

# UK MARKET VIEW

Small moves in the right direction



Q3 2024

## Introduction

---

Interest rate reductions, stable material costs and pay growth and the strength of the new government's mandate mean that the conditions for growing confidence and industry recovery are gradually being worked towards.

With the scale of change needed in the UK to meet ambitious housing targets, renew national infrastructure and deliver the changes promised at the ballot box, government, industry and the supply chain will need to collaborate closely and carefully as well as competitively. This will help to shift the dial on delivering at pace whilst managing the risks caused by legacy issues from recent years.

Private and public sector partners will need to work together to direct their focus towards their vision for the future, looking strategically beyond boundaries, attracting investment early and creating the platform for shared success through the delivery of long-term projects that will fix the foundations, transform existing towns and cities and help to create new ones.

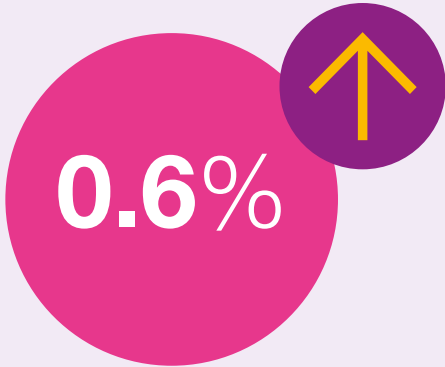


**Oliver North**

UK & Europe Director of Cost and Commercial  
Management, Consultancy

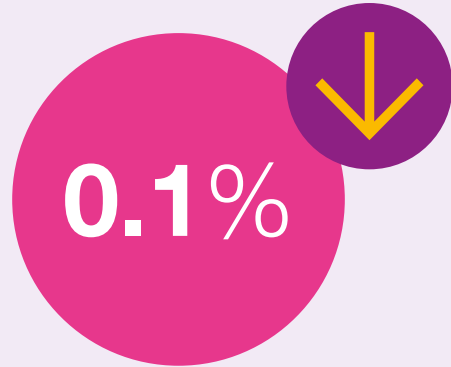
---

The economy had another good quarter, with GDP growing...



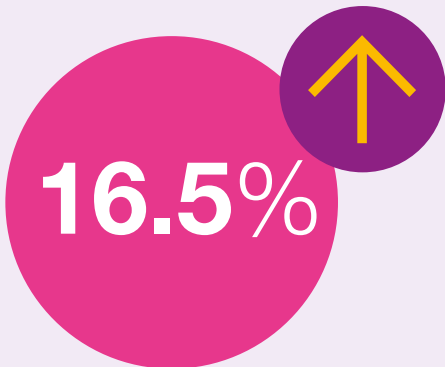
in Q2.

Wider economic strength wasn't shared by construction. With output declining...



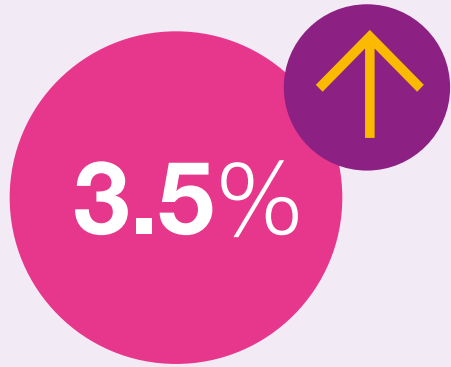
this is the third consecutive quarter in a row that the sector has shrunk.

New orders increased by...



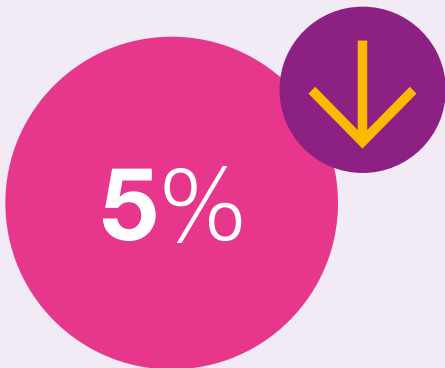
and, as with all sectors having a better quarter than Q2 2023, confidence looks like it is starting to return.

Cost pressures remain modest and, while construction pay grew relatively strongly in the second quarter, its annual growth rate of...



is much weaker than that seen across the wider economy.

The Bank of England Monetary Policy Committee cut interest rates to...



in August but held them in September – further cuts are anticipated in the coming months.

## Tender prices

	2024	2025	2026	2027	2028
National	2.5%	3.0%	3.0%	3.5%	4.0%
London	2.0%	2.5%	3.0%	3.5%	4.0%

The table gives our current tender price inflation forecast. The figures should be treated as averages and there will always be variations due to procurement methods, project type and local factors.

## Setting the scene

The UK economy is slowly turning the corner, with conditions steadily improving. Backing up growth of 0.7% in Q1, GDP grew 0.6% in Q2, and the minor technical recession that happened at the end of 2023 is now a long way behind us. Nonetheless, the strength of the first half of the year shouldn't be over-stated. The shine from GDP comes off quickly when looking at GDP per capita which, despite growing 0.3% in the second quarter, is 0.1% lower than it was 12 months ago.

Similarly, growth seems limited to business facing services. Manufacturing, construction, and consumer facing services all saw output decline in the second quarter. Given real incomes have been rising rapidly, the fall in consumer facing services is disappointing. If the economy is to continue to see robust growth in the second half of the year, consumers will have to play a more significant role.

The most important change over the past three months is we now have a new government. Part of this report looks at how we might assess the Labour government, and the early signs are mixed. While it is encouraging to see ambitious plans around housing, and a recognition that the National Planning Policy Framework (NPPF) must change, there is concern that the government is either cancelling or reviewing several infrastructure projects given their potential to spark industry and economic recovery. Clearly, it is still very early days, but the fact that infrastructure output is 10.5% lower than it was a year ago is likely, in large part, due to 2023 being very poor for public infrastructure new orders. The new government has set out a context of facilitating delivery and output growth, not necessarily funding it directly but creating the conditions to attract inward investment from the private sector, international funds and other sources.

