

## Industry to contract for a further two years

**Construction activity is forecast to decline for the next two years as slow recovery in private sector demand fails to offset the contraction in demand from public sector clients as public sector capital budgets are cut, according to the Association's latest industry forecast. By 2015, industry output is forecast to be worth £107 billion, 5% higher than in 2010, but the risks predominantly fall on the downside.**

Overall, public sector capital funding reduced by 11% between 2010/11 and 2011/12, to £44.5 billion. Funding is set to get progressively smaller until 2013/14 when it is anticipated that only £39.2 billion will be invested, nearly £11 billion less than in 2010/11. Cuts to capital budgets have not been equal across all departments, with education and social housing bearing the brunt of the falls. Between 2011/12 and 2012/13, funding available for the Affordable Homes Programme is set to fall by 50% with significant implications for social housing delivery, whereas the Department for Education will face reductions of 18% in 2012/13 and 21% in 2013/14, in addition to the 30% contraction in 2011/12, in its capital budget. The share of publicly-funded construction work, including PFI, in total construction is anticipated to reduce sharply over the forecast period, from 38% in 2010 to 28% in 2015.

On a brighter note, pockets of increasing demand are appearing within the private sector and privately-financed construction activity is predicted to rise by 3.5% this year. The pace of private sector growth is anticipated to slow to 2% in 2012 before accelerating to 4.8% in 2013 and by 2015 privately-financed construction output is forecast to be 23% higher than in 2010.

Offices and retail are expected to be the strongest commercial sub-sectors. Offices output is expected to rise by more than 50% over the next five years, albeit from a relatively low base. High profile projects in the London market, including Broadgate, the Pinnacle and 122 Leadenhall, will drive activity, with activity remaining lacklustre outside of London. Food retailers also plan to step-up development activity. Research suggests the UK's major supermarkets will add more

than 19 million square feet of new space to their existing stock between now and 2014.

With a quarter of the UK's electricity generation capacity due to close in the next 10 years, ensuring future energy provision is a priority. The recent publication of the DECC white paper was the next step on the path to significantly increasing renewable generation capacity and building replacement nuclear power stations. Electricity demand is set to double by 2050 and construction work in the energy sub-sector is anticipated to grow threefold through to 2015.

Manufacturing's significant contribution to the economic recovery provided industrial construction with a strong boost in 2010 and robust growth throughout the forecast period is anticipated. Elsewhere, the outlook is more muted. Credit market constraints will continue to limit growth in new house building activity and near term growth in privately-financed repair and maintenance work will be subdued.

Risks to the forecast, however, fall largely on the downside and have intensified in recent months. Weak economic growth in 2011 Q1 failed to allay concern after the economy stagnated in the last three months of 2010. Independent forecasters' predictions for GDP growth have been steadily revised downwards, from a relatively optimistic 1.7% in January to 1.5% in June. Additionally, pessimism is mounting ahead of the publication of Q2 GDP on 26 July. Should this pessimism prove to have a foundation, further downward revisions to growth projections for 2011 are highly likely. The persisting threat of a sovereign debt default within the European Union is a further risk to the stability of the economic recovery.

The industry will continue to face challenging conditions over the next 18 months. Industry output is forecast to contract by 0.5% in 2011 and by nearly 3% in 2012 before growth in private sector activity is sufficiently strong to offset the contraction in public sector work. Over the medium term, prospects for the industry are expected to improve, with the rate of increase expected to exceed 2%, the long term trend rate, by a significant margin in both 2014 and 2015.

