Supply Chain Sentiment

Q4 2023 report



info@pfh.co.uk | www.pfh.co.uk | 01925 737 698



Neil Butters, Head of Procurement
Procurement for Housing

In our quarterly market sentiment series, we take an in-depth look at the confidence and attitude of the social housing supply chain and what this means for PfH members.

Every three months, we speak to a range of manufacturers, merchants and contractors from across the country to understand the challenges they face now and how they feel about the future.

We hope that by reading the mood of where the market is heading, social landlords can better prepare, particularly in such volatile times.

Supply chain prepared for further stagnation, although concerns mounting around labour gap and wage bills: how will these challenges play out when uptick in demand returns?

Key findings

- **79% of supply chain are forecasting costs increases (up 27%)**
- **Inflation and its impact on labour costs is the key contributor**
- **Skills gap is growing: supplier concern has risen to 4.8 (3.4 last quarter)**
- **However, price of materials, energy and shipping all falling**
- **Supply isn't a worry: none of the supply base are predicting challenges**
- **Overall, supplier confidence remains static (down 0.04%)**

Views from the sector

In our final sentiment report for 2023, we're overlaying our market perspective with some voices from the sector.

Key questions were put to social landlords within the PfH Advisory Group, as well as a number of member housing organisations. They told us about the opportunities and challenges they see for 2024.

Each housing provider was asked to rank six focus areas (Decent Homes; Fire Safety; Green Spaces; Net Zero Carbon; New Build and Sense of Place) in priority order.

With ITV News investigations and the tragic death of toddler Awaab Ishak highlighting sector-wide issues around mould and damp, it was no surprise that Decent Homes came out on top. Fire Safety took second place.

Notably, net zero and new build have dropped down the list, taking third and fourth place, respectively. With stagnation in the construction industry persisting, contractors are looking to the public sector for work. But rather than new build or high value retrofit, their focus is delivering damp, mould and fire safety remediation.

Sense of Place and Green Spaces were right down at the bottom, with housing providers saying they are too busy upgrading stock to find the headspace (or budget) for much more.

2024: the year of compliance, not growth

Social landlords explained that they are redistributing budgets from their development and sustainability pots and re-allocating them to the improvement of existing stock.

This will, of course, have longer term implications for housing providers whose business plans work on 30-year cycles. If investment in building and retrofitting properties falls off, the impact will be felt in years to come.

Is this a surprise? Possibly not. We know that new build is cyclical and that depending on the current headwinds, focus shifts invariably between repairing and upgrading existing stock and building new homes. The interesting perspective here is the double dip in private and public sector new build, which, if sustained, could have long-lasting implications for labour and skills.

It's more a watch this space at the moment.

Skills gap is biting

Housing organisations told us that labour shortages were really being felt and they were considering their own in-house capabilities more than ever. Rather than 'outsource, outsource, outsource' which has been the mantra in recent years; the drive to insource is growing fast. Social landlords are identifying the work programmes they can undertake themselves, and we're seeing partnerships and joint ventures being established to deal with the mounting skills challenge.

Are you feeling the impact of the skills shortage in construction?

"Massively. We have a framework just for the group so seeing quite a few projects going through it. Biggest skills shortage is in the decarbonisation area with maintenance of SPV and batteries etc."

Procurement reform shake up

When we questioned housing procurement leaders about their to-do list for 2024, most told us that preparing for the Procurement Act was near the top. Procurement reform also featured highly when we asked about the one message they'd pass onto their supply chain for next year:

"Procurement act is a game changer for us and them"

"Compliance, upskilling staff and get on procurement bill training"

"Be collaborative"

Another issue mentioned repeatedly was how housing providers will tackle the new transparency regime, particularly around key performance indicators (KPI). The majority said they will be developing bespoke KPIs for each contract, although a few are planning to adopt a one-size-fits-all approach.

There was consensus from housing organisations that strong contract management will be crucial going forward. The Better Social Housing Review (set up in June 2022 by the NHF and CIH to tackle social housing issues in England) is expected to develop sector wide KPIs, something that housing providers may then adopt to manage their contracts.

