2018 to 2020 construction growth not London-centric

As is the case in many other Euroconstruct countries, the headline figures, both for the economy as a whole and the construction sector, disguise signifcant variation in performance at a regional level. The UK consists of nine English regions and three devolved nations and the commentary below provides an analysis of projected performance at this geographical level.

Gross value added (GVA) growth held up better across the UK as a whole in 2017 than anticipated last November, at 1.8%, and for a change London was not top of the growth rankings, with the East Midlands, East of England, South West, West Midlands, and Northern Ireland, all estimated to have performed better than the capital. However, we expect normal service to be resumed over the 2018 to 2020 period, with only London, the South East and the East of England exceeding the relatively modest annual average growth rate for the UK of 1.5%.
However, the prognosis for construction across the regions and devolved nations for 2018 to 2020 does not necessarily follow the wider economic trends, as in particular large civil engineering projects can significantly impact growth, especially in the smaller regions and devolved nations. Thus Wales and the South West lead the growth rankings, due to the presence of new nuclear build schemes in each, boosting overall growth. In the former, work on new nuclear build at Wylfa is expected to still be building up in 2020 while in the latter output from the Hinkley Point scheme should be beginning to plateau by then. Wales will also benefit from a number of other sizeable civil engineering projects, such as the £1bn M4 motorway upgrade around Newport, scheduled to start later this year.

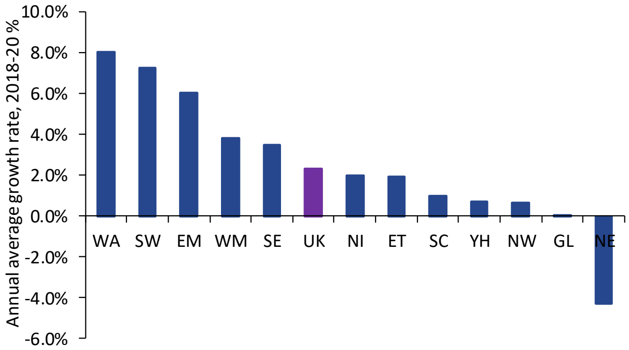
The North West has slid down the rankings recently, from 3rd to 9th, with a generally poorer performance across most sectors, partly due to the fact that 2017 was a better year than expected. This is a region that in the longer term may benefit from large infrastructure projects such as phase 2 of High Speed 2 (Hs2) and the prospect of new nuclear build at Moorside in Cumbria, but not until the mid-2020s. In contrast the East Midlands has moved up from 11th to 3rd, in the main due to a much stronger infrastructure forecast as the impact on the region of the HS2 project in terms of depots and other ancillary structures has become clearer.
The prospects for the biggest construction market, Greater London, remain weak over the next three years, pulled down primarily by the commercial construction sector and especially offices. London is estimated to account for roughly half of all office construction across the UK and with new orders down by nearly a quarter nationally in 2017, this will have a disproportionate impact on the capital. There is also likely to be a bit of a hiatus in civil engineering activity this year as Crossrail and Thameslink complete but HS2 yet to build up a head of steam.

The West Midlands should also benefit from the HS2 project as, to a lesser extent, should the South East. Phase 1 of HS2, which will take the new line from London to Birmingham, should get going in earnest in 2019 and the main regional beneficiaries of work in the early stages will be London, the South East, the West Midlands, and to a lesser extent the East Midlands. Phase 2, which will extend the line to Manchester, with spurs through the East Midlands and South and West Yorkshire, will not start in earnest until the second half of the 2020s.
All regions and devolved nations bar the North East should see some growth in housing output given government aspirations to start trying to address the long-term demand/supply mismatch in housing provision. However, demographic factors will be a primary reason for differences in growth rates across the regions and devolved nations, with stronger population growth generally centred in the south-east corner of England (Greater London, the South East, and East of England).

Weak demographics is one of the reasons for the North East's poor house building performance and a dearth of major projects after the completion of the latest A1 road upgrade (which straddled both Yorkshire and the North East), leaves the region at the bottom of the rankings with a projected annual average decline in output of 4% over the forecast period.

The prospects for Scotland have improved since the autumn forecasts with activity in both the civil engineering and commercial construction sectors stabilising in 2020 and strong growth in the housing sectors over the forecast period. The Scottish Government has been developing new funding methodologies for public projects – hospitals, schools, etc. – including the Non-profit distribution model (NPD) and Tax incremental funding (TIF). The former is a variant of the private finance initiative, but seeks to cap private sector returns. It is important to note that the NPD model is **not** a “not for profit” model. Contractors and lenders are expected to earn a normal market rate of return as in any other form of privately-financed deal. TIF uses future additional revenue gains from taxes to finance the borrowing required to fund public infrastructure improvements that will in turn create those gains. When a public project such as a new road system is constructed within a specific area, increases in the value of the land as well as new property and business investment can occur. Resultant increased site value and investment generates increased tax revenues. These increased tax revenues (whether domestic or business property) are the 'tax increment'.

Chart 1: Regional construction growth in UK 2018-20



Source: Experian

EM = East Midlands, ET = East of England, GL = Greater London, NE = North East, NI = Northern Ireland, NW = North West, SC = Scotland, SE = South East, SW = Souht West, WA = Wales, WM = West Midlands, YH = Yorkshire & Humber

Note: construction growth rates are based on current prices

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