Despite happening a little later than hoped, a second important change was the decision by the Bank of England Monetary Policy Committee to vote in favour of an interest rate cut in August. While not enough to truly stimulate the construction industry, it is a move in the right direction. Whether they cut once or twice more this year and, similarly, how far they go in 2025, will be among the most important drivers behind growth in the industry over the next couple of years. Monetary policy acts with a lag, and even if there were swifter cuts, developers wouldn't act immediately. As it is, with the Bank of England only cutting rates cautiously and incrementally, the upwards trend for the construction industry will be a gradual one.

One area that will hopefully push up tender prices over the next couple of years is the large volume of projects currently at pre-construction stage. Getting these projects through, firstly to the construction contract to boost new orders, and then onto site and pushing up output, will support tender price growth. That many projects are seemingly taking time to pass through the pre-construction stage in part indicates pent-up demand and a level of cautiousness from clients. As we've seen in the recent situation with ISG filing for administration, there are also still a range of legacy challenges working their way through the industry. Unfortunately, this will heighten uncertainty and will apply further pressure across supply chains – posing added risk to delivery. The hope is, that as interest rates fall and confidence in the UK economy improves, key projects will get the green light and support a recovery in construction output. This will need to unfold over an extended period before it mitigates the impact of recent industry events. Events which once again highlight the underlying fragility of a sector beset by low margins.

We believe that tender price growth will be modest this year, slowly accelerating over the forecast period. A pick-up in construction output, supported by loosening monetary policy, helps explain part of this acceleration as confidence grows. The pace of output growth will also be determined by fiscal policy. Here, the early impression from the government means upside risks to the forecasts. While the government is saying it wants more construction, the £22bn deficit in public finances raises questions over deliverability. Looser fiscal policy such as through road and rail spending as well on new schools and hospitals or the successful delivery of 1.5 million homes would lead to higher tender price inflation.

On the cost side, both labour and material prices have seen solid increases over the past three months, but in neither case is there much to immediately worry about. Material prices rose 0.8% on the quarter but, more recently, several key commodity prices have weakened. Notably, oil prices have sunk to their lowest level in over a year. Additionally, a lack of demand from China has led to falling iron and copper prices. Meanwhile, construction's labour costs had a surprisingly strong showing in the second quarter. Regular pay rose 1.9%, helping lift the annual rate of growth to 3.5%, the highest it has been this year. Overall, with output still facing headwinds, it is difficult to see cost pressures gain momentum through the end of this year and into early 2025.

# Output still falling, but surging new orders give hope of recovery

## Construction output

For the third quarter in a row, construction output shrank. Even though the drop of 0.1% in the second quarter was minimal, and not as bad as the falls in the previous two quarters, the industry is now 1% smaller than in Q2 2023. Once again, it was new work that suffered, down 0.5% in Q2, leaving it 6.4% lower than a year ago.

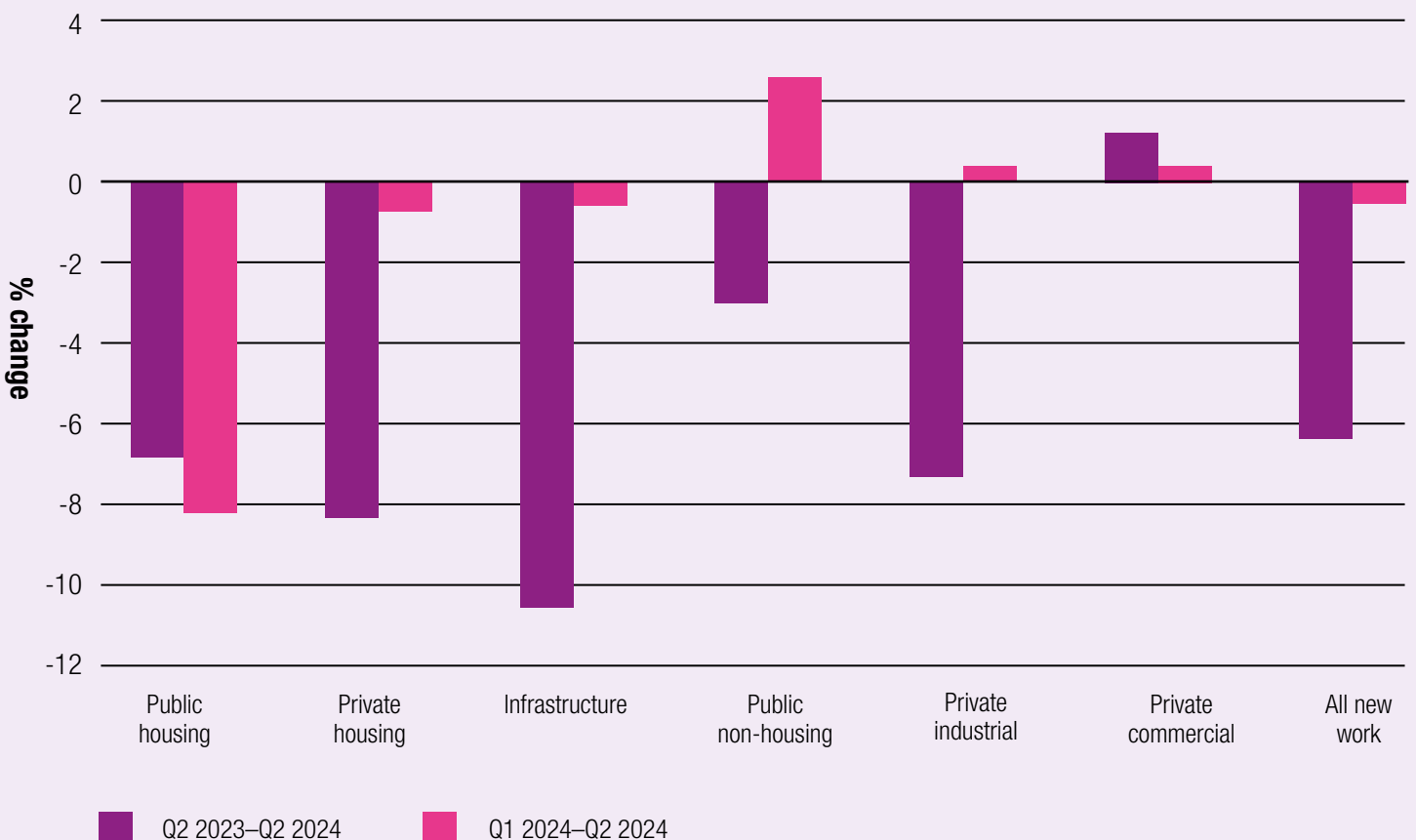
Within all new work, the challenges over the past 12 months have been widespread. Infrastructure output has fallen 10.5%, including a 0.6% drop in the latest quarter, and last year's reduction in new orders coupled with stalled starts and other factors is now damaging output. Second worst is private housing, declining 8.4% over the year; having enjoyed growth of 3.2% in Q1, output fell again in Q2. It will take time, and likely several more moves by the Bank of England, before conditions become noticeably more favourable. That Q1 was

