



Supply Chain Sentiment

Q3 2023 report





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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.

Moderate economic growth predicted for 2024 by a calmer supply base who think we've seen the worst; yet skills shortage could spell trouble if pipeline picks up

Key findings

Little change in supplier confidence

↓ 0.11%

Supply is steady: just 12% of suppliers expect shortages

↓ 6%

Yet, **60%** of suppliers still say inflation is forcing up prices

Demand is static: 44% of supply base think it will remain constant

↑ 8%

Only 52% of supply chain predict rise in costs

↓ 16%

And they predict price hikes of

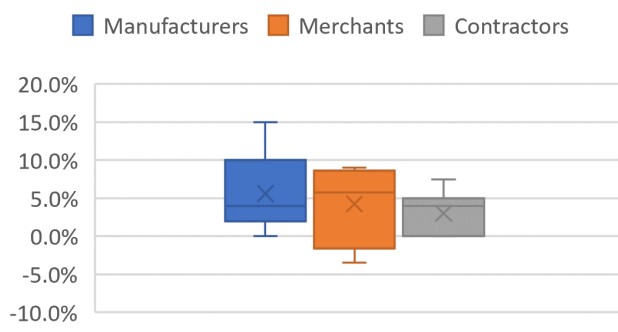
5-7% for 2024

Price expectations for 2024

Autumn is the time that many housing organisations plan budgets for the year ahead. To support this process, we wanted the Q3 Sentiment Report to provide insight on suppliers' price forecasts for the whole of 2024, not just the next six months.

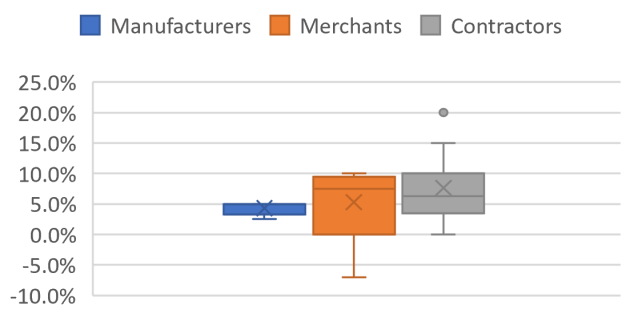
When we asked manufacturers, merchants and contractors about likely price rises for next year, the results were revealing, particularly in comparison to predictions for H2 2023.

Q3 Price Increase Expectations



Graph 1

2024 Price Increase Expectations



Graph 2

Manufacturers

When we asked manufacturers about prices for the next six months there was huge variability in their answers. Some forecast a 15% price increase, others said 10% and a few expected 3% rises or no hikes at all. This range comes from the ongoing volatility they are feeling – particularly in the fiscal environment.

“We feel that the interest rates are beginning to bite and have seen a steadying off in 2nd fixes” - manufacturer

But speaking to manufacturers about 2024, there is much more consensus. They’re all forecasting rises of between 3-5% and this narrowing of range is significant because it’s often manufacturers who feel economic and market influences first and pass these along to merchants and then contractors. They are a litmus test for what the housing sector can expect going forward and their steadier mood for 2024 provides hope that we may be entering a period of calm.

