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Construction

Where next for the construction industry…

Helping you to mitigate risk and maximize opportunities

The construction industry in the UK is often considered a bellwether of the health of the economy as the construction sector is fuelled by other industries as they look to expand or as the population grows and the demand for residential houses grows. Furthermore the UK's construction industry is a significant contributor to the UK economy in its own right. In 2022 the construction industry represented circa 7% of the UK GDP (c.£110 billion) and is composed of private (75%) and public (25%) sector work.

7%

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* Office for National Statistics (ONS), released 13 January 2023, ONS website

Challenges ahead ...

Supply Chain Issues

In 2022 we saw increased material costs as the war in Ukraine increased energy costs. The war, as well as lockdowns in China, increased the pressure on supply chains already disrupted by the pandemic and Brexit regulations.

Inflation

As inflation continues to rise, with CPI running at 11% the impact on earnings along with tax and interest rate rises are likely to see a stall in housing market turnover and private housebuilding in 2023.

Labour Supply

Reforms to IR35 introduced in April 2021, which requires operatives routinely working with the same contractors to be counted as PAYE staff, which has led to pay decreases for some, causing many to leave the industry.

Stagnated Private Sector Investment

Especially present in Retail, hotel and leisure sectors. Added to this is the change in working practices, with office staff working from home more frequently, leading to a requirement for less office space coupled with the over supply of existing office space means that new office developments are being shelved.

Finance difficult to obtain

Contractors may find they are winning work but have limited labour and/or finance to deliver these contracts. Firms may struggle to obtain finance from traditional high street banks and instead be obliged to procure alternative, more expensive, construction finance products.

VAT Reverse Charge Legislation

Cashflow problems have been heightened by the recent VAT reverse charge legislation, which takes cash out of the working capital cycle, and the return of Crown preference. CBILS and Bounce Back loans have helped. However, this may have led to overtrading, as well as latent financing issues when repayment is ultimately required.

Staged Payments

As the construction industry suffers from an almost unavoidable lag between work being performed and payment being received. Contracts often provide for stage or periodic payments in arrears. This can result in the supply chain carrying significant work in progress until payment is received.

Opportunities…

Increased Investment in Warehouse Logistics

However, it is not all doom and gloom, as 2023 is likely to see an increased investment in warehouse/logistics facilities as shopping habits continue to evolve and discount supermarkets, such as Aldi and Lidl, continue to expand.

Private Sector Investment

Increased public sector investment is forecast to increase construction activity in areas such as health and education, with a shortage of hospital beds and school places, especially in areas of recent significant housebuilding, such as in London and the Southeast. Notwithstanding this the Government's "levelling up" strategy should see increased development in the North of England.

Major rejuvenation programmes

Funding commitments for major programmes such as HS2 and road networks are expected to improve civil engineering activity. There have also been recent attempts to tackle the maintenance backlog on the nation's local roads.

Green Energy Funds

The government has promised funds to insulate the least energy efficient homes and other energy saving measures. Obviously its unknown at the moment whether there will be more uptake than previous attempts but could be worth exploring.

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How should the industry respond...

Taking steps to mitigate risk and maximise opportunities is important for survival in 2023.

Managing workloads and cashflow

- Maintain a good mixed portfolio of work, relying solely on tender contracts puts you at risk should you not win the tenders, try to get mixture of both high and low value work, along with customers and contracts.
- Take the time to produce short and long term forecasts either in-house or alongside your accountant. They need to readily assess the immediate and future of the business and resources needed to ensure adequate planning
- Closely monitor individual contracts against budget and assess profitability, how accurate is your budgeting for jobs? Could margins be improved?
- Review payment terms on large contracts and establish what impact customer failure would have. If staged payments can't be agreed is it worth the risk? Its important to avoid leaving large exposures at the end of a contract.
- Review whether work-in-progress (WIP) and debtor balances are increasing, understand the causes of this, and establish whether this indicates a problem with either the contract or the customer.
- Deal with disputes quickly, long delays often result in late payments. It's easier to deal with and resolve problems at the outset rather than them build up to larger problems later down the line due to avoidance.

Supply Chain

- Be aware of the impact your suppliers can have on your work, don't wait for the failure of a supplier to establish a back up. Where materials/services are a necessity establish a network of 2 to 3 suppliers to ensure you don't end up at risk of delays or additional costs.

Funding

- Ensure access to adequate funding lines and short-term liquidity explore options. Its useful to build relationships with banks and alternative lenders now and let them know your plans.