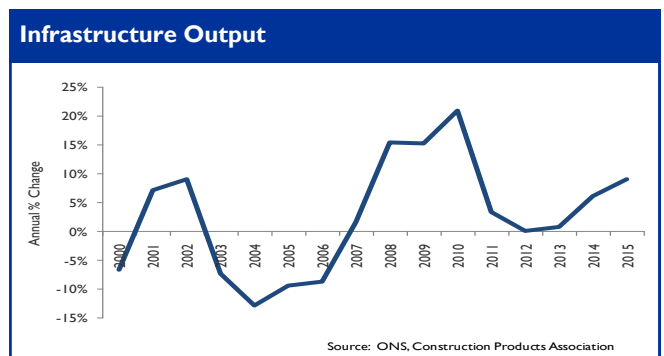
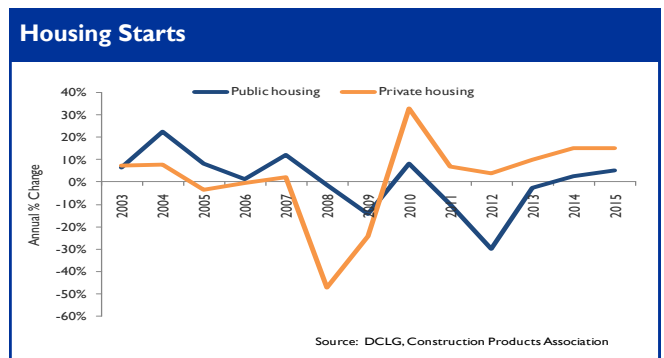
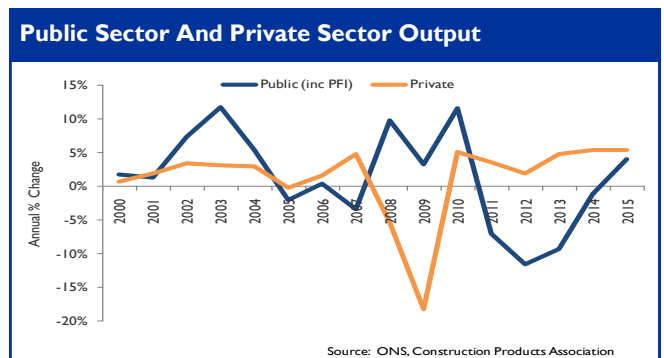
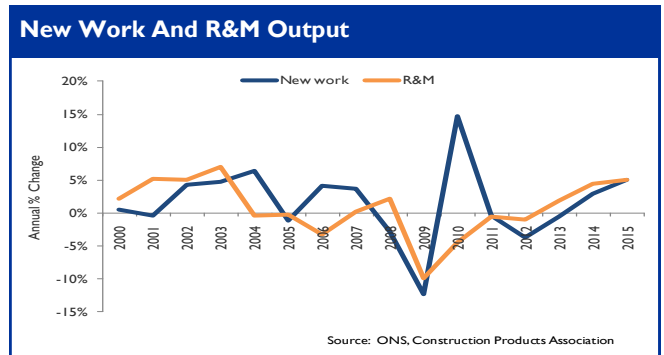
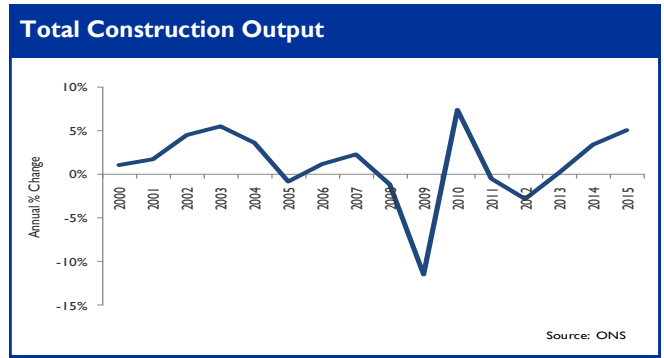
Prospects for construction activity are expected to remain subdued over the next two years as public capital spending reduces and private sector activity, constrained by subdued economic growth and a reticent consumer sector, strengthens at a relatively modest pace. Industry output is forecast to contract by nearly 0.5% in 2011 and by a further 3% in 2012. Thereafter, stronger prospects for the wider economy, an improvement in credit conditions and work on large-scale energy projects suggest that growth will be strong in 2014 and 2015.

Overall industry growth in 2010 was purely driven by the new work sector. Having reduced by 10% in 2009, r&m output fell by a further 5% in 2010 and is expected to continue to decline by around 1% in both 2011 and 2012. New work activity, in contrast, bounced back strongly in 2010, rising by 15%. Growth, however, is anticipated to stall this year before declining by 4% and 1% in 2012 and 2013 respectively. Post-2013, the outlook is considerably brighter for both sectors, with annual increases of between 3% and 5% forecast.

