

CONSTRUCTING EXCELLENCE SW

The Implications of Brexit

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10 November 2016

2017 - IS WINTER COMING?

**The UK construction industry
will soon start to feel the true
impact of Brexit In 2017.**

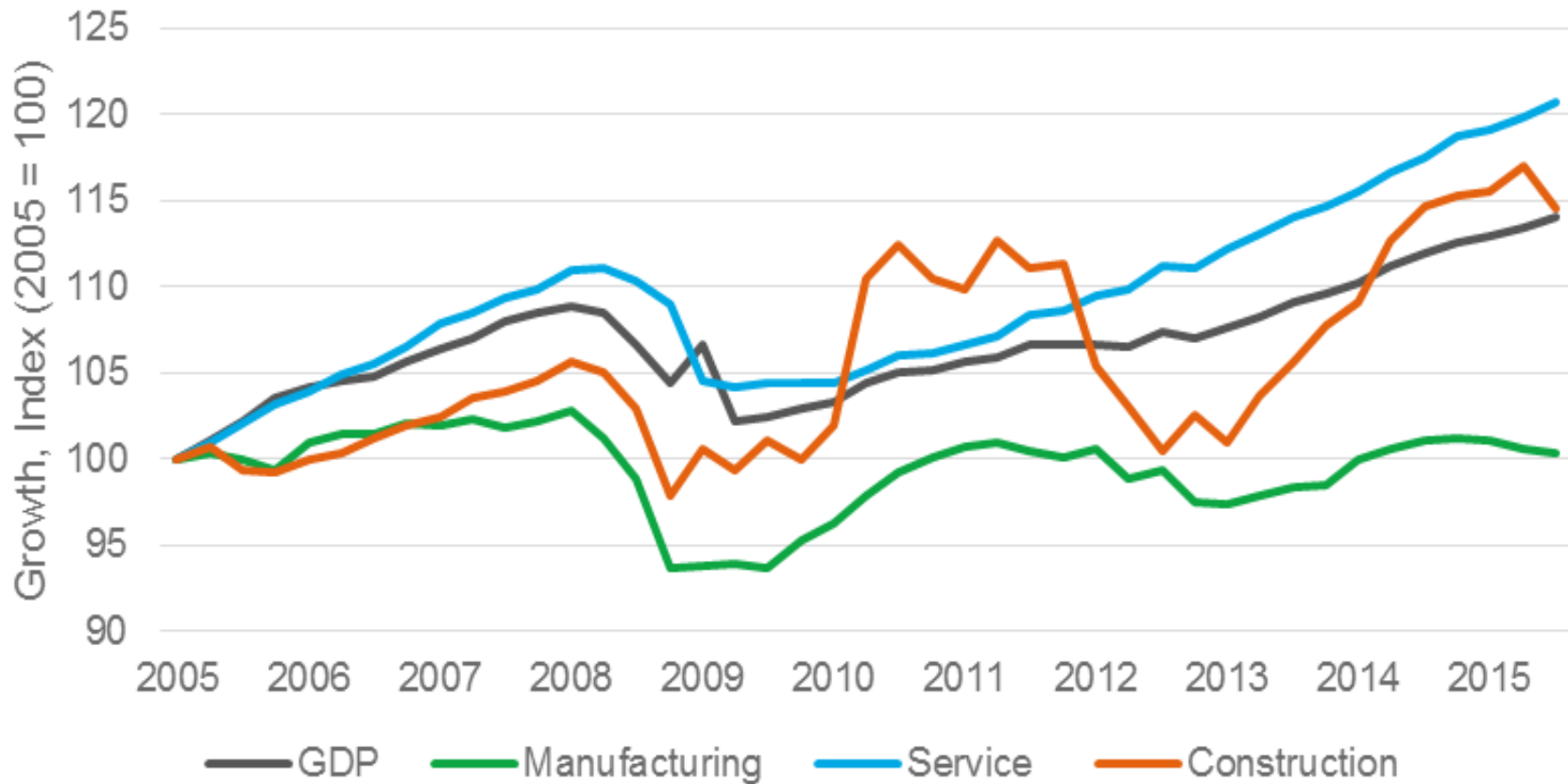


Demand side

The economic and demand outlook and why it is so important to the construction market

GDP Cycle

GDP growth - 2005 to 2015



Construction reacts to cycle in most extreme way

Economy Vitals

Economic Growth

2016 1.9%

(2016 0.4% Q1, 0.7% Q2, 0.5% Q3)

2017 1.0%

Source: HM Treasury Consensus Forecasts

Exchange Rates

£1 : €1.11

£1 : \$1.22

Source: XE.com Live 31/10/2016 2pm

Interest Rates

0.25%

Source: Bank of England

Consumer Price Inflation

2016 1.3%

2017 2.7%

2018 2.7%

2019 2.5%

Source: Bank of England Forecasts

Stock Markets

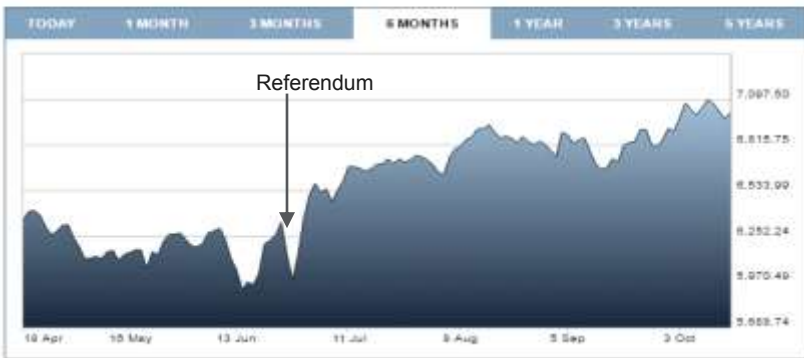
FTSE 100 and 250 have rallied to 2015 levels, although construction and property stocks continue to underperform.

FTSE 100

SUMMARY INTERACTIVE CHART CONSTITUENTS NEWS

Value	+/-	% +/-	High
6,983.82		-29.73	7,013.55

As at 17-Oct-2016 15:17:11 - All data delayed by at least 15 minutes.



Major FTSE 100 Company (Buildings Markets)



As at 17-Oct-2016 15:22:25 - All data delayed by at least 15 minutes.

FTSE 250

SUMMARY INTERACTIVE CHART CONSTITUENTS NEWS

Value	+/-	% +/-	High
17,831.44		-148.74	17,980.18

As at 17-Oct-2016 15:18:57 - All data delayed by at least 15 minutes.



Major FTSE 250 Company (Buildings Markets)



As at 17-Oct-2016 15:24:04 - All data delayed by at least 15 minutes.

Stock Markets

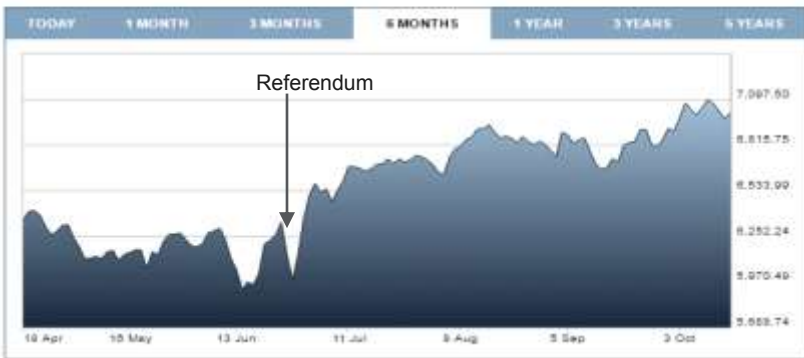
FTSE 100 and 250 have rallied to 2015 levels, although construction and property stocks continue to underperform.

FTSE 100

SUMMARY INTERACTIVE CHART CONSTITUENTS NEWS

Value	+/-	% +/-	High
6,983.62		-29.73	7,013.55

As at 17-Oct-2016 15:17:11 - All data delayed by at least 15 minutes.