Turn to page 11 for advice on how to address this issue.

You can keep updated on the latest outcomes of the Better Social Housing Review here. The Review's report on KPIs is expected to be published in early 2024.

Views from the supply chain

There is a feeling from the manufacturers, merchants and contractors we spoke to this quarter that next year will be one of stagnation. This was backed up by forecasts from the Office for Budget Responsibility (OBR) in late November, predicting that the UK economy will grow far slower in the next two years than previously anticipated because inflation is taking longer to fall. Measures in the Autumn Statement - tax cuts and a rise in benefits – chime with this.

As slow growth persists, we're hearing mounting concerns around the potential for supply chain failures – something we'll be keeping a close eye on.

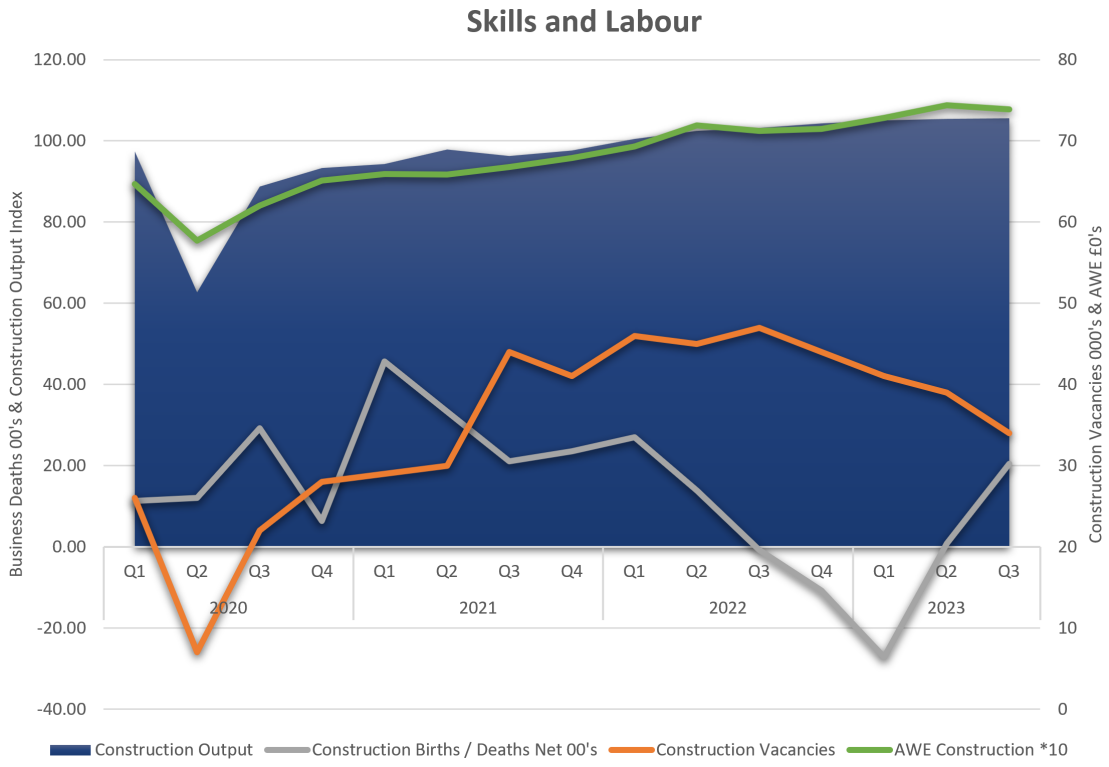
"The highest risk we envisage is the collapse of well-established businesses due to the tough market conditions over the last 2/3 years"

"Continued austerity measures adversely affecting construction investment and damaging margins potentially leading to the failure of major contractors and associated impact on supply chains"

Contractors

Looking at figures on construction company 'births' and 'deaths', the net figure plummeted in Q4 2022 as we saw a high volume of insolvencies and firms withdrawing from the sector. But, interestingly, in the last two quarters, this figure has crept up.