Labour Shortages

- Consider apprentices where possible to plug gaps, take the time to sell the career opportunities to those wishing to enter the industry.
- Consider taking advice to employ skilled workers from outside the UK. Whilst it might seem troublesome now it may be worth getting the necessary knowledge.

Opportunity for growth

- Can you look to fund projects via partnership or other alternative funding relationships.
- With public sector spend likely to increase there should be an increase in opportunities.
- Competition for good quality tenders should weaken as many companies are no longer in such a healthy position to tender.
- Taking the time to tender means you could reap the rewards but be careful not to think the lowest price will win the tender.

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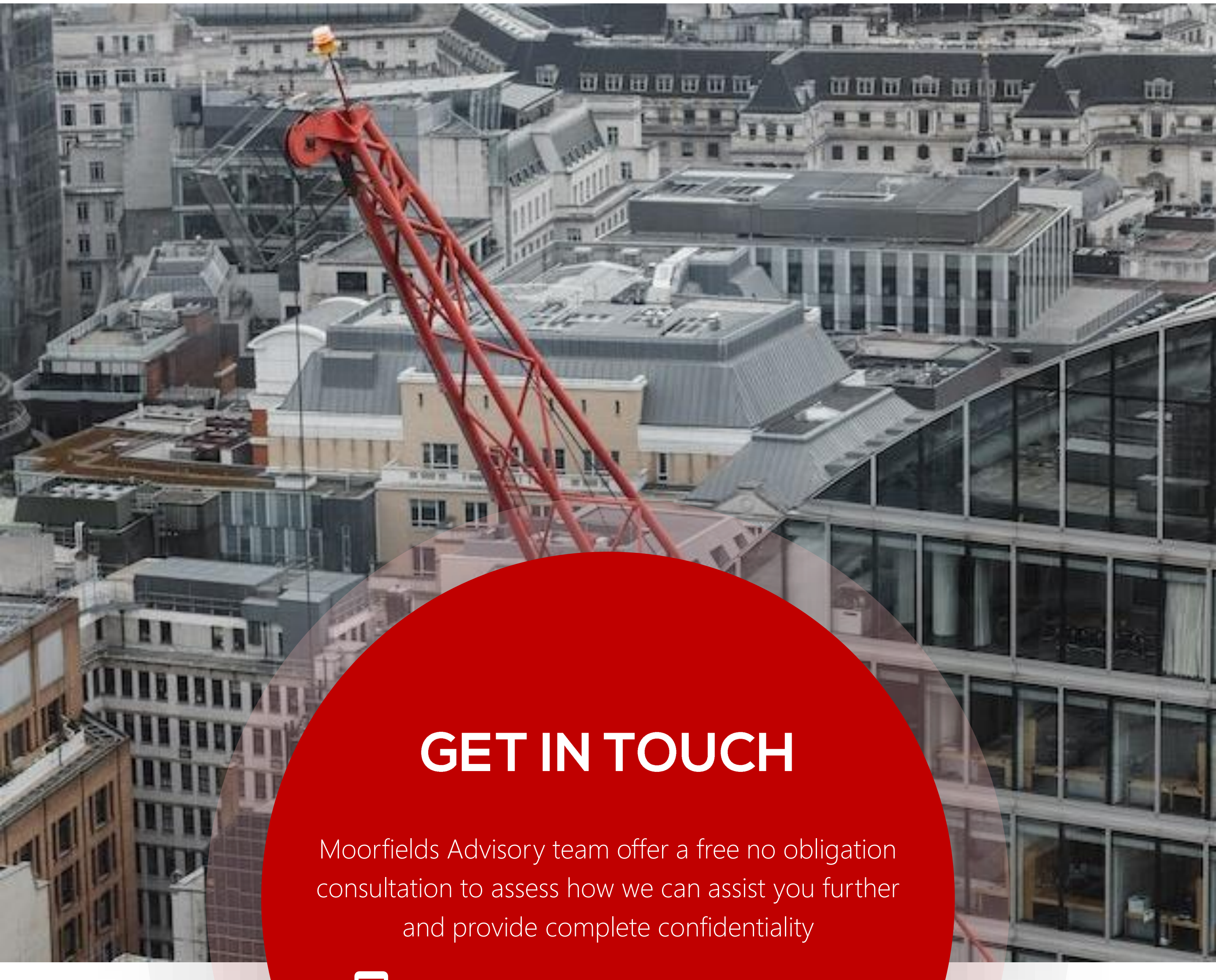

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