Major FTSE 100 Company (Infrastructure)



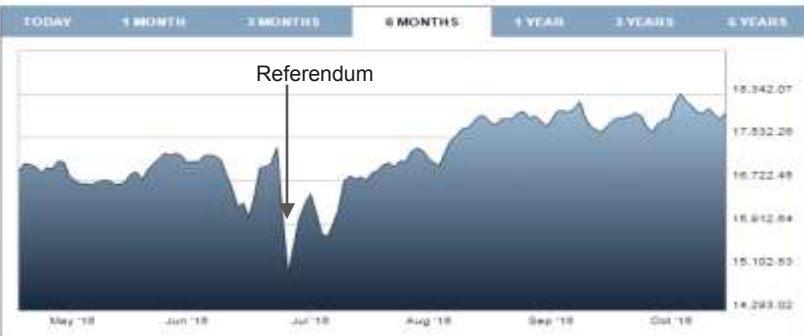
As at 19-Oct-2016 17:00:46 - All data delayed by at least 15 minutes.

FTSE 250

SUMMARY INTERACTIVE CHART CONSTITUENTS NEWS

Value	+/-	% +/-	High
17,831.44		-148.74	17,980.18

As at 17-Oct-2016 15:16:57 - All data delayed by at least 15 minutes.



Major FTSE 250 Company (Infrastructure)

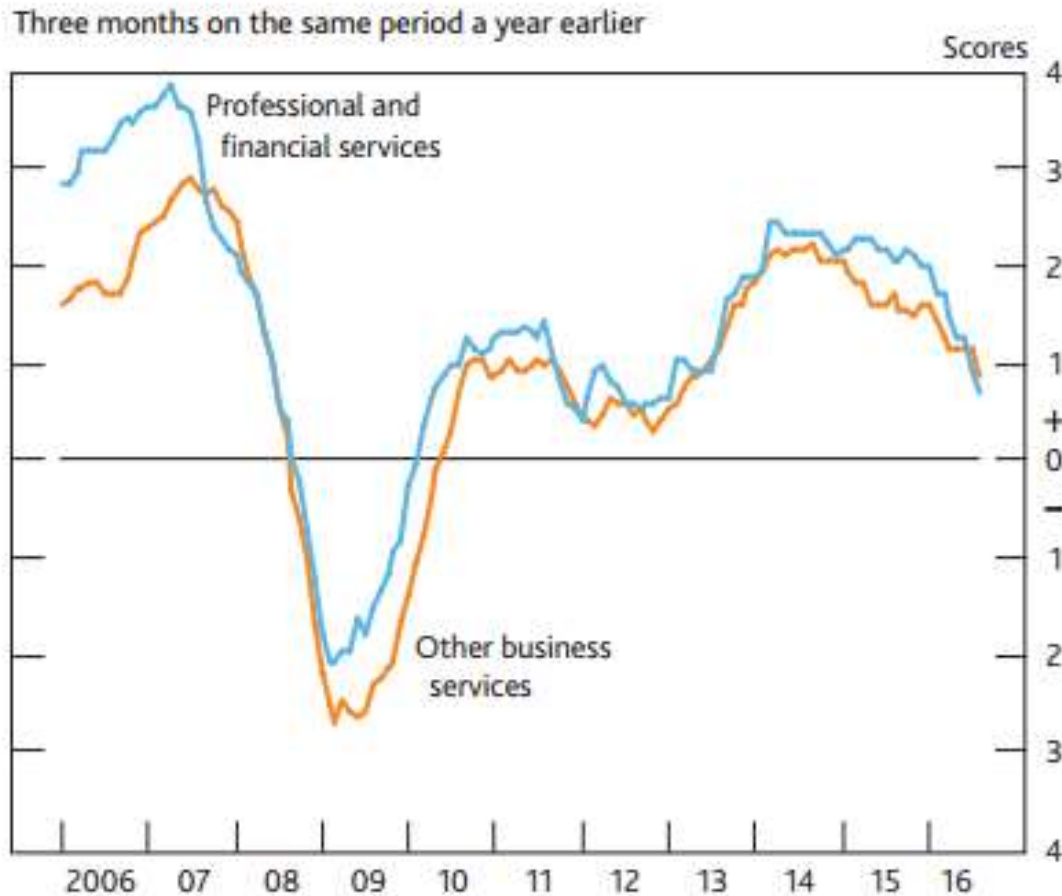


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13 November 2016

Business Turnover

Chart 2 Business and financial services turnover



In particular, transactional activity relating to real estate had slowed.

Construction output growth had slowed, partly reflecting easing growth among house builders.

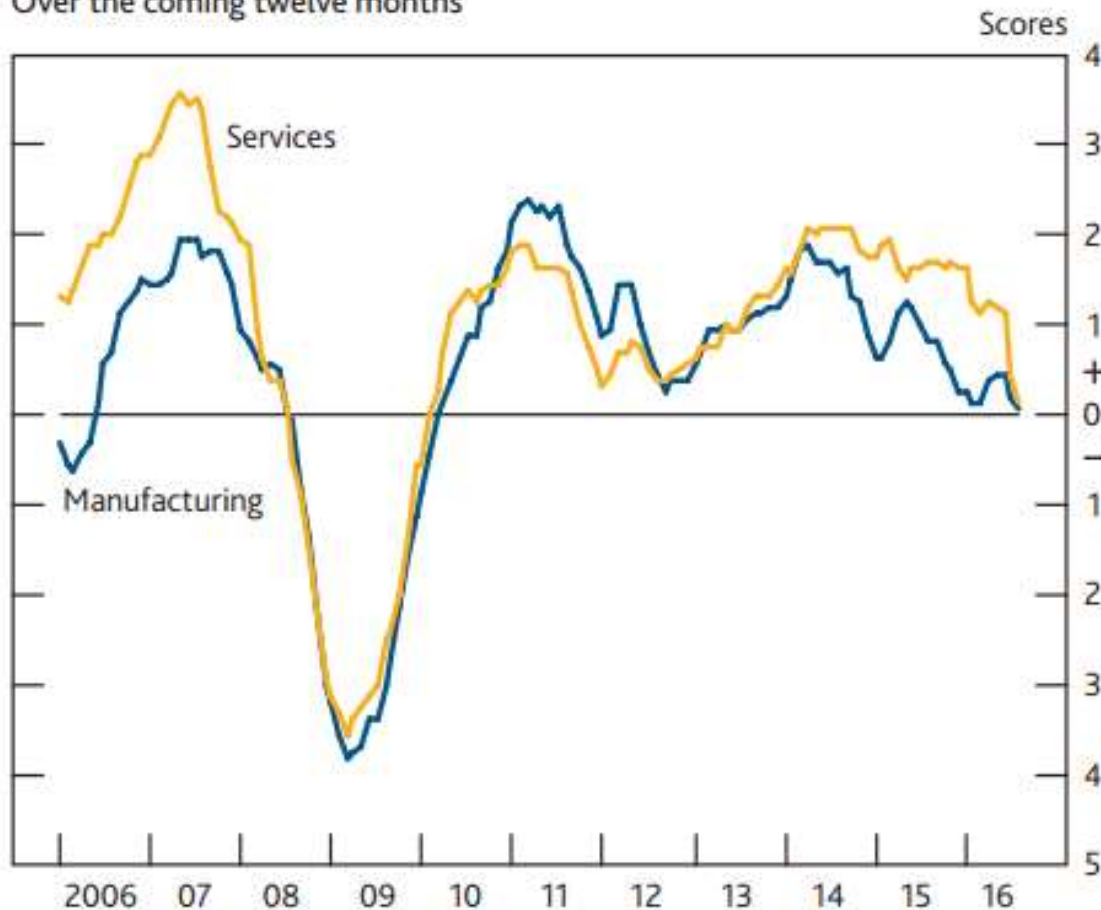
Occupier demand had showed some early signs of easing.