Graph 1

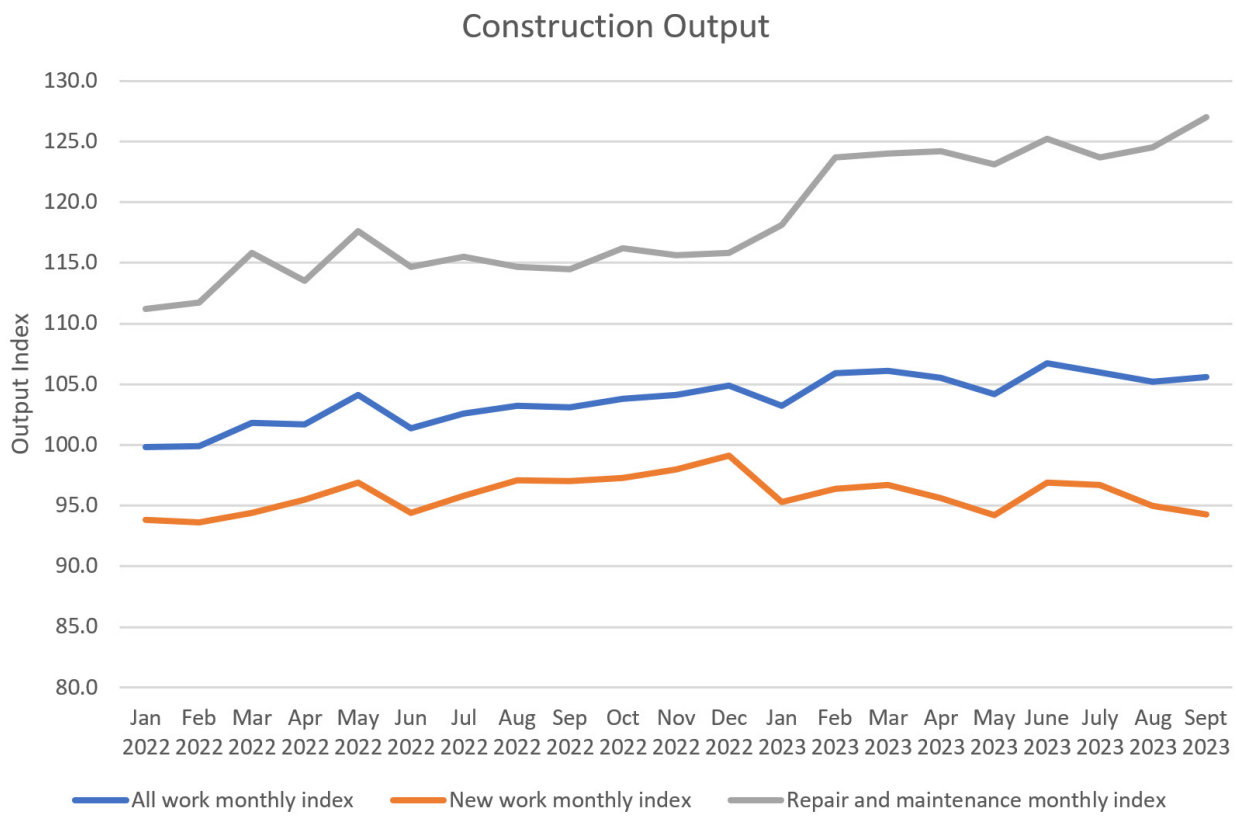


This may be an early sign of the construction industry picking back up again. Or it could be down to the fact that there was such a substantial decline in the number of building companies operating in 2022 that things are beginning to revert back to normal.

Output

Another explanation for this hike in construction 'births' could be the transition from new build work to repairs and maintenance. We're seeing a big shift from stock development to stock improvement, something that aligns with earlier views from the sector where there's been a renewed focus on decent homes and fire safety. New firms may be entering the market to meet demand around repairs and remediation.