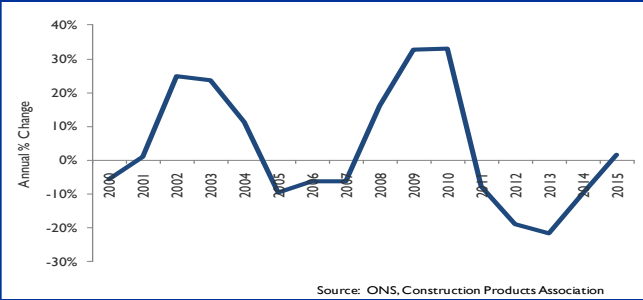
The government's package of measures to stimulate industry activity during the recession continued to yield output in 2010 and publicly-financed work (including PFI) increased by nearly 12%. Cuts to public sector budgets from April 2011 will impact in the second half of the year. Public construction output is forecast to fall, on an annual basis, through to 2014, from a peak of £38.7 billion in 2010 to just £28.6 billion. Private sector activity is forecast to rise by 4% in 2011 and 2% in 2012, before the pace of growth accelerates to over 4%.

Weak effective demand and reduced funding will constrain new house building in the near term. A more modest increase of 7% in private housing starts is forecast to follow 2010's robust growth of 33% in 2011 and a subdued increase of just 4% is anticipated for 2012. Thereafter, a gradual improvement in financing conditions should allow more robust growth. Public starts are anticipated to fall sharply as government funding is withdrawn. A 30% contraction in 2012 is expected to follow a 10% fall in 2011.

After three years of robust growth, the pace of expansion in infrastructure output is forecast to slow to 3% in 2011, with increases of less than 1% predicted for 2012 and 2013. However, within the sector as a whole, energy and rail output is set to expand considerably. Between 2010 and 2015, energy construction is forecast to grow by 195% as work on the nuclear programme accelerates and investment in increasing renewables capacity rises. Crossrail and Network Rail's investment programme will boost rail output.

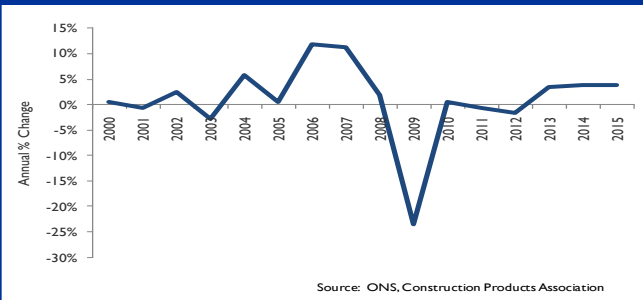


### Public Non-housing Output



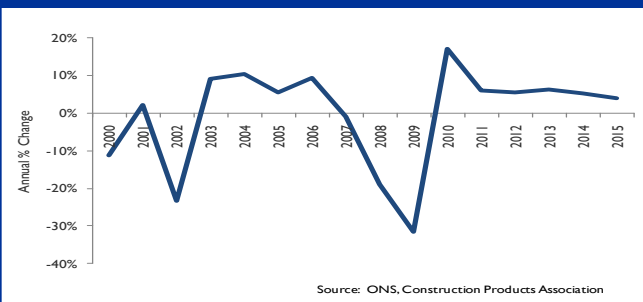
Public non-housing orders fell by 6% in 2010 and continued to fall in early 2011. Initial cuts to departmental and local authority capital budgets took affect in April 2011 and budgets will further during the next two years. The remnants of existing investment programmes continued to boost output in early 2011, but, in the year as a whole, output is forecast to fall by 8%. Between 2011 and 2014, the public non-housing sector is forecast to contract by 43%, to just £6.9 billion, before returning to modest growth in 2015.

### Commercial Output



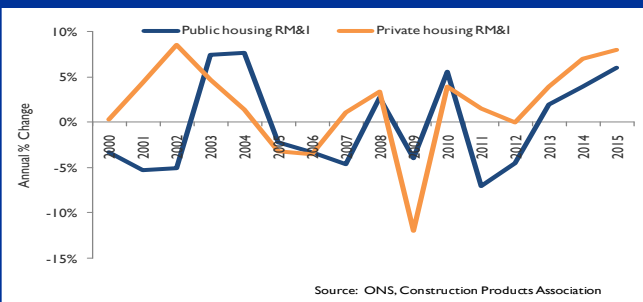
Orders growth in 2010 failed to be sustained in early 2011 and, with forecasts for economic growth being revised down, the near term outlook for commercial construction remains weak. Sub-sector demand is, however, expected to vary. Activity in the offices sub-sector is forecast to rise by more than 50% to 2015, whereas the entertainment sub-sector is forecast to contract by 4%. Overall, commercial output is forecast to fall marginally in the next two years before returning to growth in 2013.