another very poor quarter for housing starts suggests any sizeable turnaround won't take place until next year at the earliest.

The one sector that has seen growth in the past 12 months is private commercial which has been driven by a range of factors including office and estate transformation and rationalisation. However, an increase of 1.1% is nothing to shout about and the sector is still over 25% below the level seen in Q4 2019, before the pandemic. One of the biggest challenges facing private commercial has been falling real wages and a lack of consumer confidence. With these now on the up, parts of commercial such as entertainment and retail should follow suit. There were some signs of this happening in the latest new orders numbers, and with offices also growing, by next year, the sector's slow recovery may have quickened.

## OUTPUT FALLS AGAIN

Source: ONS



### New orders

There was another robust increase in new orders in the second quarter. Growing by around 17% for the second successive quarter, new orders rose to their highest level since Q4 2022. This suggests that the industry may have finally turned a corner, with emerging policy from the new government plus lower interest rates providing further support and renewed confidence here. Nevertheless, after such a difficult 2023, any rebound in output growth will be slow. The sum of new orders in the most recent four quarters is noticeably lower than it was in the four quarters to Q2 2023 and, for a number of sectors, the previous steep declines experienced will not be easy to recover from.

Other than public new housing, which is small and volatile, the fastest growing sector in Q2 was infrastructure. Concerns are already being raised about what the Labour government will commit to, but for the time being, and coming from a low base, infrastructure rose by 23%, with healthy increases in its two largest sectors: electricity and roads. Unlike many figures the ONS publish, data on new orders are not revised and historical data does not change even when projects are cancelled. Furthermore, as the latest numbers only reflect what happened between March and June, even if some of the recently announced cancellations were to alter the figures, the changes would not be seen here.

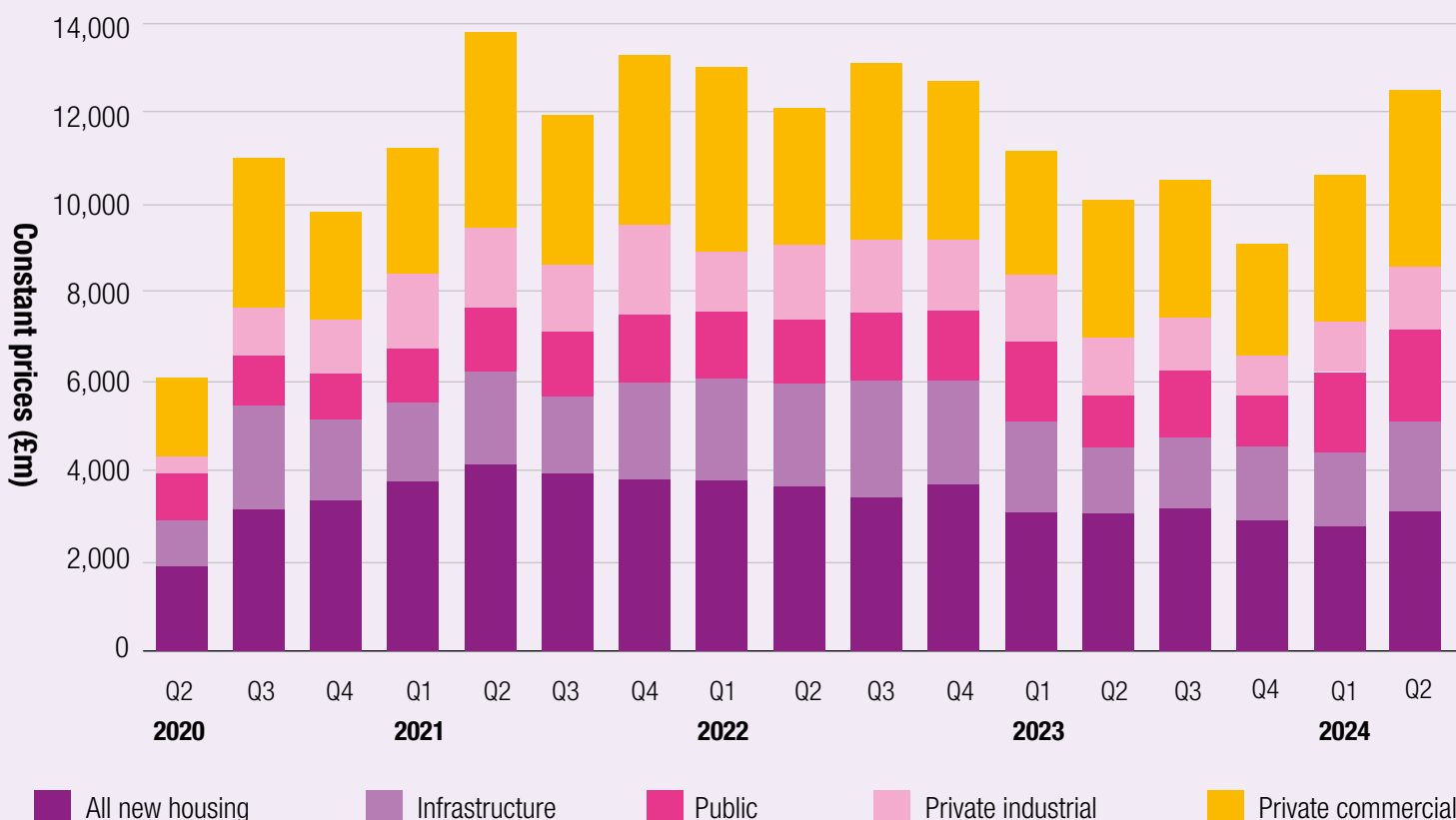
New orders are the best indicator for what will happen to construction output, but the relationship is far from perfect.