Graph 2



This shift of budgets from development to upgrades may prove challenging when economic growth returns, and new build construction taps are turned back on. Will contractors be able to entice labour away from repairing existing homes and back onto building sites? And how will this play out in wage bills?

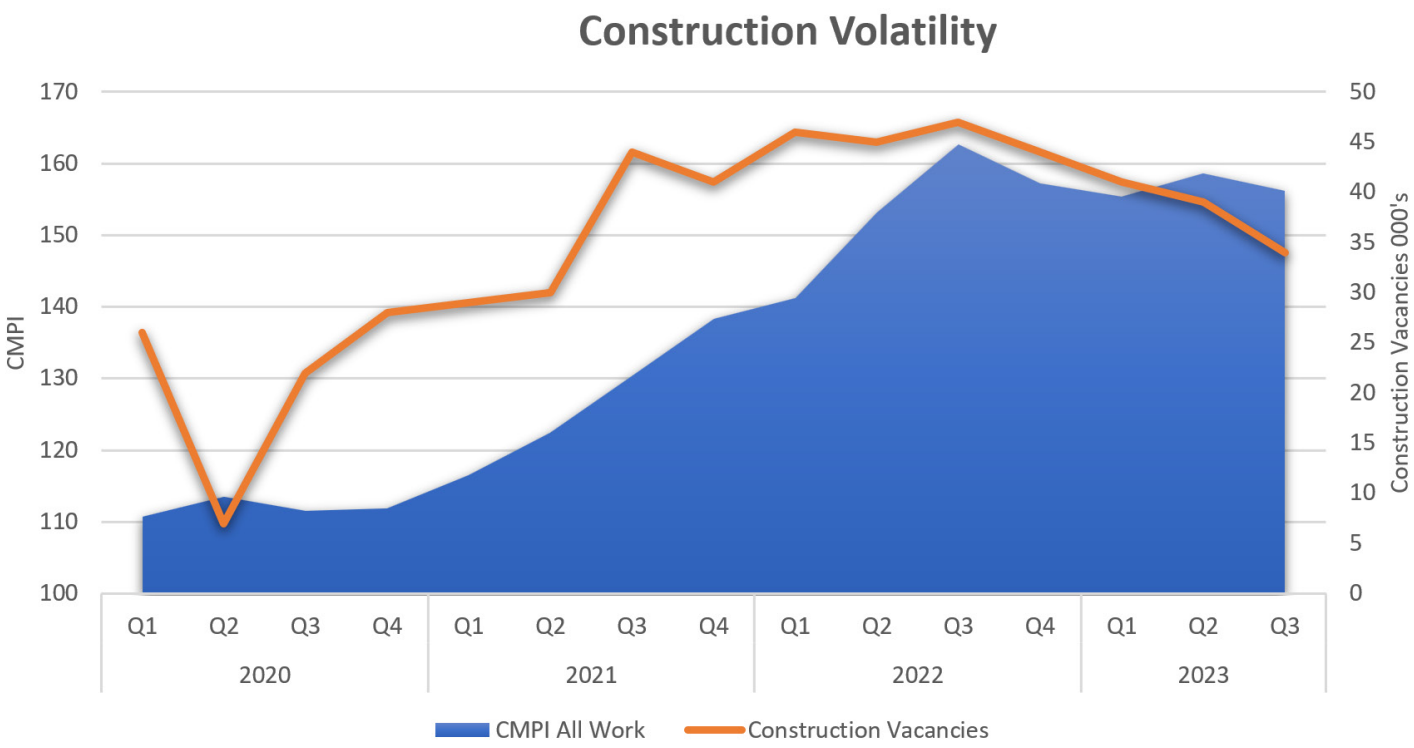
Graph 1 shows the continued upward trend in the cost of labour - average weekly earnings have been rising steadily since Q3 2022. Worryingly, this growth in wages is bucking the wider construction output trend.