### Industrial Output



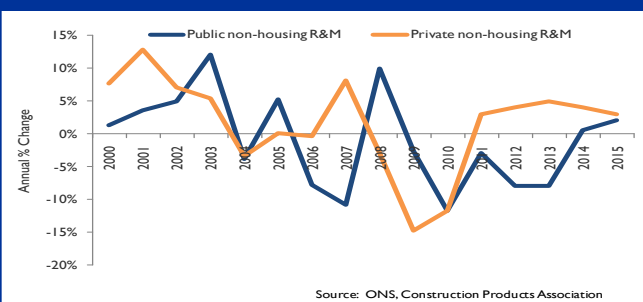
Output rose by 17% in 2010 and continued to increase on an annual basis in 2011 Q1. Looking forward, industrial output is expected to continue to rise. Factories construction is expected to continue to benefit from expansion in manufacturing activity, which has played an important role in UK economic recovery so far. With online retailing expected to become even more prevalent and overseas trade volumes rising, the outlook for warehousing activity is even stronger. Overall, industrial output is forecast to rise by 30% to 2015.

### Housing RM&I Output



Private and public housing rm&i output rose in 2010. While private housing rm&i output continued to increase in early 2011, public output slipped into decline on an annual basis. With work on the Decent Homes programme largely complete, the near term outlook for public housing rm&i is weak and subdued growth in household spending will constrain growth in private housing rm&i. Green Deal, which is to be piloted in the public sector, should provide a boost to housing rm&i in the latter stages of the forecast period.

### Non-housing R&M Output



Non-housing r&m output was scaled back sharply during the recession as non-essential work can be postponed with relative ease. Having fallen for two consecutive years already, public non-housing r&m output is forecast to fall for three further years and by 2013 output is expected to be 18% lower than in 2010. Private non-housing r&m is, in contrast, forecast to rise throughout the forecast period, at a rate of between 3% and 5%. By 2015, output is forecast to total £13.1 billion, 20% higher than in 2010 but 12% less than the 2007 peak.