Source: Bank of England Q3 Report

Investment Intentions

Chart 4 Investment intentions

Over the coming twelve months



Source: Bank of England Q3 Report

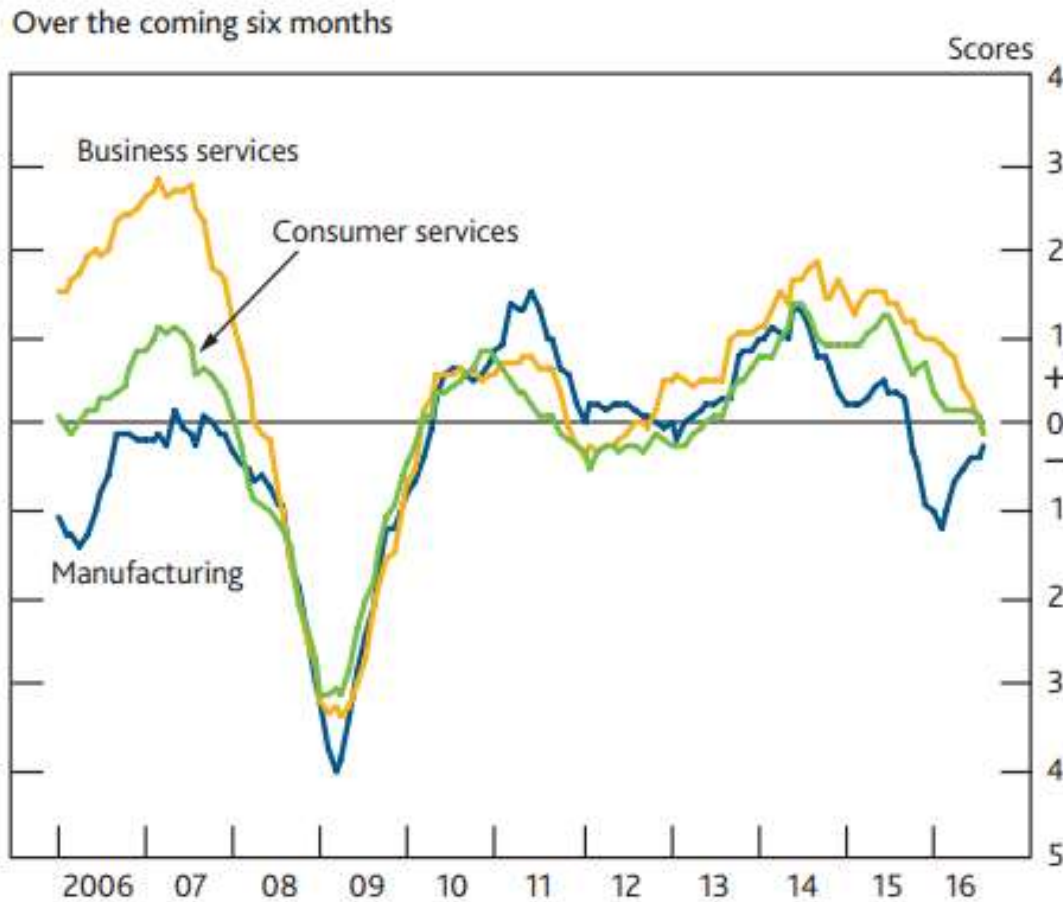
Projects being challenged more rigorously. Some scaling back or deference.

Investor demand for commercial real estate had fallen, particularly in London and from foreign investors.

Slowing capital spending most pronounced among companies providing professional services to the commercial real estate market.

Employment Intentions

Chart 5 Employment intentions



Source: Bank of England Q3 Report

Broadly point to flat staffing levels over next 6 months.

In some cases, primarily in corporate real estate -related subsectors, all non-essential recruitment had been frozen.

Brexit Scenarios

Less

More

'Harder' Brexit

'Softer' Brexit

A hard Brexit?

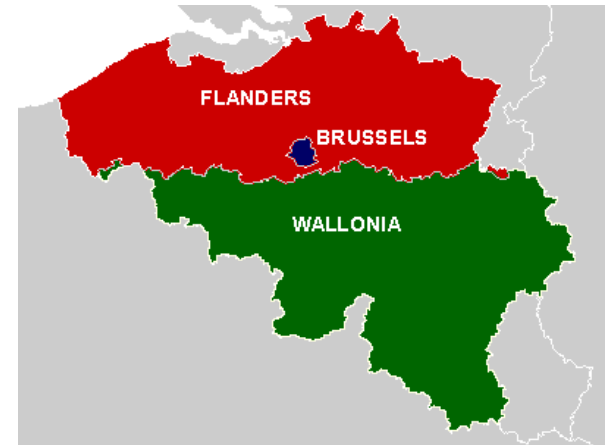
Has the balance of probability shifted further towards a hard Brexit?

May's change of tone raises prospect of sector-by-sector deals

Nissan pledges likely to prompt approaches from other companies



**TWO
YEARS
AND COUNTING**



A hard Brexit will create the most economic volatility

Politics SWOT

Strengths

- Swift resolution of leadership and reshuffle
- Step change in rhetoric
- Article 50 timeline (?)

Weaknesses

- New faces and departments

- Delayed decisions
- Government focus and capacity
- Deeper uncertainty post Article 50 triggering
- Parliamentary vote needed for Article 50 trigger, increased chance of general election?

- Rhetoric around pull back from austerity
- Obvious stimulus target
- November autumn statement
- Cheap borrowing