Often in the lead-up to an election, spending decisions are pushed back, however, in Q2 the majority of infrastructure's growth came from government spending. The non-housing public sector has also fared well recently and while the non-housing public sector's increase in Q2 was only modest, there was strong growth in Q1. On a rolling four-quarter basis, the sector is almost 8% larger than at this point last year, with the latest four quarters being its best since before the pandemic. In part, this shows how poorly the sector has performed recently.

As we discuss in the next section, there are big questions about what the new government will bring and how it plans to deal with the need to curb spending while fostering stability and growth.

### NEW ORDERS CONTINUE TO RISE

Source: ONS




## Costs

The third quarter saw regular construction pay increase 1.9%, which helped push the annual growth rate up from 2.7% to 3.5%. While this is the fastest the annual rate has risen this year, it is much lower than in any other sector covered by the ONS. Earnings across the whole economy are 5.4% higher than last year, and with construction output dropping over this time, it is easy to see the reason for the sector's relatively weak pay growth and having levelled out earlier than other industries. In the short-term, rising construction vacancies in the past quarter may provide some further impetus to pay. Weak demand, however, will continue to offset this. Further ahead, as output recovers, challenges around skills shortages pose one of the biggest structural risks to the sector. Becoming more productive would go a long way to solving this, but for many years significant productivity gains have proved elusive.

One factor helping slow pay growth, is cooling inflation. In May, the Consumer Prices Index (CPI) had eased to 2% –the Bank of England's target rate – and although it has since had a small rebound, likely ending the year around 2.5%, it is no longer the driving force in wage negotiations that it was in the months following inflation's peak of 11.1%. Since the global financial

crisis, real wage growth above 2% has been rare and, with it currently standing at 2.4% as well as supporting the economy through higher consumer spending, it has probably peaked. Expectations are that pay growth will continue to gradually come down and the Bank of England will be monitoring upcoming data releases closely. If the growth rate comes down faster than expected, it will give the MPC greater scope to cut interest rates, whereas if it remains stubbornly high, rate cuts may not come as quickly and by as much as the construction industry would like.

Within the basket of goods and services that the CPI looks at, there is a clear divergence between goods and services. Goods are falling, whereas services are rising. This difference is important when thinking about construction materials as, unsurprisingly, they move much more closely to the goods category. The 'all work construction material price index' is 0.9% lower than a year ago and over 5% down from the peak in 2022. While prices have risen since the end of last year, in Q2 2024 they were barely higher than in Q4 2023; this should mean contractors aren't experiencing any significant pressures. Recent S&P Global UK Construction PMI surveys also indicate this, with healthy stocks and shortening lead times.



**While prices have risen since the end of last year, in Q2 2024 they were barely higher than in Q4 2023; this should mean contractors aren't experiencing any significant pressures, shortening lead times.**

## What success could look like for the new government

There are many economic indicators and metrics from which one can benchmark the success of a government. Most obvious are GDP and GDP per capita. Last year's recession, as well as a string of quarters where GDP per capita fell, surely contributed to the Conservative Party's defeat. Other key figures, all of which have been poor recently and which the new Labour government will hope to see noticeable improvements on, are foreign direct investment, real wages and NHS waiting lists.

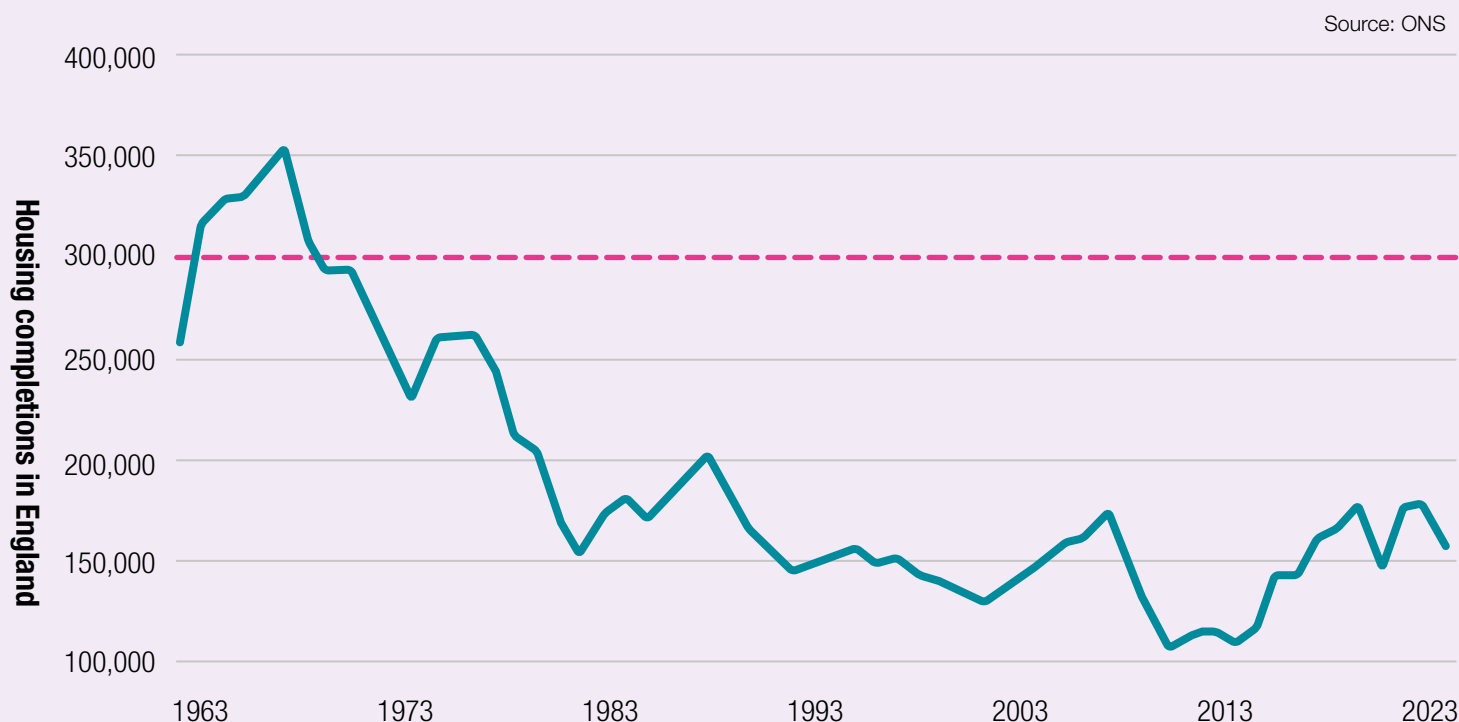
Such familiar indicators are likely to help determine Labour's chances of re-election in five years' time, but there are also more construction-focused statistics which we can analyse and use to measure success. However, this will be a two-way street and the government will also be dependent on the industry in meeting its goals and so, while government can help create the environment necessary to achieve them, it is also down to the industry to deliver the desired growth.

