 23% increase on 2018/19. A further 12% increase in spending is earmarked for 2020/21.

Increased investment in the national road network is anticipated as Highways England brings forward projects under its collaborative framework. Highways England has also been given the go-ahead to appoint a contractor for the Stonehenge Tunnel, with the tendering process running in tandem with the planning process. Construction is scheduled to start in 2021, although it will be vulnerable to delays in planning and tendering.

Water industry projects starting on site had fallen away during 2018 and 2019 as the current industry investment period (AMP6) ended. The new investment programme (AMP7) will start to lift industry spending from this year. In addition, sector activity will benefit from major work packages for the £4 billion Thames Tideway Tunnel.

Chart 14: Main Contracts Awarded for Civil Engineering



Source: Glenigan

Key Recommendations

FOCUS ON THE BEST PERFORMING SECTORS OF THE MARKET

The pattern of UK construction activity is being reshaped by the COVID-19 pandemic. As construction workloads are rebuilt over the next two years, the best performing sectors will differ from those prior to the outbreak. Increased government funding will drive growth in the education, health, civil engineering and community & amenity sectors. Structural changes are also expected to create new opportunities in warehousing & logistics, office refurbishment and the repurposing of redundant commercial premises. Regionally, construction markets in the northern half of the country are set to outperform London and the South East over the forecast period reflecting a shift in government funding.

Firms will need to target these new emerging opportunities, ensuring that they have the expertise and resources to increase their exposure to growing markets.

RISK MITIGATION

Turnover and cashflow will remain a concern over the remainder of 2020 as construction sites have to operate with fewer personnel. This will reduce the pace of site development, delaying stage payments from clients. Contractors and sub-contractors may wish to offset the lower monthly revenues generated per site by spreading their workforce across a greater number of projects.

A diversified client base will reduce exposure to any one client with a work pipeline spread more evenly over a larger number of customers. This can help reduce the business's exposure to a financial crisis or adverse change of payment by any one firm.

Supply chains should also be reviewed to ensure that firms are similarly not over-exposed to a few clients and to identify any potential interruption of product supply, especially from overseas sources due to COVID-19 pandemic or new trading arrangements for 1st January 2021.

WORK MORE EFFICIENTLY

Near term on-site working restrictions to contain COVID-19 transmission rates is exacerbating the need for the industry to use on-site labour more sparingly and effectively. With the UK's departure from the EU shrinking the pool of available skilled site labour, this will remain a priority as restrictions are eased over the next two years and firms seeks to expand their onsite workforce. This threatens to increase construction costs and disrupt the timely delivery of projects. Companies should invest in design solutions, site operating practices and offsite manufacturing options that reduce the reliance on site labour to safeguard the timely and profitable delivery of projects. In many cases this will involve the use of digital solutions to cut waste and accelerate design and construction processes.

EMBRACE DIGITAL SOLUTIONS

The pandemic has thrown a spotlight upon the benefits of digital systems as more traditional ways of working have been disrupted. Investment in an effective CRM, digital marketing channels and a modernised salesforce will help firms to rapidly identify and target emerging opportunities, sustain their workload, cutting the cost of winning work, improve efficiency and enhance profitability.

Do you need reliable insight and statistics to help you budget, forecast, realise size of market or penetration?

Do you need a better understanding of your competitor's activities, or would you like to see the trends shaping the future of construction?

Contact us today to discuss your strategic business requirements:

Call **0800 060 8698**

Email **info@glenigan.com**

Visit **www.glenigan.com**

80 Holdenhurst Road,
Bournemouth BH8 8AQ