Construction update Spring 2022

Sector overview

2021/2022 construction activity continues to power ahead despite the stormy clouds that gather over the supply chain. Cost inflation looks set to stay as construction companies continue to grapple with the unique challenges that the UK construction market presents. New work is there to be won, but at what cost is the question that many construction businesses face an uncertain answer to. It is also important to note that UK construction insolvencies are increasing following the retraction of Government backed Covid-19 initiatives.

Economic Data

- **ONS Data:** UK Construction output increased by 12.7% in 2021 following a 14.9% decline in 2020.
- **IHS Markit/ CIPS UK:** A score of 59.1 was posted in February 2022.
- **The Gazette:** In 2021, construction sector insolvencies increase by 25% to 2,579. This accounts for almost one in five (19%) of all insolvencies in England and Wales.
- **CPA:** UK Construction growth of 4.3% is forecast in 2021, slowing to 2.5% in 2023.

Notable Insolvency Events

- **P.D.R. Construction Ltd** (January) – Contractor, £83m t/o
- **Beaumont Morgan Developments Ltd** (January) – Contractor, £47m t/o
- **Midas Group Ltd** (January) – Contractor, £292m t/o
- **Kace Holdings Ltd** (February) – Facade specialist, £14m t/o
- **Mulbury Homes Ltd** (February) – Property developer, £38m t/o
- **Caledonian Modular** (March) – Contractor/ Modular specialist, £45m t/o
- **Roadbridge UK Ltd (March)** – Civil Engineering Contractor, £96m t/o

Made possible

Strengths – Regional spotlight

> **Manchester:** Construction activity remained resilient throughout the pandemic with the regional levelling up agenda expected to unlock further funding and opportunities throughout 2022 and beyond.

> **Leeds:** 2021 was a record-breaking year of construction activity for this city (22 new starts) – Momentum will remain strong for Leeds as they prepare for the Year of Culture 2023.

> **Birmingham:** New scheme starts nearly doubled from 10 in 2020 to 18 in 2021, with 2022 set to be the year that construction activity will shine in this city as they prepare for the 2022 Commonwealth Games.

> **UK Infrastructure:** Expected to be the main driver of construction growth in 2022 with a 9.7% rise in output forecast (CPA). Key projects include the Thames Tideway Tunnel, Hinkley Point C and HS2.

Challenges

> **Supply Chain issues:** The biggest threat to overall construction growth. Material, product, skilled labour, and HGV driver availability remains challenging, coupled with import complexities. Smaller sub-contractors with less supply chain leverage are expected to feel the most pressure.

> **Hyperinflation:** Construction material prices are forecast to increase by 18.5% in 2022 (UK CMPI) as the perfect storm of supply shortages attempt to support heightened construction demand. Inflation concerns have further been exacerbated by the Russian invasion of the Ukraine which is set to see energy, fuel and selective raw material prices rocket.

> **Red Diesel:** Lobbying to suspend the removal of the construction industry's red diesel rebate in April 2022 continue. When the 11.14ppl tax cap is removed, construction companies will pay a standard rate of 57.95ppl which could cost the industry between £280m and £490m per year.

Underwriting Approach

> **Stable underwriting stance in place for construction with closer emphasis on smaller sub-contractors:** Case-by-case underwriting approach with each business to be assessed on their own individual financial merits.

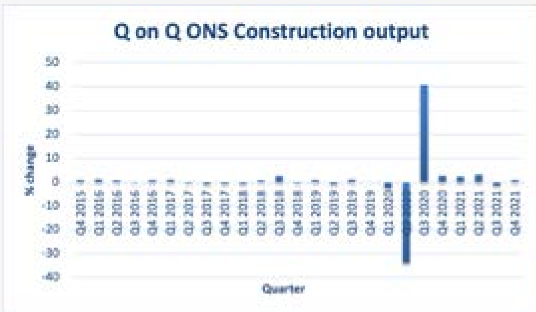
> **Information remains key:** Up to date financials, order books, bank forms and covenant visibility remains important when assessing credit risk in construction.