Housebuilding will always be a key metric upon which the government is judged. Angela Rayner, the new Deputy Prime Minister and Secretary of State for Housing, Communities and Local Government has

announced ambitious plans to build 1.5 million homes over the next five years. Starting with an update to the planning system, changes include new mandatory targets for councils in England. Revisions to the Green Belt system and new flexibilities around affordable homes, plus the creation of a taskforce looking into developing a programme of new towns, each with at least 10,000 homes, have set a progressive tone, but the government recognises this is a first step and that multiple solutions are needed to address the complex challenges of increasing the supply of new homes.

While such policies are welcome, delivering 1.5 million homes involves a huge expansion in the market as the following chart shows. The last time 300,000 homes were built in a year in England, Harold Wilson was Prime Minister and The Beatles were still together (1969) - recent years have seen far fewer completions. The new mandatory targets show how widespread the problem is. Of approximately 300 local authorities, only 37 saw their new homes target met on average over the past three years - with slightly fewer hitting the previous target. Even accounting for Covid 19, that a little over 10% of local authorities have seen the homes needed being built in recent years underlines the scale of the challenge.

### HOUSING COMPLETIONS ARE A LONG WAY FROM 300,000





It is also worth discussing the wider regional implications of the new method. Notably, London is the only region where there has been a cut to the housing target. Yet for the capital, having averaged fewer than 40,000 new homes a year against a previous target of almost 100,000, even the new target of around 80,000 requires more growth than any other region. The region requiring the second largest scaling-up in order to reach the new target from current net additions is the South-East, but with no English region having hit their updated targets, inflationary pressures will be widespread.

Data from the past three quarters shows a considerable drop-off in housing starts, meaning the starting position for building 1.5 million homes in five years is, on the surface at least, considerably behind the line. A multi-layered approach to increasing delivery is the best opportunity for realising these ambitions.

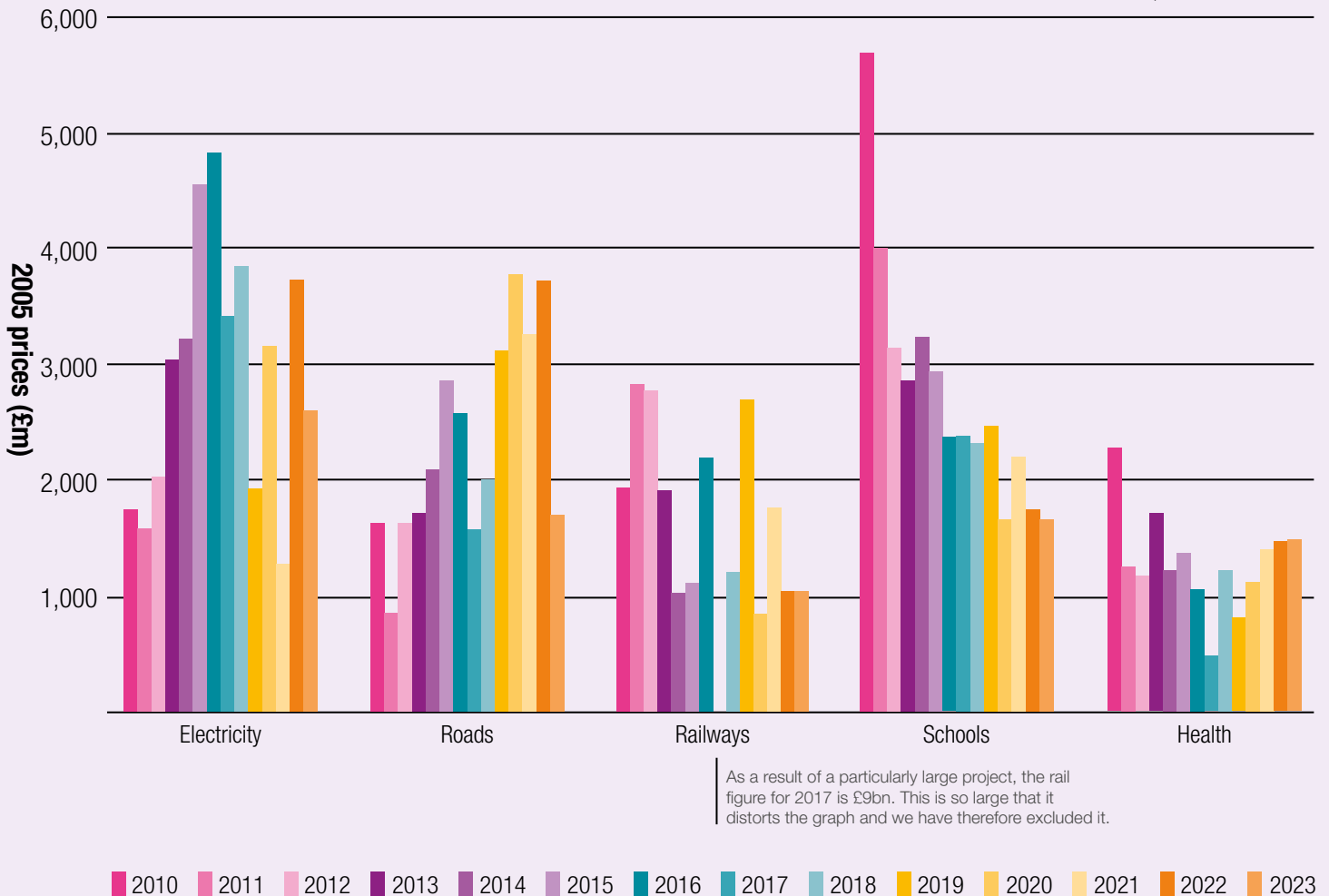
Even a slightly more realistic aim of 300,000 homes being completed in 2029 will only come about if there are wholesale changes to the way the market operates. One such change could be an increase in modular housing, but unfortunately the past few years have