Threats

Opportunities

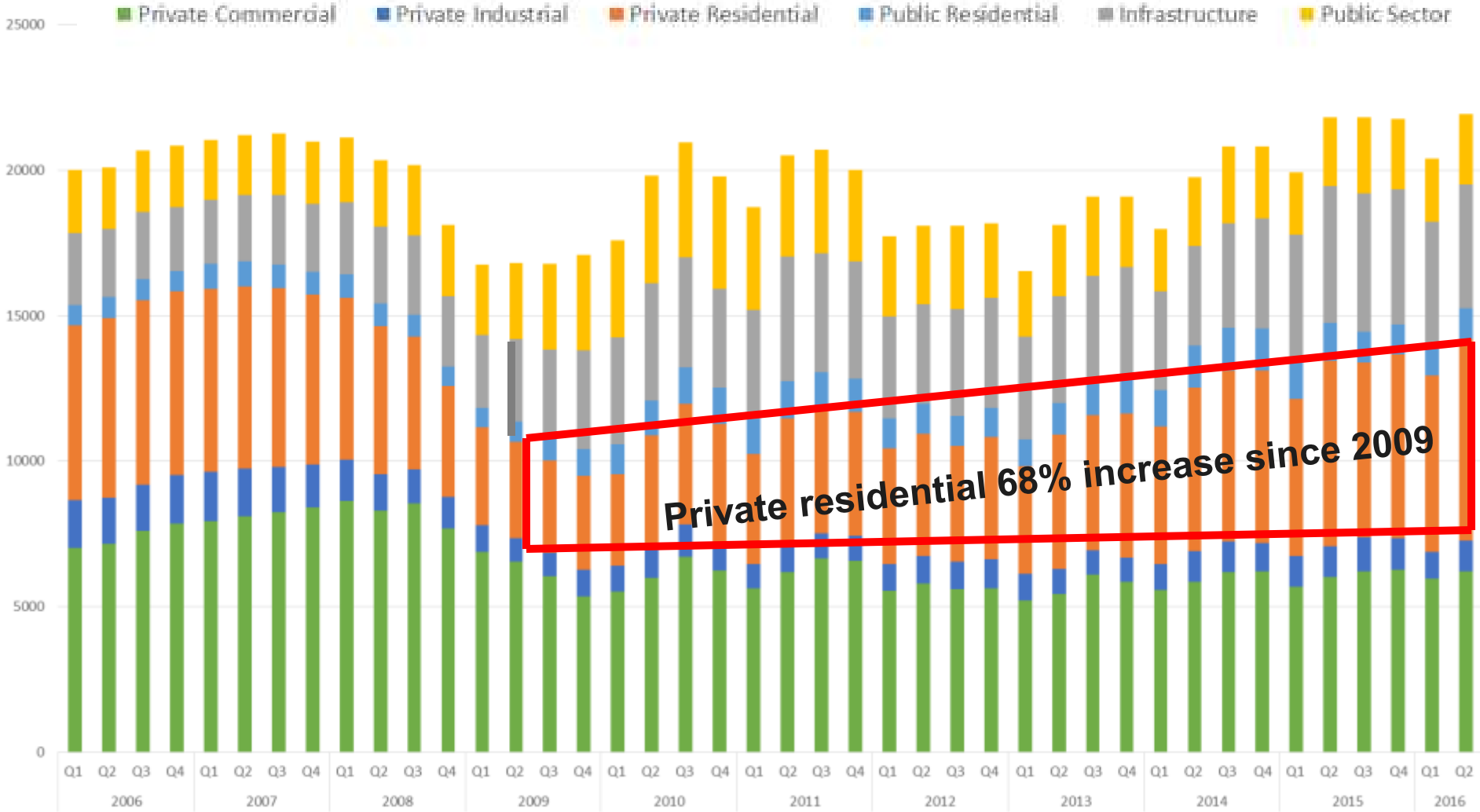
Theresa May's In-tray

Activity	Pre-referendum status	Current status
Airport Expansion	July 15 Airport Commission recommended Heathrow. Government delayed decision Dec 15.	Heathrow recommended. The 'ball' has been passed back to the private sector.
Tata Steel Rescue	Tata was reported as leaning towards keeping bulk of UK business, with support package.	A deal now looks more likely but unlikely to be announced before end of year.
High Speed 2	Construction was due to start 2017.	Uncertain with some rumours that government will delay, restructure or call off. Grayling and May have backed the project.
Devolution Deals	Of 38 deals submitted Sept 2015, 8 have been agreed. No timetable.	Osborne was leading this. May's rhetoric might signal a move away from this direction.
Prison Reform	White paper originally due in spring but delayed to autumn.	Uncertain. Gove was main sponsor – now gone. What will Liz Truss do?
Hinkley Point C	Plans had already been delayed but was due to produce power by 2025.	Decision made.
Land Registry Privatisation	Underway with consultation completed in May.	Uncertain. Quietly postponed by government.
Digital Economy Bill	Wide ranging but would give rights to fast broadband for example.	Progressing. Introduced to Parliament July.
Government Digital Strategy	Will set out plans for digital infrastructure. Was meant to be ready for publication few months before referendum.	Uncertain. Reports the strategy will be launched October but not confirmed.
UK Carbon Plan	Due to be published by end of year.	Uncertain. Abolition of DECC.
Industrial Strategy		Uncertain. Expect more detail from BEIS near term.