Q4 2021 ONS construction output

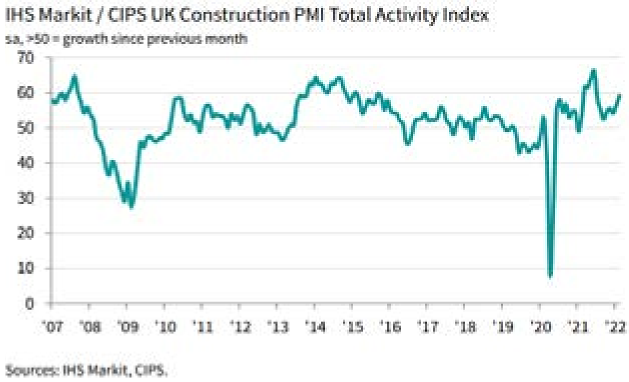
Q4 2021 quarterly construction output increased by 1% compared to Q3 2021. Nearly all sub-sectors saw an increase in Q4, the largest contributors of which were public other (8.7%), private industrial (4.9%) and private commercial work (2.1%). Total construction new orders increased by 9.2% quarter-on-quarter, which means new orders are now higher than pre-pandemic levels.

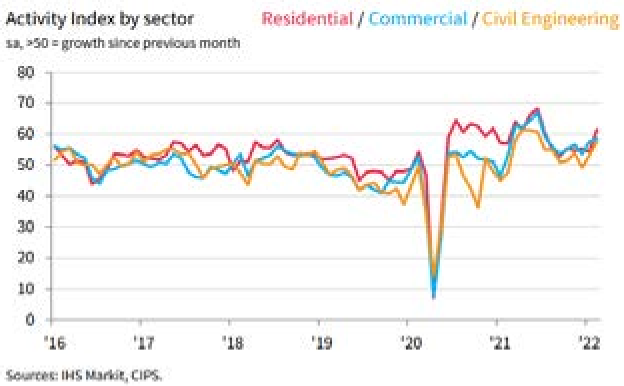
The 2021 annualised rate of construction output increased by 12.7% in 2021 when compared to 2020 which is the largest increase since records began (1997). This follows the pandemic led record fall in construction output of 14.9% in 2020. Anecdotal evidence suggests infrastructure projects such as HS2, motorway improvement schemes and green energy developments contributed significantly to 2021 growth.

The Construction Output Price Index (OPI) estimated price increases of 6.2% in the 12 months to December 2021 which is the strongest annual growth rate to ever be recorded.



Source for Graph: https://www.ons.gov.uk/businessindustryandtrade/constructionindustry/bulletins/constructionoutputingreatbritain/december2021





Source for graph: https://www.markiteconomics.com/Public/Home/PressRelease/539b99e000a443698d02f1c93bc89b39

February construction PMI

The IHS Markit/CIPS UK Construction Total Activity Index continued strong momentum in 2022 with output volumes increasing to 59.1, up from 56.3 in January, and above the all-important 50.0 no-change mark.

The house building index (61.5) replaced commercial work (58.4) as the best performing construction category. Residential work was recorded at the strongest level over the last eight months. Civil engineering activity also accelerated (57.5) resulting in a bumper month for overall construction activity.

Pipelines remain resilient in construction, however reports of extensive supply constraints (longer delivery times impacted by driver and material shortages, coupled with international shipping delays) and sizeable increases in input costs continue to dampen market sentiment. This has led to business confidence declining to the lowest levels since January 2021.

Contacts

Dave Murray
Risk Underwriting Manager
Trade Credit (Heavy Industries)
Credit & Surety Europe
QBE European Operations
email dave.murray@uk.qbe.com

QBE European Operations

30 Fenchurch Street
London EC3M 3BD
tel +44 (0)20 7105 4000
QBEeurope.com

Made possible
QBE

367870/2203