"To maintain qualified staff we have had to increase hourly rates to ensure our qualified guys don't move elsewhere"

"Cost of labour impacted by cost of living, still a concern"

As new businesses have entered the construction sector, we've seen construction vacancies decrease and wages have continued to climb. If this is the picture at a time of limited construction output, housing providers need to think about what might be round the corner when growth does return – and prepare for it now.

Graph 3



People

In line with the skills crunch reported earlier by housing providers, we asked manufacturers, merchants and contractors how concerned they are about a current or future skills shortage, on a scale of 1-10 (10 being most concerned). This metric has risen by 1.4 points from last quarter to 4.8 – demonstrating mounting anxiety.

"Challenges include bringing skilled operatives into the business. Shortage of available labour to recruit is a concern"

"Employment inflation causing a shortage of skilled employees in our customers organisations meaning they will have to subcontract to maintenance contractors rather than being able to carry out all the work themselves"

"Product supplies have in the main stabilised, the biggest problem we are faced with is finding/training good installation teams"

Some suppliers told us that apprentices are no longer providing enough capacity to fill the labour shortfall, so they are upskilling existing staff, too.

"Speaking with colleagues within our industry, we feel labour will be an issue - Although we have a strong apprenticeship line, this alone will not be enough, so we are investing in upskilling current and new employees"

The supply chain is tackling this issue head on, putting a range of measures in place.

"...availability of 'good' people is the biggest challenge... so we have 3 main initiatives...
1. We use a reward specialist consultant to benchmark...remuneration for all roles
2. We have an apprenticeship programme in place for younger people to be trained up
3. We continue to identify 'rising stars' within our business and look to train and develop them"
"Increase in people needing works due to the upcoming digital changeover. We have purchased a company and are upskilling our staff to cope with this predicted increase in demand"

"Constantly recruiting and taking on increased numbers of apprentices"

"Labour/skills shortage is long term issue - trying to partner with colleges"

"Looking to recruit via apprentice placement and upskill our current resource"

Although the supply chain is doing more to manage labour headaches, they're also telling us that the situation is wearing thin. So, when construction growth finally kicks back in, how will suppliers (and the housing providers procuring their services) cope? Will housing associations and local authorities upskill their own operatives, boost the size of their Direct Labour Organisations (DLOs) and recruit new inhouse expertise to offset the risk?

We're also hearing fears that when there is an uptick in construction again, workers who've been trained in new skills may leave their jobs and follow better wages and fresh opportunities in other sectors.

"Building trade skills shortages, as many SHDF funded programs roll out, demand on electricians/ plumbers to enter retrofit markets is increasing, potentially leaving gaps in traditional social housing funded work. A disparity may grow in wages between private and public which may impact ability of landlords to run DLO teams efficiently"

It still feels like there is no concerted effort to address this systemic skills problem. It's been a challenge for the past twenty years and the Construction Industry Training Board is now predicting that 225,000 workers are needed by 2027 to meet UK demand.

Everyone points the finger at government but what about the supply chain and social landlords themselves? A collaborative, system-wide approach is required to make the building industry attractive to work in, particularly for new recruits needed to replace the many thousands of construction workers retiring over the next 10-15 years.

Prices

There's been a jump in the proportion of suppliers expecting a rise in product and service costs. In our last Sentiment Report this figure was 52%, but it's now increased to 79%. Contractors are the ones pushing this figure up - a massive 88% forecast price hikes compared to 54% three months ago.

Graph 4



In terms of price range, the majority of manufacturers and merchants expect to see increases of around 0 – 5% in the next six months. A few merchants, however, think prices might actually drop.

It's contractors again who are forecasting a wider range. Graph 4 shows some outliers falling into a 0 - 15% range, although most contractors anticipate between 5 – 8% price rises.