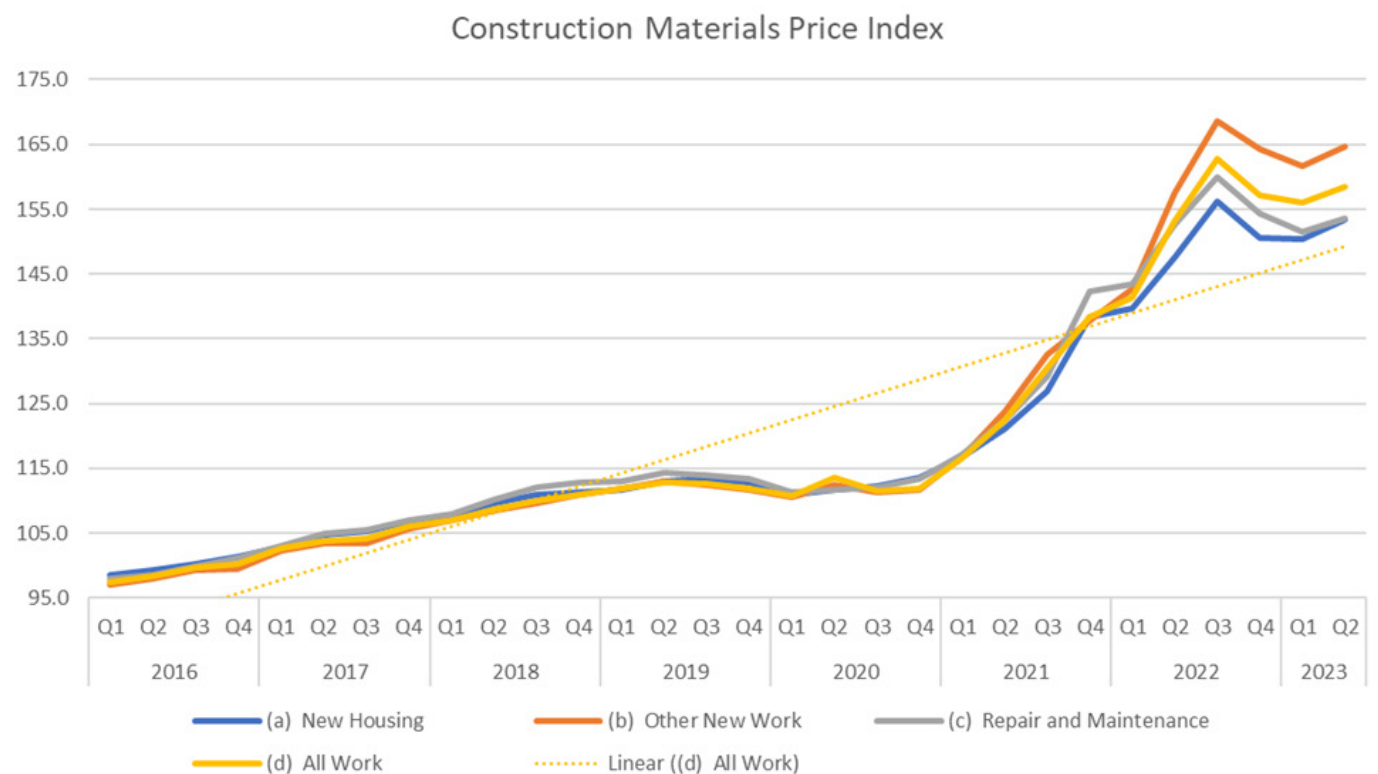
Inflation

Recent figures from the Office for National Statistics support this view. In August this year, UK inflation fell to its lowest level since before Russia's invasion of Ukraine.

Despite this steadier economic picture, 60% of the suppliers we spoke to cited inflation as a contributing factor to price rises over the next six months. Although this is down 8% from last quarter it could indicate that inflation for inflation’s sake is still happening in the supply chain. This is something to challenge with your supply chain if it’s unjustified.

Materials

The quarterly construction price index shows that materials prices are still unstable.



Graph 3

Prices took a downwards trajectory from Q3 2022 through to Q4 and then Q1 2023. But there was an uptick in the second quarter of this year as high inflation hit home.

Whether or not you're feeling this hike in materials prices will depend on when you last reviewed your prices. Q2 2022 and Q2 2023 prices rose by 3% only, so if you reviewed in July last year you shouldn't feel much difference 12 months on.

But in Q3 last year, prices began a speedy rise due to economic challenges. Merchants priced in risk as they just didn't know how long this spike would last. So, 12 months on, merchants should be starting to price out some of that risk and the cost of products ought to drop, or at least remain static.

Housing providers need to understand the complexities of this cycle and look not just at prices now, but predictions for the next 12 months and the risk profile this presents.