seen a number of firms fail and this sector won't be the source of an immediate solution. Another change is greater institutional investment, and here more certainty around planning helps make the market more attractive. Joint ventures and greater collaboration between the public sector and developers will also help, although housebuilders will continue to face constraints on how much they can deliver. However, getting Britain building homes again is unlikely to cause house prices to fall; a recent article by The Economist suggests bringing down prices would need a much greater, and more sustained increase in housing supply to achieve this.

Another dataset serving as a proxy for government performance in our industry is new orders. New orders show the value of new construction work awarded to main contractors and are the best forward-looking indicator for construction output available. Data also comes at a more granular level than construction output and, while hopes are that total spending on infrastructure and the public sector will rise, knowing which components are seeing growth will be important.

## INFRASTRUCTURE AND PUBLIC SPENDING NEED TO INCREASE

Source: ONS, Mace Calculations



For a number of sectors, the 14 years of Conservative government saw a noticeable drop in capital expenditure and, alongside specific challenges such as RAAC and overcrowded prisons, a rebound in spending is essential, although the £22bn black hole in public finances suggests government will be under significant constraints. Alongside the government, the private sector will be the main backer for some sectors, in particular utilities (energy and water) and infrastructure. As well as funding projects, the new government must therefore set the conditions to encourage such investment with covenants that avoid the pitfalls of past initiatives such as PFI so that value for money for the public purse is built in.

In contrast to housing, the early government announcements regarding public-sector-funded construction projects were more disappointing. In explaining the public spending position that Labour has inherited, new Chancellor Rachel Reeves announced the cancellation of several transport projects and said there would be a review of the New Hospitals Programme. While the focus of the speech was on a £22bn overspend by the previous government, manifesto pledges had already

showed Labour would be operating under tight fiscal constraints. Just how constrained the government will be, will only become clear next year. A Budget will take place in October, with a Spending Review which sets out departmental budgets for at least the next three years due in Spring 2025. Unfortunately for construction, the initial signs are that there won't be the sort of increase in budgets that would be hoped for.

More promisingly, and likely to be one of the biggest growth areas over the next five years will be electricity. Decarbonising the economy requires significant infrastructure changes, with green energy, such as solar, wind and nuclear, having to replace fossil fuels such as gas. Replacing internal combustion vehicles with electric and hydrogen powered ones, alongside strong growth from data centres, will also increase demand for electricity. Much of this expenditure will come from the private sector.

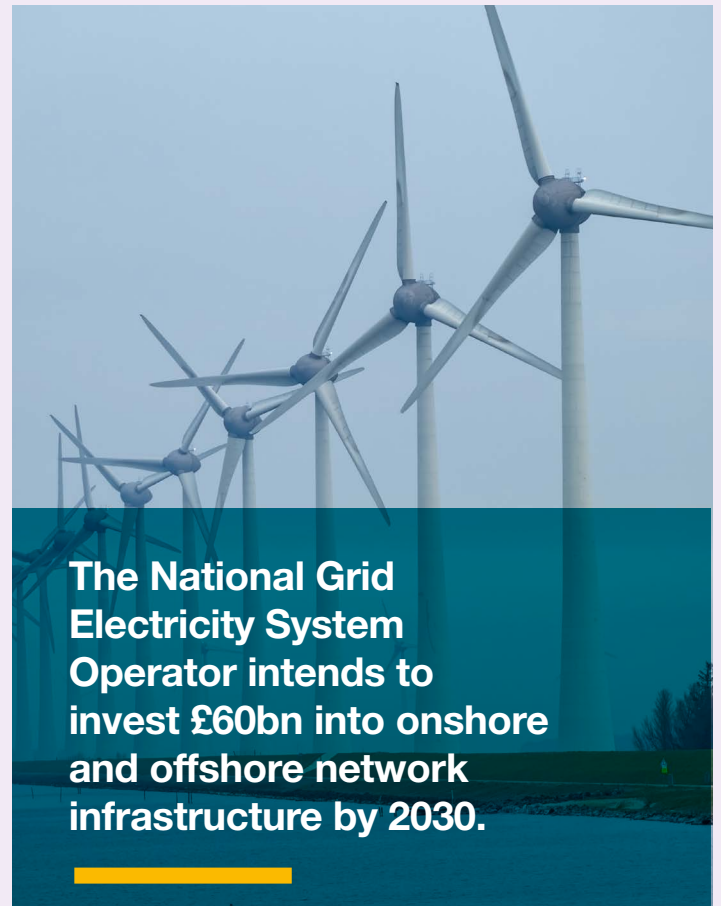
One such example is the National Grid Electricity System Operator which intends to invest £60bn into onshore and offshore network infrastructure by 2030.