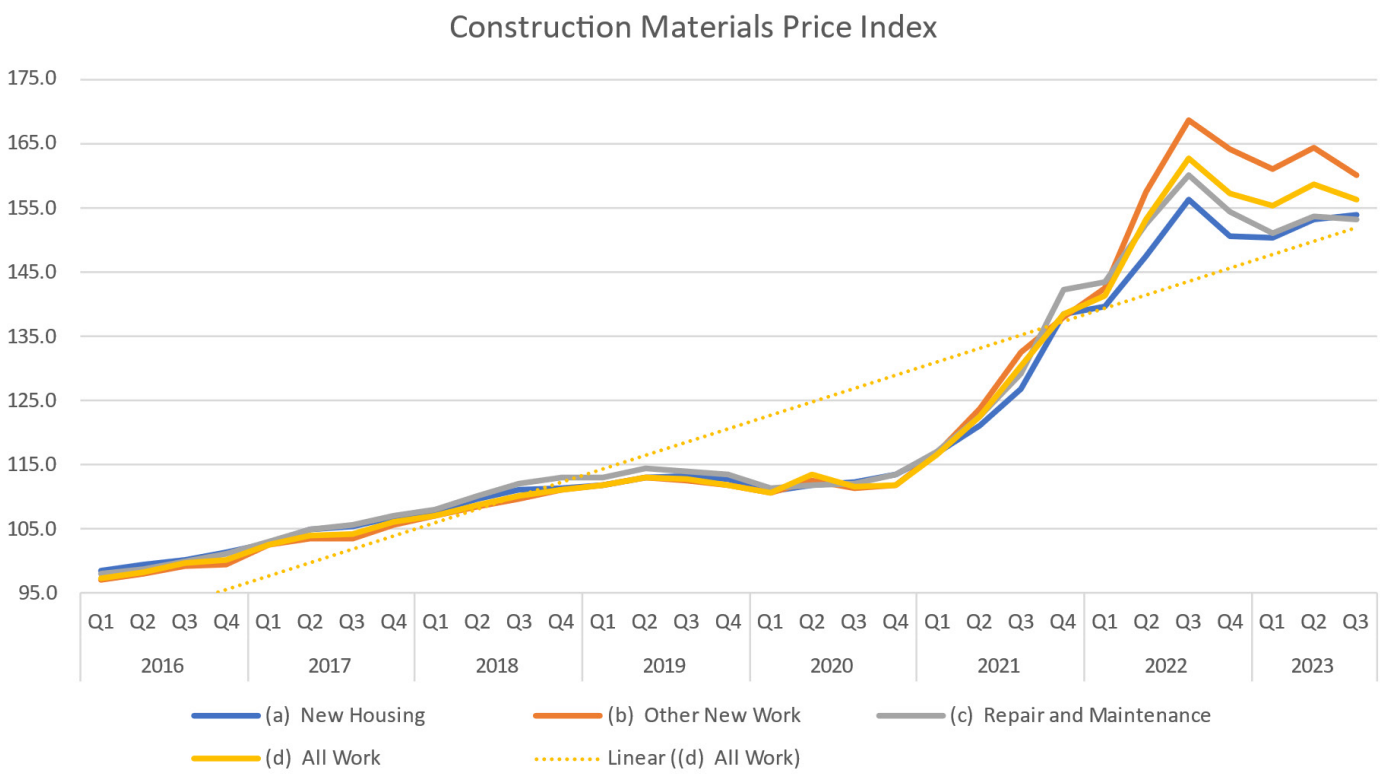
Inflation remains the primary driver around prices hikes - 50% of suppliers cited it as a contributing factor - although this figure has dropped from last quarter, when it stood at 60%. This is reflective of a softening in price rises as the economy stabilises. Indeed, UK annual inflation fell to its lowest rate for two years in the autumn due to cheaper gas and electricity.

However, inflation is still impacting supplier wage bills and training costs. A substantial 87.5% of contractors told us they are seeing an increase in their cost base around labour.