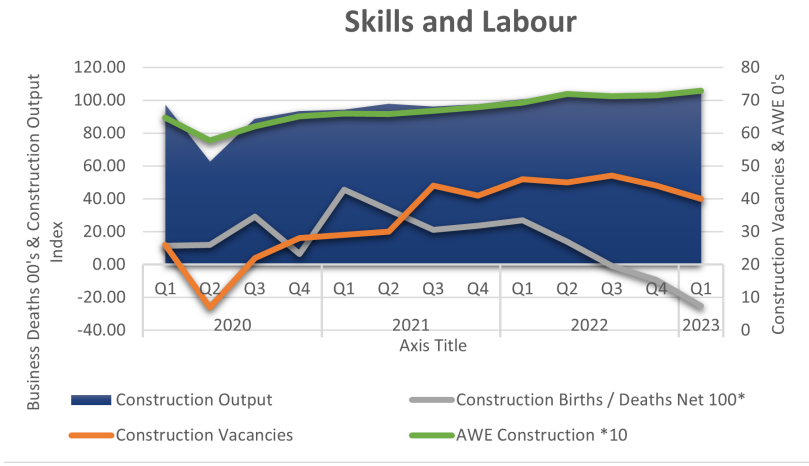
Contractors

Contractors' price increase expectations for the next six months were lower than manufacturers' and merchants'. Most told us they thought prices would rise between 0-6% and there weren't many outliers. This view stems from the current contraction of the construction industry with contractors having to compete more for work. Growth has been fairly static with an uptick in contractor company 'deaths' - more info on page 4.

But when we asked contractors about 2024, the majority forecast a greater increase in prices - with a few expecting hikes of 15 - 20%. Overall, there was a sense that contractors are expecting demand to improve next year and prices to adjust for higher wages accordingly.

People

Stagnant construction demand resulted in a net drop in the number of construction companies operating in the UK. In Q1 2023 there were just under 80,000 new building firms set up. But in the same period, 106,000 companies went bust - so there was a net loss of 27,000 businesses in Q1. Q2 saw further net loss of 7,000 businesses, bringing the total for H1 to over 34,000.



Graph 4

Graph 4 shows that construction vacancies have come down too – no surprise following a dip in the number of firms operating in the sector and therefore recruiting people.

Conversely, we're also seeing an increase in average weekly earnings in construction. This indicates that construction organisations haven't been taking on more work or employing new people, rather they've been paying their existing staff more to retain them.

That is a worrying sign and points to the persistent construction skills shortage, something the government is attempting to tackle by relaxing immigration rules. Bricklayers, roofers, carpenters and plasterers have been added to the shortage occupation list (SOL) which means migrant workers in these occupations are eligible for the Skilled Worker visa. Less stringent Home Office requirements also apply to firms interested in recruiting for such roles.

Despite this government intervention, if building firms are already paying their workers more in challenging times, when output does pick up again (as forecasts suggest it will in 2024) there will be some major recruitment and wage challenges ahead.

"Potential Shortage of qualified engineers"

"Good engineers come at a premium"

"Cost of living and shortage of skilled engineers is increasing prices"

"Reviewing databases for new suppliers, subcontractors and continuous interviews for new staff"

For housing providers, those challenges translate into higher costs. So, are the significant 2024 price hikes predicted by some contractors (a few said they were expecting 20% rises) being driven by higher labour costs?

Contractors will have to pay more for construction labour, so where housing organisations have existing repairs and maintenance workers, for example, these people may be tempted by the prospect of higher wages if they move to the private sector.