Construction Output

Source: ONS

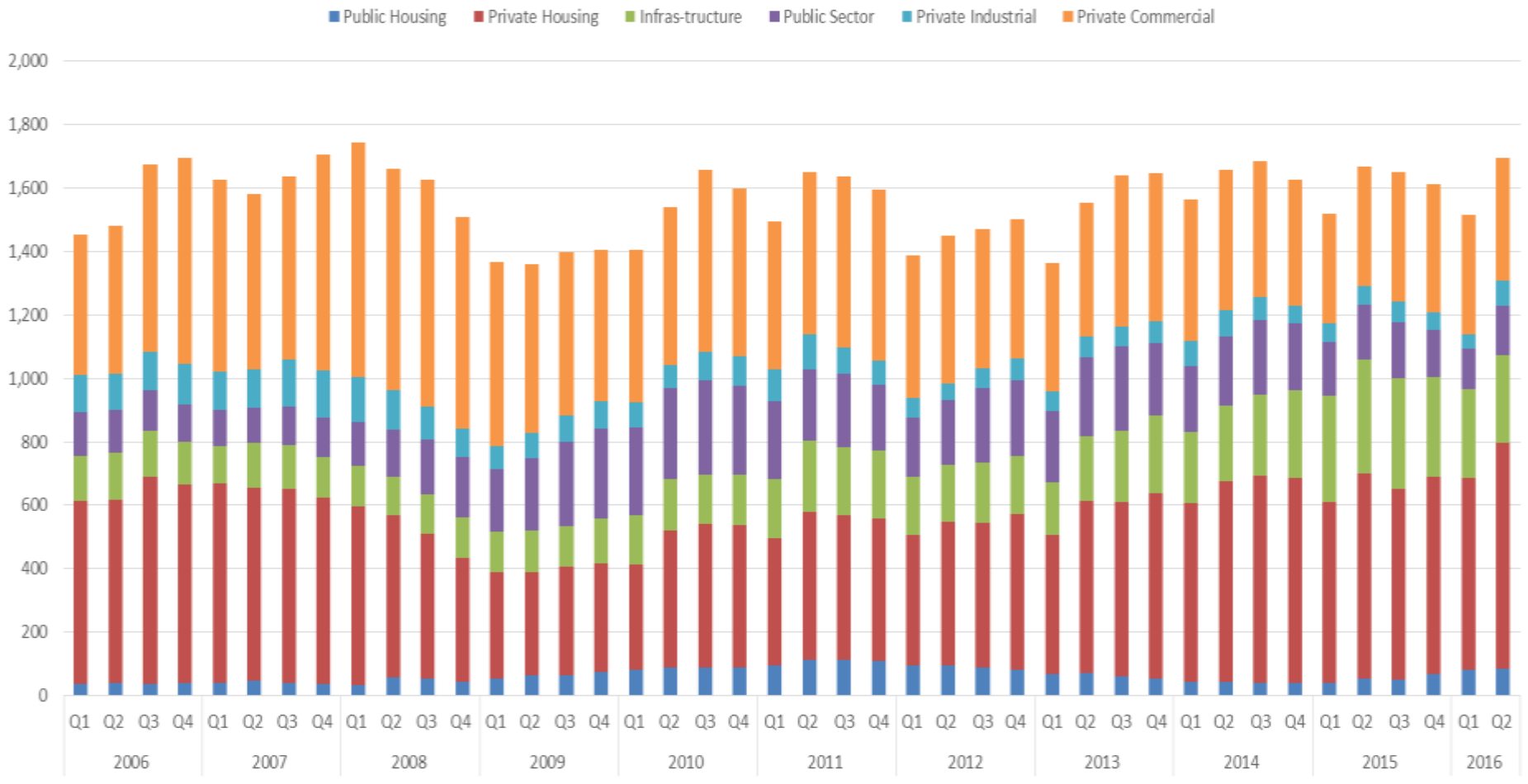
National Construction Output £m



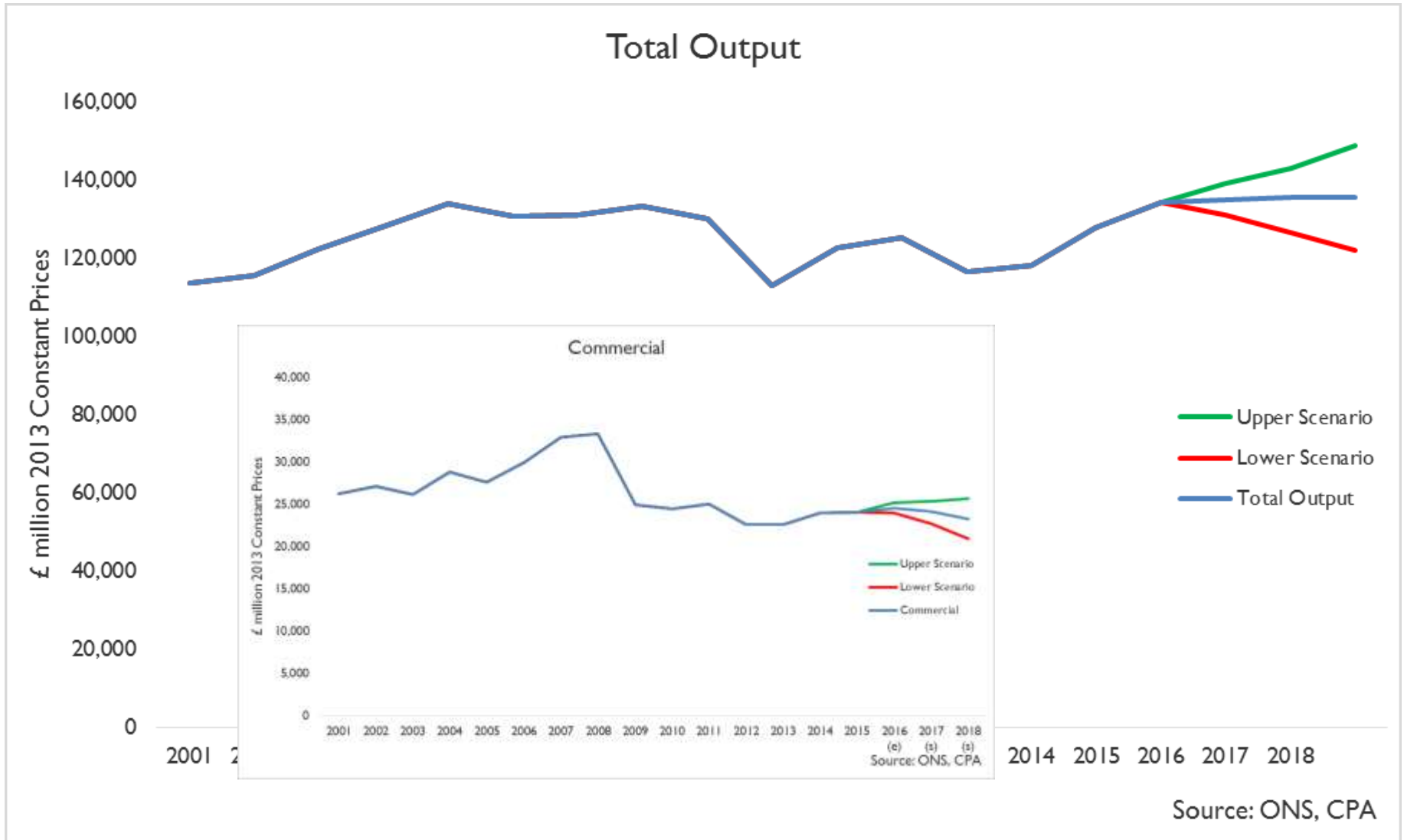
Construction Output

Source: ONS

South West Construction Output £m



Output Forecast



So what?

Will the short-medium term impact on sentiment and investment bring significant risk of impact on demand for construction, particularly in commercial sectors?

So what?

Supply side

The supply chain outlook, costs and prices

What will be dominant market force?

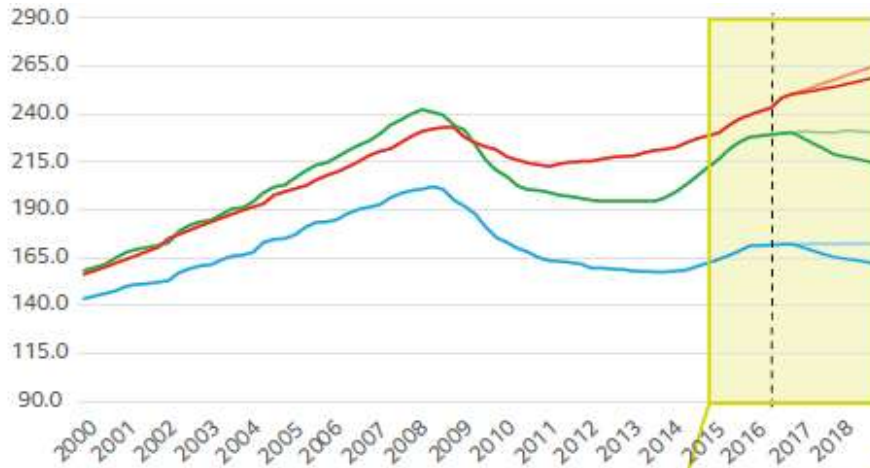
Rising input costs or supply chain discounting?

What will be the dominant market force?