**One of the biggest growth areas over the next five years will be electricity. Decarbonising the economy requires significant infrastructure changes.**

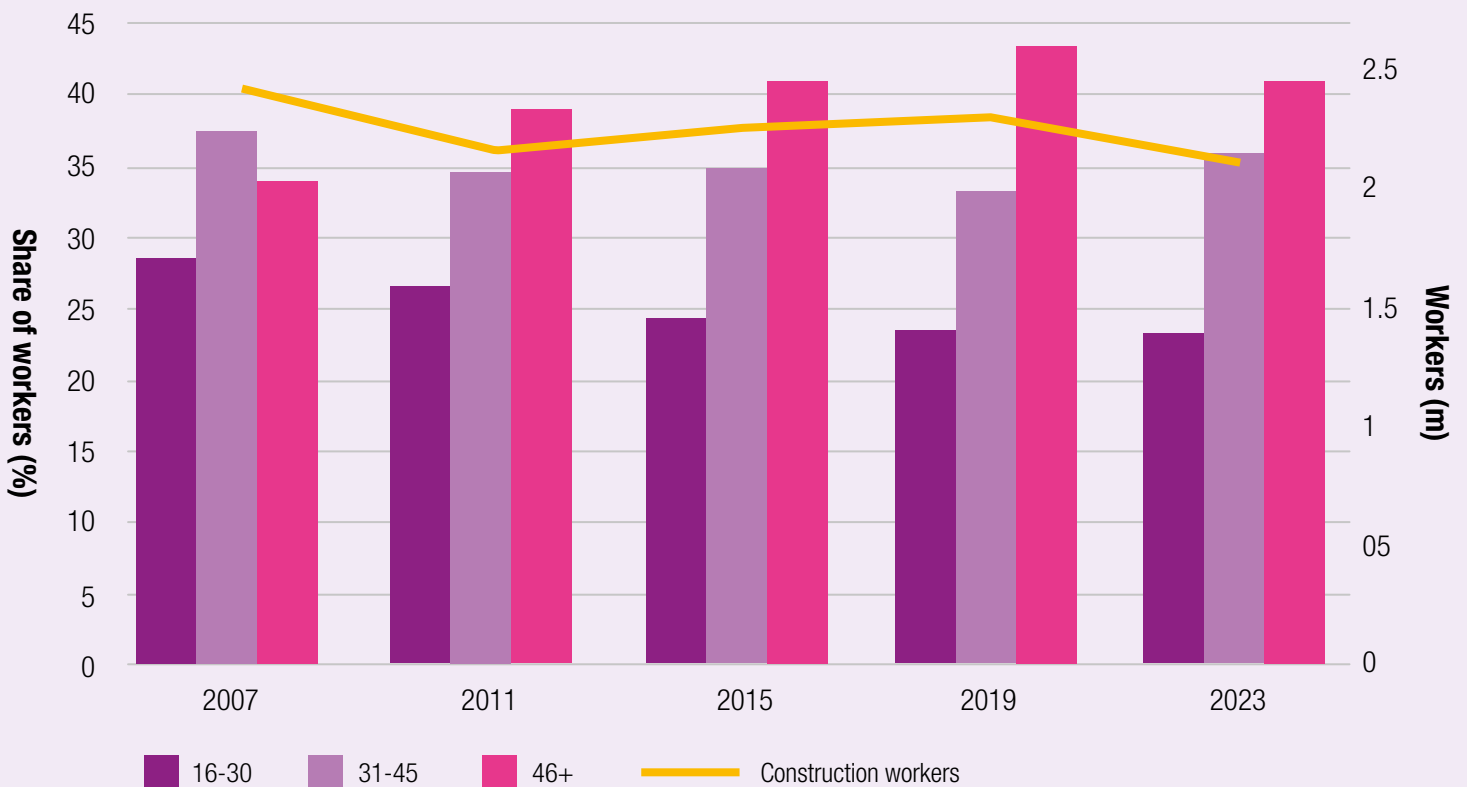
However, it is also dependent on the government creating the opportunity for such investment, and changing regulations might be easier than providing new funding. The first major public decision by Ed Miliband, the Energy Security and Net-Zero Secretary, was to approve three large solar farms. Potentially more important than the infrastructure itself will be the confidence developers get from this decision, making it more likely that they will look to bring forward similar projects.

Crucial to the success of both housing and infrastructure will be employment and, in particular, encouraging younger workers into the industry. Without expanding the workforce, increasing the number of houses built by over 50%, as well as delivering all the infrastructure schemes planned will not be possible. Made harder by many other countries also having considerable infrastructure plans, achieving this will mainly be dependent on the industry but, as with other supply-side changes, the government also has a role to play. The following graph shows how the number of people working in construction has hovered at a little above 2 million for the past decade. More worryingly, it shows how the share of workers under 30 has slipped considerably since just before the global financial crisis. At the same time, the share of workers aged over 46 has increased.



### FALLING SHARE OF YOUNGER WORKERS

Source: UK Data Service, ONS



The first area where the government could act is in supporting younger workers into the industry. Data from 2022 and 2023 showed a noticeable drop in the number of apprentices starting. The Labour manifesto mentioned the party would bring “forward a comprehensive strategy for post-16 education, while also guaranteeing training, an apprenticeship, or help to find work for all 18 to 21 year-olds.” How this looks in practice remains to be seen but, given how long it can take for such changes to be felt in the labour market, speed is of the essence. Developing inclusivity further, making the industry more attractive across genders, diverse ethnic backgrounds, disability (whether hidden or visible) and more would further the progress being made towards making construction an industry for everyone and would reap rewards.

Even with improvement in these areas, it is unlikely to be enough to grow the workforce by the scale necessary to deliver some of the more ambitious targets, particularly in the next five years. Therefore, a second area which the government might need to investigate is around immigrant labour. A contentious issue, and one which has become increasingly politically charged since the EU referendum, but

Brexit has not helped address the skills shortages that employers already find prevalent - this will only worsen if the workforce size doesn't increase. While highlighting skills shortages and an ageing workforce presents nothing new to keen observers, the targets that the government has laid out will be impossible to meet without pulling on a range of policy levers, including measures to create the conditions needed to support technical training and supply chain growth, to reach a remedy.