> "Good people are difficult to find and some of our suppliers are having to now pay more than minimum wage for their operatives and thus wage inflation coupled with an increase in logistics costs because of high fuel prices will also drive costs up"

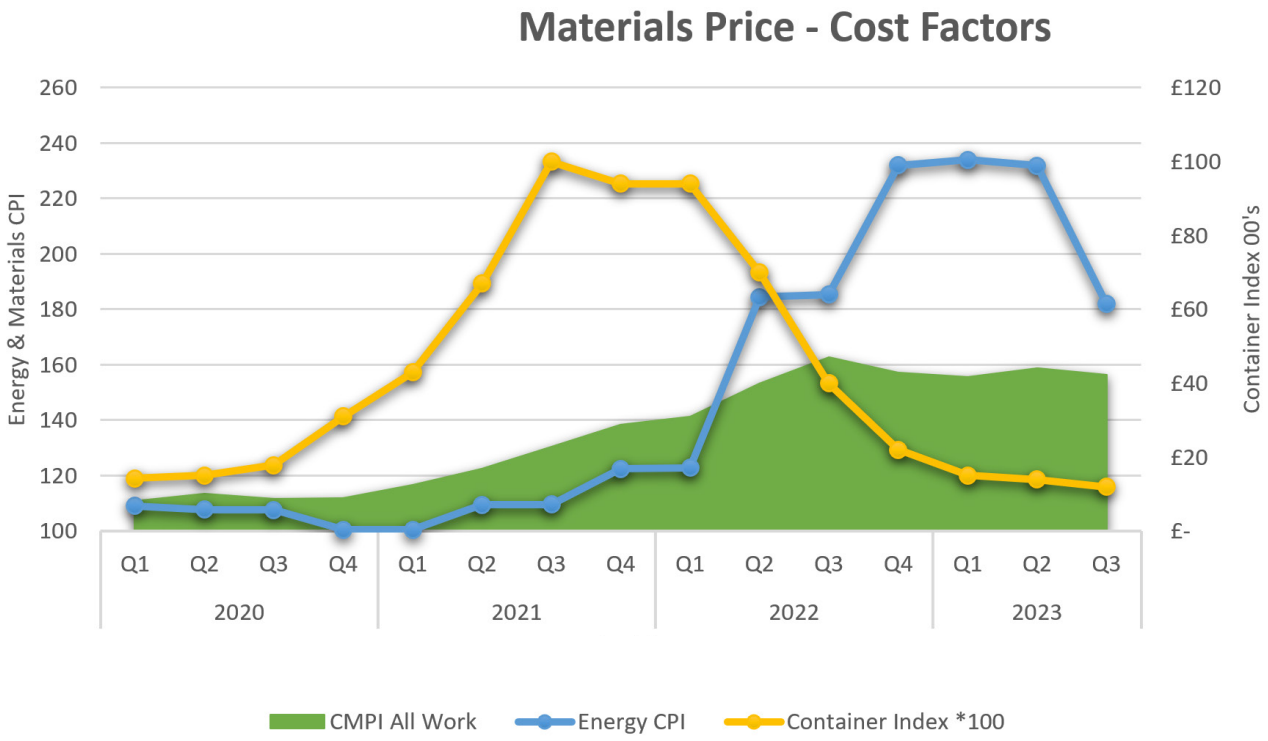
In terms of materials, it's a more encouraging picture. We're seeing the cost of building materials fall after a peak in Q3 2022.

Graph 5



Energy, too, has come back down in the last quarter and the container index continues its descending trend.

Graph 6



These structural cost factors all indicate a more positive outlook for 2024 – they will just take a little time to feed through into all prices.

As we've said in previous Sentiment Reports, the moment housing organisations feel this impact will depend on their price review cycle. Those that priced in Q2 last year may have seen a marginal drop or at least stasis, 12 months on. But those that reviewed prices in Q3 2022 – when costs were hurtling back up – should now start to see a much more positive picture filter through.

Merchants

There's been a change in market dynamics in the merchant sector. In times of economic slow-down, contractors fill their order books with public sector work to make up for the dip in private sector projects. What we've noticed is that merchants are now doing the same. With a dramatic fall in private development and new build spend (prompted partly by a declining domestic extension market) merchants are now relying more heavily on public sector income.