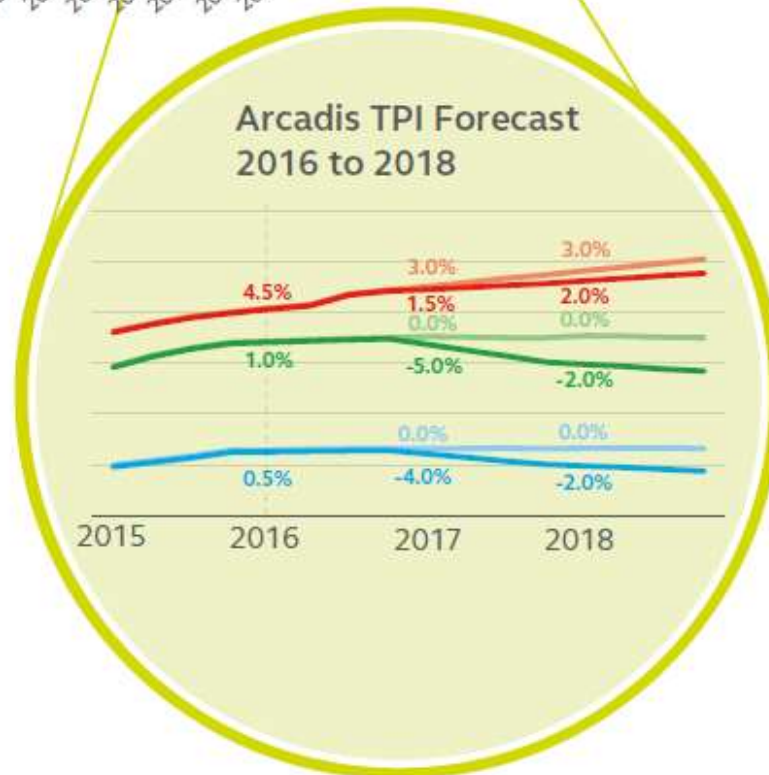
The construction price mix



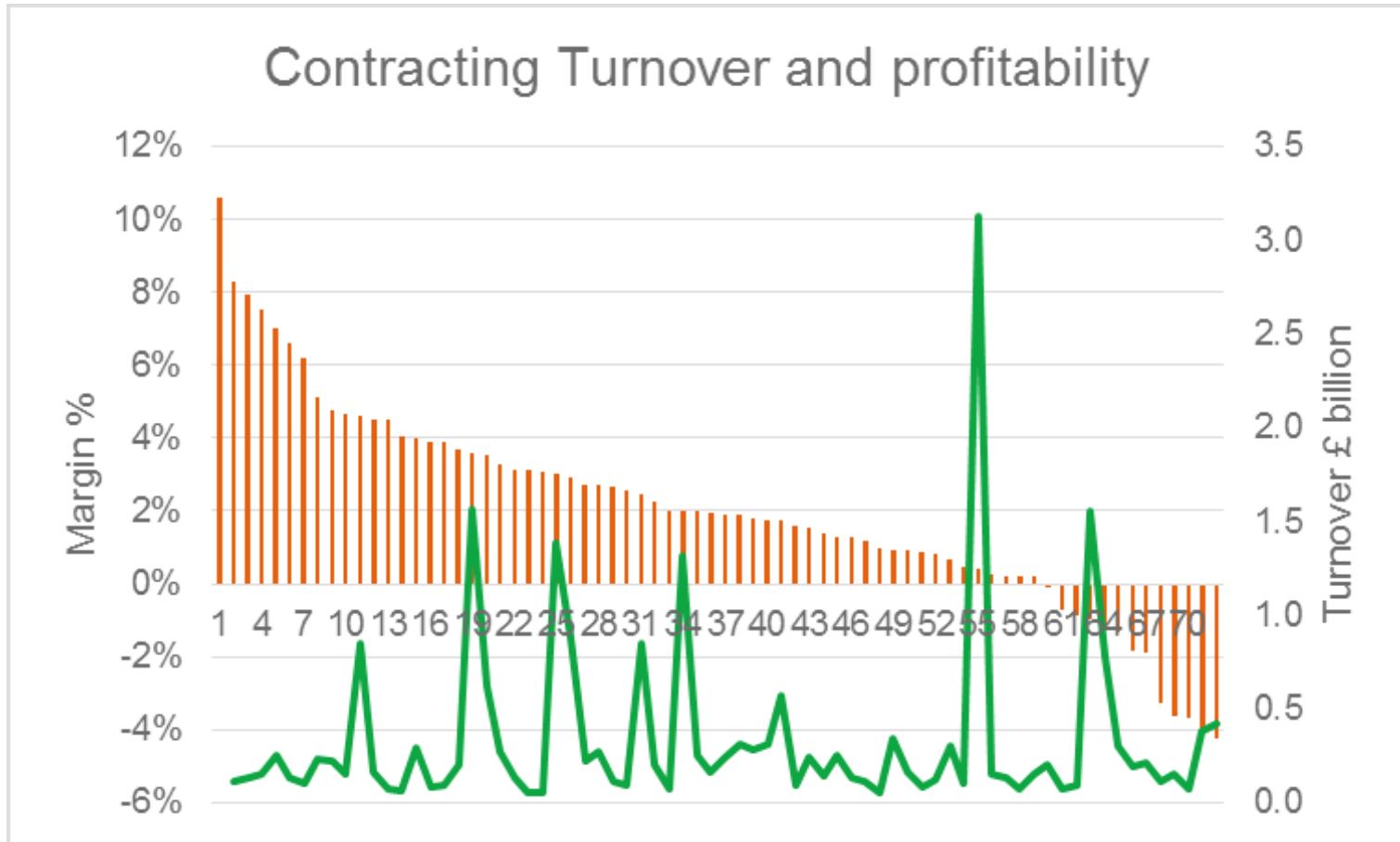
Our price forecasts



- Infrastructure - Lower Scenario
- Infrastructure - Upper Scenario
- London TPI - Lower Scenario
- London TPI - Upper Scenario
- Regional TPI - Lower Scenario
- Regional TPI - Upper Scenario



Profitability has improved but is not high for most large contractors



Green – Turnover

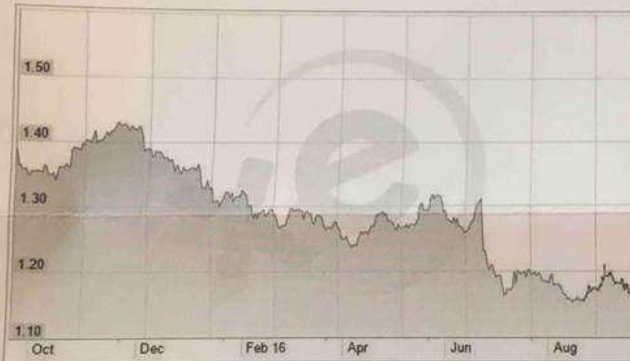
Orange - Margin

Impact of currency on materials costs

30th September 2016

Dear Sirs,

The effect of the EU referendum result has created a significant change in the relationship of the pound with the Euro and other key international currencies; i.e. circa 15% against the dollar and 17.5% against the Euro. This has had an adverse impact on the cost of raw materials, which will affect the whole market.



Euro per 1 GBP – source: www.xe.com

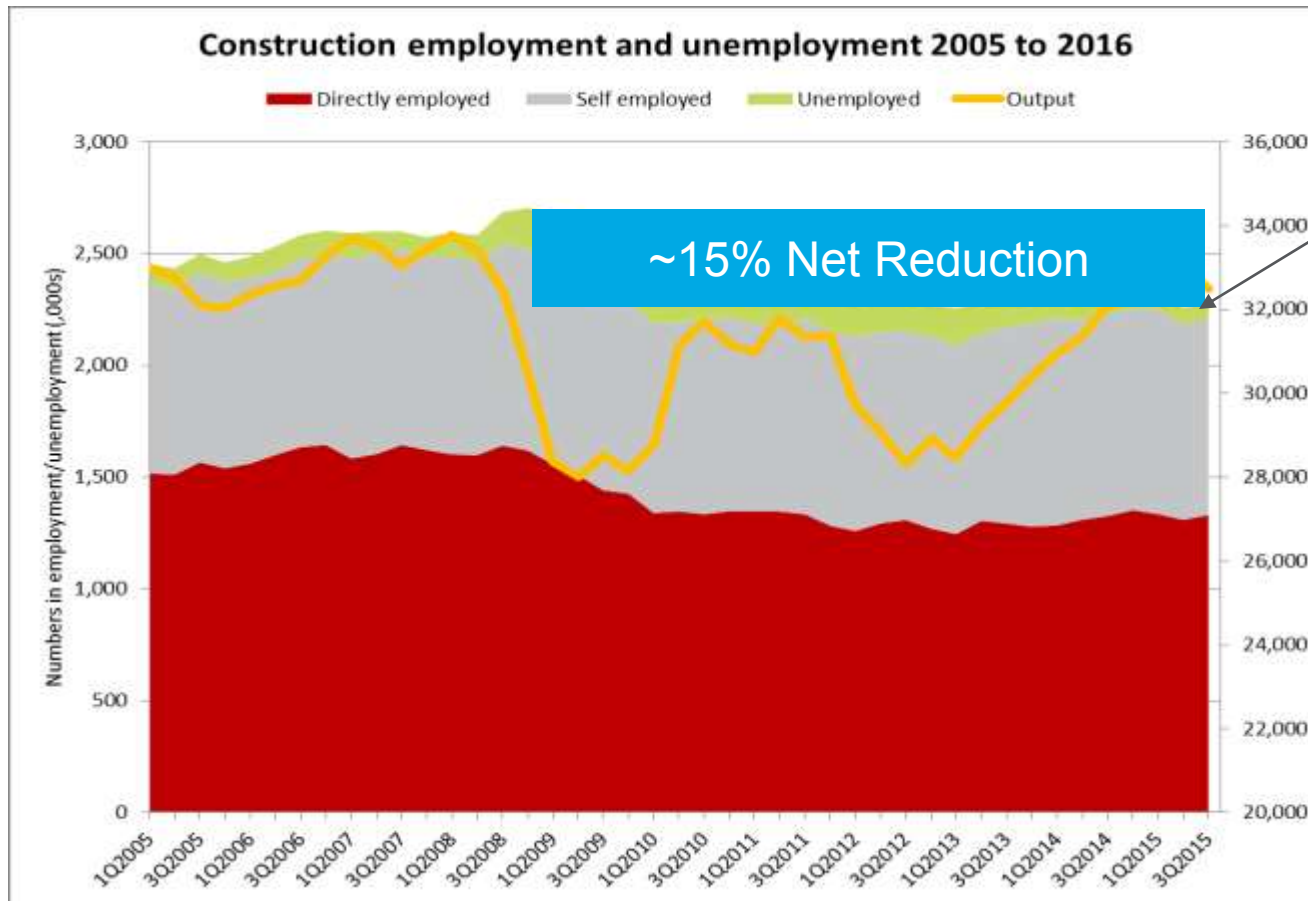
We have been pleased to be able to hold our prices for the last two years, this has been largely due to our large stock holding and forward thinking finance department. To enable us to continue providing you the level of service you require we do have to introduce a small price increase.