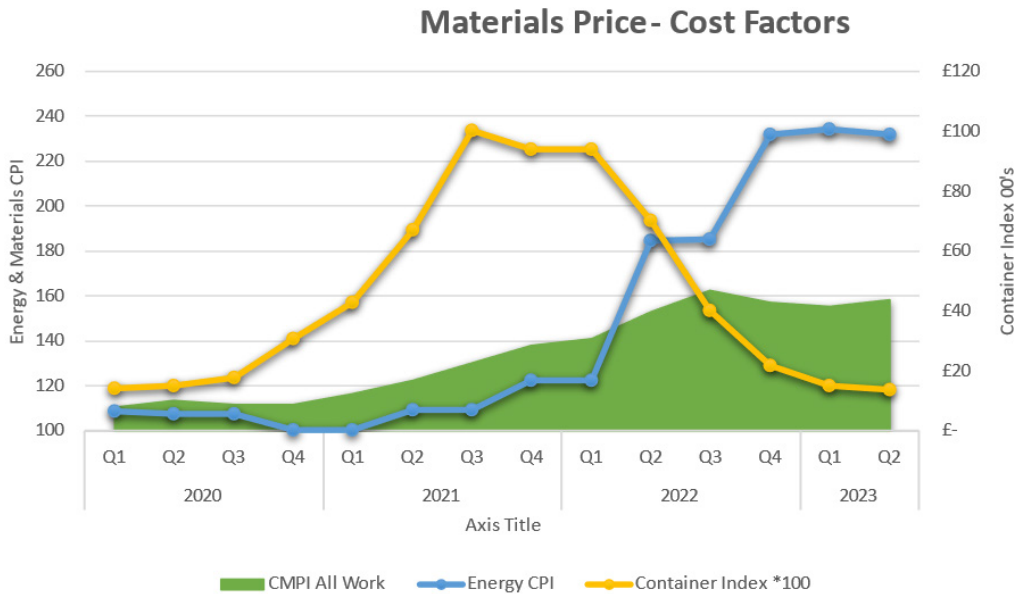


Costs

Half (52%) of all manufacturers, merchants and contractors are expecting an increase in construction costs over the next six months. This is down 16% from last quarter and reflects the mood of relative calm we're seeing amongst the supply base.

As we mentioned earlier, suppliers are still citing inflation as a main driver when we asked them about price increases. If your suppliers echo this, then it's worth investigating what their cost base looks like. Yes, there has been an increase in labour costs, but what we haven't seen is an increase in energy costs - they actually petered out following a peak in Q4 2022 and have been fairly static ever since.

We've seen the shipping container index revert to pre-pandemic, normalised rates. Materials costs, too, have been relatively stable with no substantial shortages.



Graph 5

“We have seen costs for materials & labour stabilise recently which we forecast to continue”

So, barring any unforeseen disasters, it looks like we're in a more settled period from a cost base perspective.

China and Taiwan

This quarter, we asked suppliers for their thoughts on the potential crisis between China and Taiwan and how that could impact their business on a scale of 1-10, with ten being an existential organisational threat. As expected, manufacturers were the most worried, scoring an average of 4, with merchants at 3 and contractors the least concerned at 2.77.

Although pulses are slightly raised, there wasn't any sense of pending doom around this conflict and what it could mean for construction in the UK. Could this be down to suppliers' new attitude of 'what will be, will be'? Over recent years they have dealt with global macro event after global macro event and resilience and preparedness levels are now at an all-time high.

“Don’t believe we have a major issue as we’re stockpiling components well in advance and have already built a mitigated allowance into stockholdings”

“Supply of raw components [could be an issue]”

“Plans to mitigate already in place with increased order of raw components”

“Certain suites will become un-obtainable, we may have to offer more expensive options which could hurt margins, but we are committed to our customers”

“Raw material costs will no doubt increase. Supply costs will then increase. Lead times for materials will increase”

Supply

As mentioned above, supply of materials has stabilised, something reflected in suppliers’ predictions this quarter. Only 12% said they were expecting shortages for their products, services or works in the next six months, down 6% from last quarter.

“No issue [on supply]”

“Supply is very stable currently”

“No issue with supply”

“Shipping from China still remains precarious”

Micro-chip shortages are no longer a problem. For the housing sector, boilers were the main area impacted by this scarcity and that supply line has stabilised.

Demand

Like the supply environment, demand is reasonably static – prompted by a slowdown in output. The high demand environment of previous years just isn’t here right now.

When we spoke to manufacturers, merchants and contractors for this report, a significant 44% told us they expect demand to remain static over the next six months, compared to 36% last quarter. Indeed, most of the challenges that previously impacted demand have disappeared.