At the same time, we're also seeing a greater demand for merchant specialisation from public sector customers. More housing organisations are opting for full service and van stock management solutions with delivery of products to their operatives or specialist branches - rather than using traditional merchant networks.

As a result, we're likely to see a shift across the merchant market in 2024, be that mergers and acquisitions, consolidation or divestment of branches.

Optimism Score

Manufacturers: 8.4%



Merchants: 10%



Contractors: 8%



The confidence picture remains similar to last quarter with an overall score of 8.8% (down just 0.04%). Contractor optimism, however, has dropped nearly 1%, impacted by anticipated price rises and skills shortages. However, the mood of merchants is buoyant – up 1.4% - despite a potential shift in market dynamics.

This overall sentiment follows a general feeling of stagnation in the supply chain. Manufacturers, merchants and contractors are all expecting (and prepared for) a prolonged period of sluggish growth in the first half of 2024.

Analysis

So, what does all of this mean for social landlords?

> ***"Batton down the hatches. There's a broad realisation that growth in the next year will be slow but suppliers are ready for it. 2024 is expected to be a steadier year. However, the last thing we need are any global challenges. That's when we may see real difficulties amongst the supply chain."***
>
> ***"The overall message to suppliers from the housing providers we've been speaking to is 'be collaborative' and 'work with us'. There is a sense that everyone will have to adhere to new procurement rules, so the best way forward is to join forces."***
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> ***"We're at a crossroads when it comes to procurement reform and how housing organisations will manage their KPI requirements in 2024. Some will do well – working in partnership with their supply chain to measure KPIs and use them as contractual relationship levers. Others that use KPIs as a stick to beat and shame their suppliers won't do well. I think 2024 is going to be the year of contract management and housing providers need to think carefully about the right approach."***

Checklist for PfH Members

What actions should social landlords consider in response to this market intelligence?

Collaborative contract management is key

Under the Procurement Act (which comes into force in October 2024), housing providers will have to collect data and share key performance indicators (KPIs) on their higher value contracts. This will require careful planning from social landlords, particularly around how they work with the supply chain on measures and milestones.

Forcing set targets on to suppliers and then calling them out for non-performance won't work in the long-term. But, if a housing organisation decides to create bespoke KPIs for each contract and use them to effectively manage a supplier's performance, they need to be the right measures. There's activity happening across the sector, including different workstreams within the Better Housing Review, to determine what those milestones could be. Stay tuned to these developments and speak to other housing providers about their KPI approaches.

Grow negotiation capabilities

Procurement reform means social housing teams will have to negotiate again. After nearly ten years of restricted tenders where negotiation is banned, this is something many procurement managers are thinking about. Training is one solution and recruitment is another. Social housing can sometimes be overlooked as a sector for procurement professionals, but reform will open it up to a wider pool of talent, including private sector candidates used to negotiating. Think about how you can make your organisation as appealing as possible to new employees.

Involve suppliers in KPI-setting

As we've just outlined, there's a growing need for housing organisations to re-skill their teams in the lost art of negotiation. But another challenge lies around the potential 'name and shame' culture that could spring up with new regulations. The last thing suppliers want are loads of contracts being published that show them underperforming. As a result, they might negotiate meaningless targets which they can hit each and every time. Or alternatively, suppliers may price a premium service into a contract, giving themselves bucket loads of headroom to hit KPIs.

Whatever the approach, it's going to be a challenging time for the sector under this new transparency legislation. A rule of thumb is to develop effective KPIs that all parties commit to. Think carefully about what a 'good' KPI looks like. For example, 'operational efficiency' is a metric that benefits both supplier and housing organisation.

Contact

PfH's procurement team reviews prices on behalf of Members. For more information on how PfH can support your organisation today, get in touch:

01925 282 398

info@pfh.co.uk

www.pfh.co.uk

Or alternatively you can request a call back from a member of our team **here.**

Report contributors

Thank you to the following organisations for their continued support in contributing to knowledge pool across the Social Housing landscape.