We will be launching a new Product Directory valid from 1st November 2016, which will include an average price increase of 7½%.

We look forward to assisting you in the future.

In our Market View we asserted our weighted assessment which showed depreciation of sterling adding around 6-8% to the cost of materials.

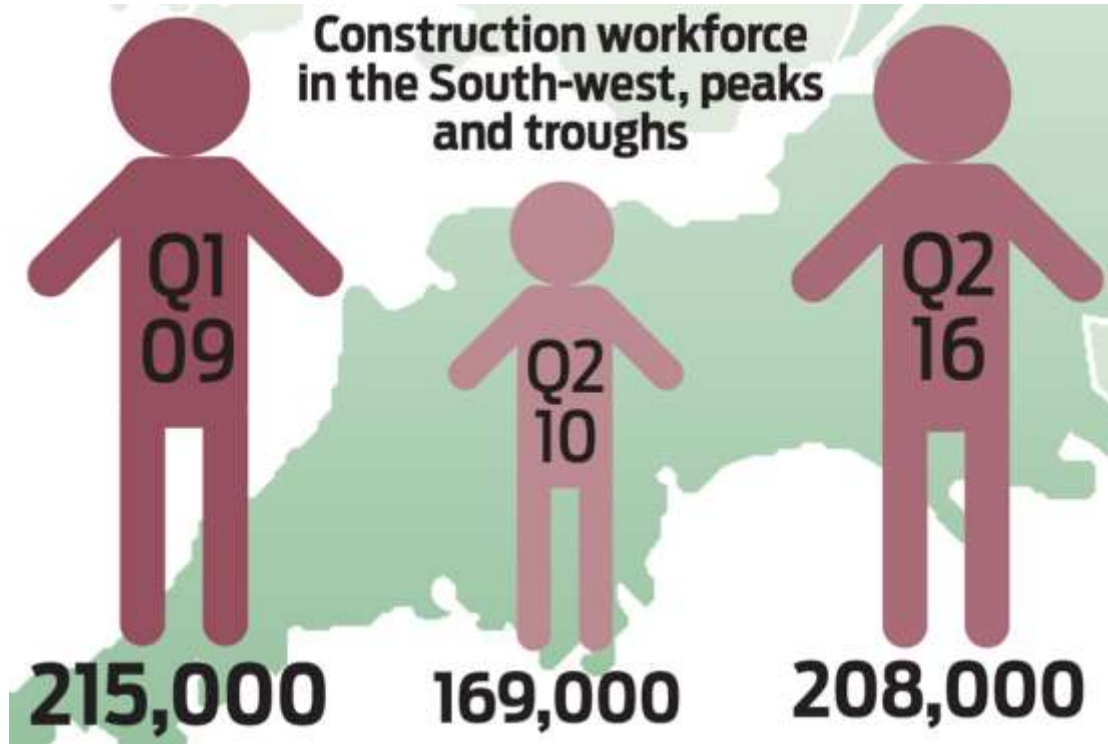
Current labour trends



3% unemployment in construction (many are long term unemployed) compared to 5% in wider economy. Emphasises just how little spare capacity there is.

Labour market structure limits training and skills investment

South West Labour Trends

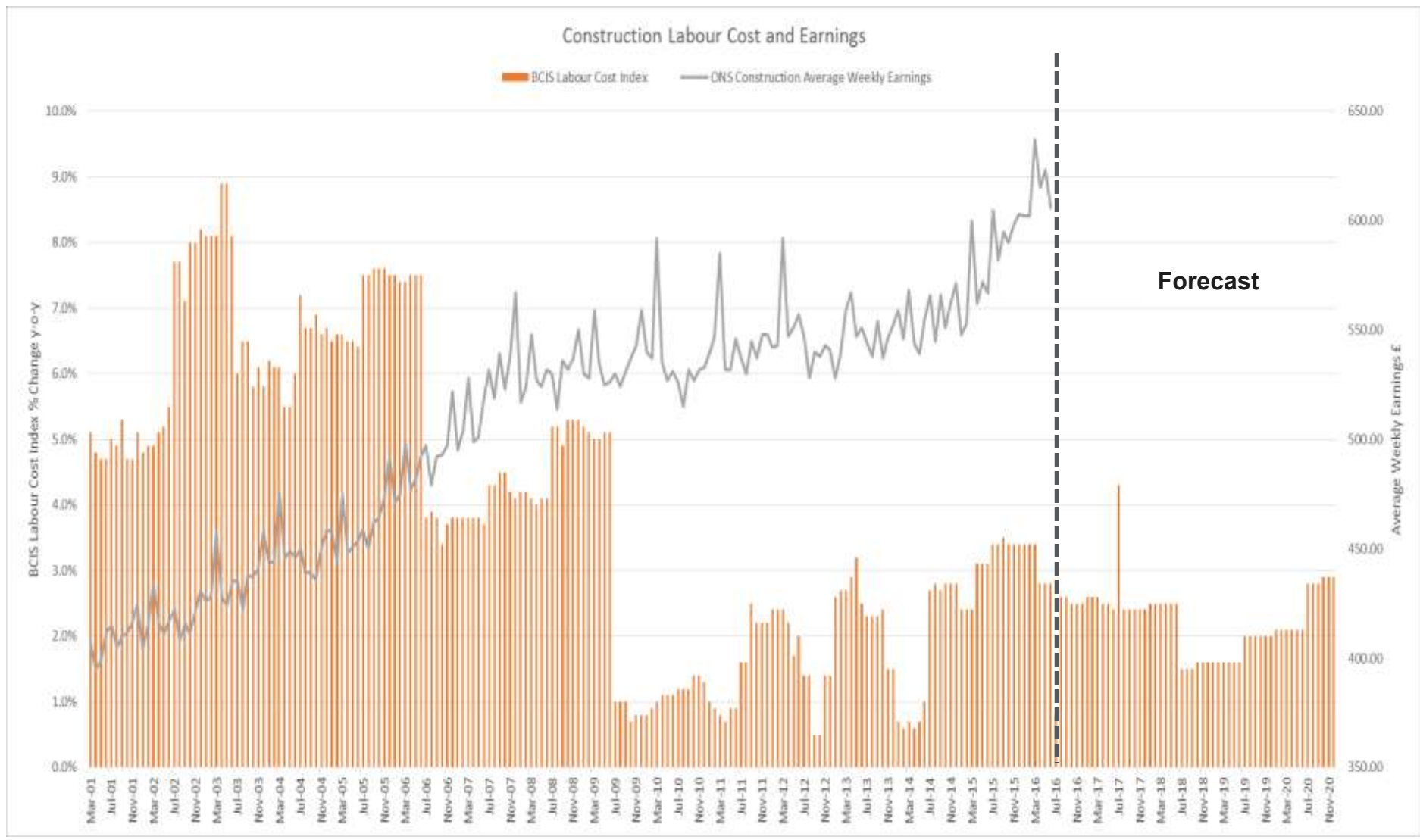


Source: ONS and Construction News

Hinkley will place huge labour demands for both skilled and unskilled workers. According to EDF, the project will provide 25,000 job opportunities and more than 5,600 people are expected to work on site during its core construction phase. (Construction News)

What impacts will this have on other projects in the South West?