## Key Statistics on the UK Economy and Construction Industry

		Annual % change unless otherwise stated								
Next Issue	<b>Economy</b>	2010	09Q2	09Q3	09Q4	10Q1	10Q2	10Q3	10Q4	11Q1
26-Jul	GDP	1.3	-5.9	-5.3	-2.8	-0.3	1.6	2.5	1.5	1.6
	Fixed Investment	3.7	-18.3	-14.6	-14.2	-0.8	2.4	6.4	7.2	-0.2
	Consumer Expenditure	0.9	-4.1	-3.6	-1.1	0.4	1.5	1.4	0.3	-0.5
	Real Disposable Income	-0.8	2.2	2.0	-1.4	2.1	-2.5	-1.3	-1.4	-2.7
26-Jul	Government Consumption	1.0	1.0	0.7	-0.4	0.8	1.1	1.3	0.9	1.1
14-Aug	Unemployment Rate	8.0	7.9	8.0	7.9	8.1	8.0	7.9	8.0	7.9
		2010	Nov'10	Dec'10	Jan'11	Feb'11	Mar'11	Apr'11	May'11	Jun'11
16-Aug	Inflation - Consumer Price Index	3.3	3.2	3.7	4.0	4.3	4.1	4.5	4.5	4.2
16-Aug	Inflation - Retail Price Index	4.6	4.7	4.8	5.1	5.5	5.3	5.2	5.2	5.0
		2010	Nov'10	Dec'10	Jan'11	Feb'11	Mar'11	Apr'11	May'11	Jun'11
	Manufacturers' Output Prices	4.2	4.1	4.2	5.0	5.3	5.6	5.6	5.4	5.7
		2010	Nov'10	Dec'10	Jan'11	Feb'11	Mar'11	Apr'11	May'11	Jun'11
	House Price Inflation (Nationwide Index)	5.8	0.2	0.1	-1.4	-0.1	0.1	-1.3	-1.2	-1.1
	House Price Inflation (Halifax Index)	2.9	-1.4	-3.2	-2.5	-2.5	-3.4	-4.6	-3.7	-2.0
21-Jul	Property Transactions HMRC (000s)	859	73.0	71.0	68.0	70.0	68.0	77.0	68.0	-
	Property Transactions HMRC (% change)	1.4	-8.8	-27.6	3.0	-5.4	-8.1	-2.5	-4.2	-
29-Jul	Mortgage Approvals (number)	2.5	-18.8	-27.4	-4.6	0.0	-3.1	-9.2	-7.2	-
		2010	Nov'10	Dec'10	Jan'11	Feb'11	Mar'11	Apr'11	May'11	Jun'11
04-Aug	Interest rates (End of month)	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5
	£ - € Exchange Rate (End of month)	1.17	1.17	1.18	1.18	1.18	1.15	1.13	1.14	1.13
	US\$-£ Exchange Rate (End of month)	1.55	1.60	1.56	1.58	1.61	1.62	1.63	1.63	1.6
	Brent Crude Oil (Monthly average)	28.7	85.7	91.8	96.3	104.0	114.4	123.1	114.5	113.8
		2010	09Q2	09Q3	09Q4	10Q1	10Q2	10Q3	10Q4	11Q1
02-Sep	<b>Construction</b> Total New Orders	3.9	-14.0	-5.1	4.0	30.2	-4.2	-15.3	10.8	-18.0
12-Aug	New Output	2010	09Q2	09Q3	09Q4	10Q1	10Q2	10Q3	10Q4	11Q1
	Housing	20.6	-22.0	-21.0	-9.2	0.5	21.2	34.1	27.9	14.5
	Infrastructure	21.0	7.5	9.7	42.2	34.6	31.2	23.1	0.6	2.9
	Other public sector	33.0	25.7	33.1	48.5	42.2	43.5	35.4	15.9	8.7
	Industrial	17.0	-33.6	-33.9	-19.0	-3.0	15.0	40.9	18.2	13.7
	Commercial	0.5	-20.1	-27.4	-26.8	-14.8	-4.2	10.7	13.9	-0.7
	Repair and maintenance	-4.5	-14.8	-4.2	-10.1	-9.5	-2.1	-6.6	0.5	3.8
	Total work	7.5	-13.8	-10.8	-6.4	-0.8	9.0	11.8	9.9	5.2
		2010	09Q2	09Q3	09Q4	10Q1	10Q2	10Q3	10Q4	11Q1
	Housing (000's of dwellings) <i>England</i>									
	Private Housing Starts (000s)	83.0	14.3	17.4	17.3	20.4	22.3	21.3	19.0	23.6
	<i>percentage change</i>	37.0	-38.3	33.2	46.6	74.9	56.5	22.9	9.5	15.8
	Social Housing Starts (000s)	20.3	4.0	5.1	4.7	5.0	6.1	5.1	4.1	5.6
	<i>percentage change</i>	15.0	-39.6	-4.2	3.7	27.9	54.0	0.2	-12.5	12.3
	Private Housing Completions (000s)	81.0	23.4	22.5	22.1	20.4	20.8	21.9	17.9	22.1
	<i>percentage change</i>	-12.7	-23.1	-19.0	-11.4	-17.5	-11.3	-2.9	-19.0	7.9
	Social Housing Completions (000s)	22.2	6.5	7.2	5.7	5.9	5.8	5.0	5.7	7.3
	<i>percentage change</i>	-13.7	1.7	17.0	-19.1	-8.5	-11.3	-30.8	-0.7	25.3
		2010	09Q2	09Q3	09Q4	10Q1	10Q2	10Q3	10Q4	11Q1
	Material Deliveries									
	Ready-Mix Concrete	-0.2	-37.0	-26.0	-23.0	-7.1	5.0	5.6	-5.0	15.0
	Concrete Roof Tiles	9.8	-30.7	-10.7	2.6	6.8	25.1	8.5	-1.4	16.4
		2010	Oct'10	Nov'10	Dec'10	Jan'11	Feb'11	Mar'11	Apr'11	May'11
	Builders Merchants Sales	-4.0	-0.8	-3.6	-12.4	6.7	-2.6	-1.8	-2.3	-
	Bricks	6.8	3.9	5.5	-41.9	64.3	7.9	0.7	-6.4	-2.8
	Concrete Blocks	2.2	-9.3	0.5	-28.8	19.6	2.9	0.3	-13.3	-2.0
	Steel Output	-1.6	-20.2	-23.3	-32.4	-9.6	0.3	-2.9	-7.2	-5.3

N.B. Monthly interest rate figures are bank base rates at the end of the month.

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