**Making the industry more attractive across genders, diverse ethnic backgrounds and different abilities would help to make construction an industry for everyone and would reap rewards.**

## How much of a problem is a lack of competition?

From a tender price perspective, the effect of too much or too little competition is much harder to measure than higher wages or material costs. Even so, like other metrics measured on sentiment driven by supply, demand and wider market conditions such as pipeline and risk attitude, it is still important in a highly competitive sector like construction. Cases such as steel price shocks are easy to understand (if not manage) from all parts of the supply chain. By contrast, if a lack of competition is pushing up prices, it can undermine clarity, trust and collaboration and impact deliverability.

For the London market, major competition concerns exist around major industry players exiting the UK market, contractor insolvency, particularly ISG entering administration and risk aversion from M&E firms. The decision by Australian firm Lendlease to sell its UK arm, partly attributable to cost escalations and low profitability, has left its clients and those looking for Tier 1 contractors capable of delivering the largest schemes in London in an uncertain position. As one of only a handful of firms with the capacity to work on such projects, less certainty about the competition in this market could risk leaving large-scale developers with fewer choices.

ISG entering administration is a sad loss to the industry. As well as the human cost, that a £2bn business servicing significant private and public projects will send shock-waves across the industry. This underscores some of the challenges faced by the industry when combining risks posed by fixed cost contracts and low margins. To a supply chain already experiencing stretch this will, for some, only make matters worse. That ISG's sister company, ESS Modular has already followed ISG into administration shows not only the immediate effect on the supply chain, but also how modular firms continue to struggle. While it's sometimes suggested that modular offers a way of avoiding some of the problems that traditional construction firms such as ISG face, that so many have struggled in recent years indicates MMC is still a long way from being the desired panacea.

Over the medium to long term renewed competition could emerge from these changes, encouraging contractors who don't typically bid for the biggest and most complex schemes to enter the market. For the moment though, the change in competition could mean those currently at the necessary size could become more selective.

Lower down in the supply chain, selectiveness and risk-aversion are commonly being seen from M&E firms. Even before last year's failure of MJ Lonsdale this sector only had a handful of large firms, and MJL's collapse meant that those left are more able to pick and choose the jobs they work on, as well as increase their prices. Further strengthening M&E firms' collective hands are the growing market for data centres and changing requirements due to the net-zero push. This underscores that competition is, in part, a function of market size and, when output is growing, a lack of competition becomes more evident.

While specific insolvencies grab the headlines, figures from the Insolvency Service show that Q2 was another incredibly problematic one for construction. Disappointingly, insolvencies rose again during Q2 – following a promising first quarter where the number of insolvencies was at its lowest for two years. That the challenges besetting the industry are persisting means our previous advice about the necessity of considered procurement and due diligence on the supply chain remains relevant. Similarly, clients must be responsible and treat the supply chain fairly.

In England and Wales, construction firms went insolvent at a faster rate than the all-sector average in the first half of the year. In the first half of 2024, around 0.6% of construction firms have failed, compared to 0.5% of firms across all sectors. The impact is, therefore, likely to be that in certain pockets of the industry, or in parts of some supply chains, a noticeable reduction in competition will be experienced. In the most noticeable cases it is likely that the market was already suffering from a lack of competition – one or two firms failing amplifies this.

Another competition-related talking point from earlier in the year was the Competition and Markets Authority's (CMA) report on the housebuilding market in Great Britain. Investigating the reasons for the under-delivery of new homes, the main one reported was planning. Unpredictable, time consuming, costly and complex – the planning system was described as all of these and as hindering the number of permissions given. The CMA also found that a lack of competition isn't the main reason for not enough homes being built, while the eleven largest firms built two-fifths of new homes, there are thousands of smaller firms who build 1,000 homes or less per year.

## Is competition bringing it back home?

It is also interesting to link the competition report to the question about whether it is possible to build 1.5 million homes over the next five years, and here the findings are not promising. The CMA suggests that housebuilders build at a slower pace than they could, instead building at a rate that balance local market absorption rates with pricing strategies. In building at the local absorption rate, the developer doesn't have to discount aggressively to sell new homes.

Alongside planning problems which slow the build-out rate another recommendation to help reduce the absorption issue is increasing the amount of non-speculative building. Institutional investment in build-to-rent is one part of this but, short of the government or local government building homes at volume again, it is difficult to see how it will be possible to meet the volume of new homes desired. Housebuilders will always be motivated by profit and so the absorption rate, and build-out rates being pitched to support value will drive the number of homes built.

We expect these conditions to prevail – at least until the range of policy interventions being introduced to catalyse planning approvals, work across strategic boundaries and release land take effect.

As touched upon earlier in this report, government has set out an ambitious programme for new homes delivery at a time when much of the housing sector has stalled. Partly due to market fundamentals and

managing sales risk, housebuilders are also having to deal with impairments and remediate or improve existing stock, a position which will take time to turn around. Delivering new homes effectively can offer both public and private developers an exceptional return on investment and, more widely, will deliver a boost to the economy and so creating the conditions for confidence and an increase in the appetite to build are a top government priority.

Ambitious targets to meet the pan-generational challenge of increasing new housing supply will help to deliver focus on both the scale of the challenge and the size of opportunity it presents. As the new government's agenda to deliver new towns (backed by both public and private investment, domestic and overseas) gains momentum, working with a range of developers across the tenure mix will help to de-risk and drive these projects forward.

This will require collaborative partnering amongst competitors, with developers 'thinking beyond the red line' on their site plans to deliver in carefully sequenced phases which deliver revenue streams that can sustain present and future delivery while achieving the pace required. Having the right infrastructure and amenities planned or in place, particularly around transport hubs, will be key to unlocking the potential of these collaborations in delivering on the vision for these new town masterplans and working towards housebuilding targets.



**Delivering new homes effectively can offer both public and private developers an exceptional return on investment and, more widely, deliver a boost to the economy.**

---

**Mace**

155 Moorgate  
London EC2M 6XB  
+44 (0)20 3522 3000

**Contacts**

Oliver North [oliver.north@macegroup.com](mailto:oliver.north@macegroup.com)  
James Donald [james.donald@macegroup.com](mailto:james.donald@macegroup.com)

**[macegroup.com](http://macegroup.com)**