Labour costs

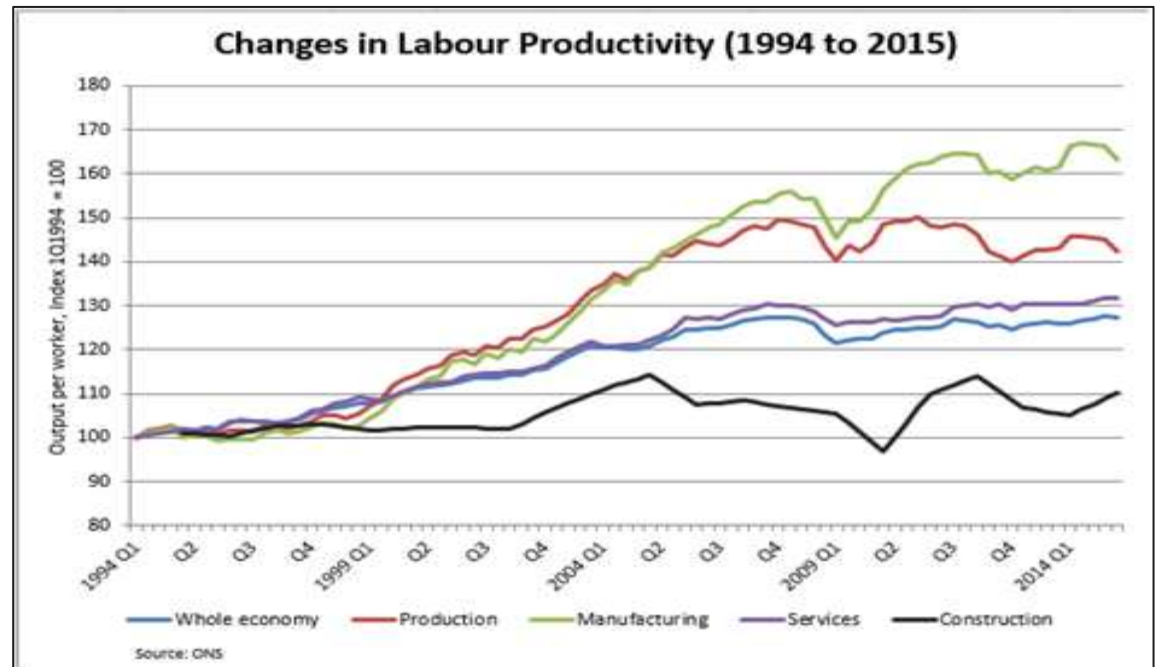


**The case for technological
innovation remains as strong
as ever**

The productivity imperative

UK lagging other G7 nations and 26% less productive than the USA for example.

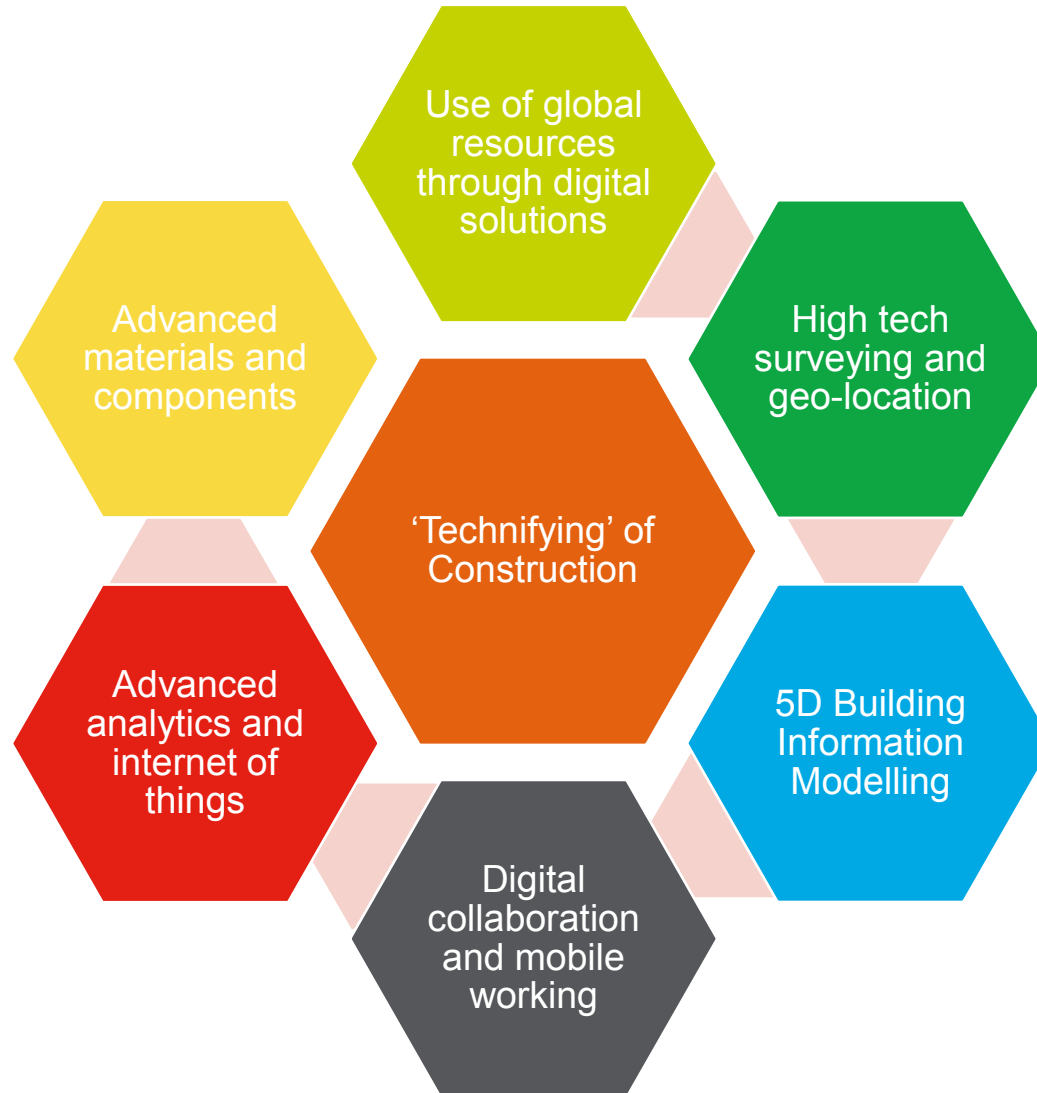
Since 1994, productivity of other key sectors, and the wider economy, has outstripped productivity in the construction sector.



Whilst manufacturing productivity has increased by 60%, construction has increased by 10%.

Investment in innovative construction methods could likely boost productivity.

Changes that will shape construction



What can the Government do?

Public Sector

- Government guarantee scheme to underwrite overseas investment in regeneration and growth; helping to reassure nervous investors and sending clear message that UK remains growth – focussed
- Statement confirming commitment to the Government’s vision for devolution, this will continue to see geographically balanced activity, creating and maintaining much needed activity across the country and supporting stable, self sustaining communities
- Procurement reforms to clarify the position on OJEU, and perhaps more importantly, make it easier and less challenging to enter into innovative partnership models with the private sector and other public sector bodies

Labour Market

- Early clarity on status of existing EU Nationals working in the EU. Prolonged uncertainty could be damaging. With reducing migration, declining new entrants and aging workforce, losing migrant workers could make things worse
- Help to create right incentives and conditions for clients and industry to adopt pre-manufactured solution. Need to reduce our reliance on labour and improve productivity making industry more attractive for younger people
- Use policy tools to help ‘smooth’ construction demand cycles. Use housing stimulus and infrastructure commitments to avoid damaging long term capacity

Infrastructure

- Commitment to the three big H's, namely Heathrow, Hinckley and HS2. Heathrow needs to be dealt with swiftly to demonstrate we are open to business
- If growth does slip into the red, take advantage of low interest cost of borrowing to drive pan UK programmes of shovel ready infrastructure projects. – sustaining further housing and commercial property development
- Get commitment from Government and quangos to commit to long term programme of investment in infrastructure to insulate against worst affects of any recession – five year investment programmes in rail, roads, water and regulated utilities.

Concluding thoughts

- Whilst it is clear the Government have a role to play, particularly in focussing policy and investment in housing and infrastructure, and providing means for investor confidence
- As clients and supply chain we have our own responsibilities:
 - Significant improvements in productivity and efficiency
 - Keep investment programmes running, and increase efficiency in procurement
- Lets avoid talking ourselves into negative growth

There will be uncertainty but we need to create the opportunities to sustain our markets

Questions?