“We have sufficient labour & recourses to manage current demand”

Optimism score

When we asked manufacturers, merchants and contractors how confident they feel about the success of their business in the next 12 months, the average response was 8.84%, not far off last quarter's score of 8.95%.

Suppliers might be a touch less optimistic this quarter than last, but it's a marginal dip. This speaks to the general feeling of stasis in the sector. Everyone is in a holding pattern, waiting to see what happens economically. The sector's mood might well be frozen like this for the next six months with no real movement until 2024 when growth is predicted to begin again.

Manufacturers: 9%



Merchants: 8.6%



Contractors: 8.92%



"Contracts seem to be ticking along nicely during the summer months. Clients seem more confident in starting previously shelved projects"

Analysis

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

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"There are signs that H2 2023 may well be a phase of 'nothingness' - a calm period of reflection where we all let the last few years settle in the hope that there are no more sudden crises. If this turns out to be the case, it could mean that 2024 will be a normal year too."

"We still haven't seen the 'recession that never arrived', underlying cost rates are static, as is demand and supply. Everything indicates that suppliers aren't worried, but they're ready to put mitigation in place if needed. Supply chains are more resilient now than a few years ago and there is less concern about how they might cope with significant events."

"There is a palpable sense of waiting and seeing. Things have returned to normal and we're all just holding fire to see what the next few months will bring."

Checklist for PfH Members

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

Budget for 5-7% price rises

By asking suppliers for their 2024 price forecasts, we wanted to brief housing providers on what to prepare for. When you're setting next year's budgets, we recommend you plan for between 5-7% rises. If your organisation is heavily reliant on contractor-led services, then it's worth keeping a very close eye on construction demand. If that gathers pace in H2 2023 then the cost of services will rise too. Construction firms often fill their order books with public sector work when the economic outlook is negative but if output accelerates then we may well see a migration to private sector work, leaving housing authorities with higher costs and a shortage of builders.

Procure now

If there is economic growth in 2024 then construction (and contractor prices, particularly) may become more volatile. So, now is a good time to procure contracts because we're in a relatively stable environment. It may not feel like it with talk of inflation, but overall, things are pretty steady. Demand is flat, as is output. Contractors have filled their order books with public sector work to help with their risk profile. But as soon as we see an uptick in demand, prices will skyrocket from a contractor perspective. So, buying now and putting a long-term contract in place, before output begins to climb, will enable you to offset unpredictable pricing over the next 12 - 18 months.

Put tools in place to tackle price volatility

If you do procure a number of contracts while the economic landscape is calm, make sure you have the right contractual mechanisms in place. There are different tools to help you address an inflationary environment within the term of an agreement.

For example, a three-year contract could be linked to some form of price index, or it could include a maximum price increase. There are different ways you can increase your bargaining position when it comes to price management.

Prioritise works

Identify what's essential and what can be pushed back if costs increase markedly. For instance, given the ongoing focus around living standards (including damp and mould) and also tenant bills, works around these areas may need to take priority over planned kitchen and bathroom refurbishments.

Be ready for labour shortages

We've talked about the skills gap in construction for years and people seem to get by, work still gets done. But take heed of price rises predictions from some of our respondents this quarter - up to 20% (see page 2). In a relatively stable product environment, these figures are being driven by increased wage costs. The volatile conditions that have dominated headlines for the past few years have masked the growing skills challenge. It's worth planning for this problem now - both in terms of your contractors but your own workforce too.

How can you make your organisation more attractive to construction workers? Benefits are much better for staff in the public sector, so that's something to emphasise over private sector employers. But it's the challenge of attracting a younger, more diverse construction workforce to your housing organisation that's one to focus on.

Cutting edge, renewable technologies might be a pull for younger workers. Think about how you can make inhouse construction careers more appealing to women and people from a wide range of communities, so they're seen as welcoming, flexible and exciting roles.

"We have a solid direct model and unique graduate training centre"

"We are engaging with a local Training academy and widening our sub contractor base"


Report contributors


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



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:

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