

COST UPDATE

The quarterly analysis of changes to costs and prices shows many costs beginning to rise. **Peter Fordham** of **Davis Langdon** reports

01 / KEY CHANGES

- ▲ All of the construction cost index series now on an upward trend
- ▲ Consumer price inflation overshoots target by large margin
- ▲ Industry input costs experience resurgence of cost pressures
- ▲ Industry output prices begin to rise in response
- ▲ Construction materials prices show sharp rise over last six months
- ▲ Electricians get 5% wage increase and steel erectors 2%
- ▶ Wages remain frozen for builders, plumbers and heating and ventilating operatives

Percentage change year on year (fourth quarter 2008 to fourth quarter 2009)

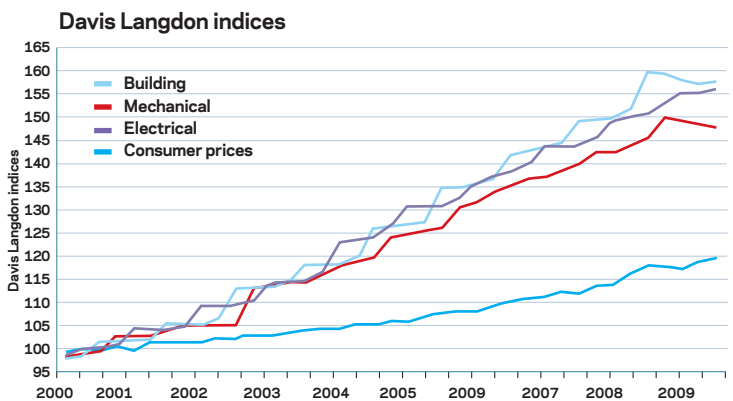
	%	Trend
Building cost index	-0.4	▲
Mechanical cost index	-1.2	▶
Electrical cost index	3.8	▲
Consumer prices index	2.1	▲

(Fourth quarter 2009 figures are provisional)

Building cost index The index rose 0.8% in the fourth quarter as materials prices returned to an upward trend but still shows a year on year fall.

Mechanical cost index The previous three quarters of decline in the index was halted in the fourth quarter last year. The index was virtually flat for the last seven months of 2009 but recorded a year on year fall of 1.2%, the first annual drop since 1999.

Electrical cost index Electrical contracting is the sector with the highest inflationary trend as materials prices rose strongly in the second half of 2009 and labour costs rose at the beginning of 2010.



Guide to data

Davis Langdon's cost indices track movements in the input costs of construction work in various sectors, incorporating national wage agreements and changes in materials prices as measured by government index series. They provide an underlying indication of price changes and differential movements in the various work sectors but do not reflect changes in market conditions affecting profit and overheads provisions, site wage rates, bonuses or materials' price discounts/premiums. In the current market, many costs recorded here are rising but prices charged to clients are still falling. Market conditions are recorded in Davis Langdon's quarterly market forecast (last published 29 January).

02 / PRICE ADJUSTMENT FORMULAE FOR CONSTRUCTION

Over the last 12 months between February 2009 and February 2010, the 60 Building Work categories have recorded an average rise of 1.4% but over the last six months between August 2009 and February 2010 an average rise of 2.0% has been recorded, illustrating how the trough of the cost trend occurred mid Summer last year.

Sixteen work categories still show a price decline over the last year (compared to 32 categories six months ago). In most cases the decline is now less than 2% but some steel based categories still show higher price falls over the last year:

% change	Feb 09-Feb 10	Aug 09-Feb 10
Piling: steel	-9.6	0.5
Concrete reinforcement	-8.8	-1.0
Metal: miscellaneous	-5.8	0.5
Fencing	-4.2	2.5

The work categories that have seen the greatest price increases come under three headings: metals, timber and oil, which have all suffered substantial price increases.

% change	Feb 09-Feb 10	Aug 09-Feb 10
Cladding and covering: lead	19.0	15.2
Windows and doors: softwood	9.1	4.6
Pavings: coated macadam	9.6	4.2
Softwood carcassing and structural members	8.1	4.4

Copper, lead and zinc prices rose by more than one and a half times over the year to January (though have since slipped back a little) and these price increases are still feeding into the price of metals products.

The price adjustment formulae indices are compiled by the Department for Business Innovation and Skills.

They are designed to help with the calculation of increased costs on fluctuating or variation of price contracts. They also provide useful guidance on cost changes in trades and industry sectors and on the differential movement of work sections in Spon's Price Books.



Materials Inflation is back, thanks partly to VAT reverting to 17.5% and a weak pound

03 / EXECUTIVE SUMMARY

- ▲ Consumer price inflation leaps as higher rate VAT is reintroduced
- ▲ Industries' input costs rise on the back of higher gas prices
- ▲ Industries' output prices edging steadily upwards
- ▲ Construction materials' prices show year on year increase for first time since last April
- ▲ Electrical materials prices have risen sharply in response to copper prices
- ▶ Steel prices show large year-on-year price falls but may have stabilised

04 / KEY INDICATORS

	% change, Jan 09-Jan 10	July 09-Jan 10
Consumer prices index	3.5	1.4

The annual rise in consumer prices has accelerated since last October, reaching 3.5% in January. The rise in inflation has been attributed to the past depreciation of sterling, the 25% increase in fuel costs over the year and, most recently, to the re-introduction of 17.5% VAT. Inflation is likely to drop back below the 2% target by mid year.

Industry input costs

Materials and fuels purchased by manufacturing industry	8.4	7.7
Materials and fuels purchased by manufacturing industry excluding food, beverages, tobacco and petroleum	1.8	5.1

The annual percentage change in industry's input costs has swung from -12.2% last July to +8.4% in January with the bulk of the rise occurring in the last six months. The big difference in the headline figure and the lower 1.8% annual increase recorded by industries other than the food, beverages, tobacco and petroleum industries lies in the 71% increase in the price of crude oil over the 12 months to January. However over the last six months, costs for the reduced sample of industries have risen by nearly as much and the main contributor has been gas prices which have fallen 25% over the year but have surged by 41% since September. This is a normal seasonal effect but the increase is considerably larger this year than last year's 27% rise over the same period.

Industry output prices

Output prices of manufactured products	3.8	2.3
Output prices of manufactured products excluding FBT&P	2.5	2.0

Over the first half of the period, the headline inflation figure was largely driven by a substantial increase in the price of petroleum products. Over the second half, output price inflation has been edging steadily upwards over a broader front. Output price inflation in those product areas most associated with construction has varied:

	% change over year to January 2010
Wood and wood products	1.7%
Rubber and plastic products	0.8%
Fabricated metal products	-0.9%
Electrical machinery and apparatus	4.0%
Recovered secondary raw materials	21.2%

The decline in prices in fabricated metal products reflects the fall in steel prices that occurred in the second half of 2008 and first half of

2009 but prices have now risen nearly 2% since last September.

The increase in prices for electrical machinery and apparatus reflects the steady rise in copper prices that has occurred for most of the last year. There has been a new surge in scrap prices, lifting the price of recovered secondary raw materials 15% between November and January. Steel scrap prices have risen 27% over those two months.

Construction industry

Construction materials price increases last year are detailed below:

	% change, Dec 08-Dec 09	June-Dec 09
Construction materials generally		
New housing	2.3	2.5
Non-housing new work	-1.0	2.3
Repair and maintenance	2.0	3.4

Overall construction materials prices rose by just 0.3% over the year to December but rose by 2.7% over the last six months. The differential movement over the twelve month period between non-housing new work and the other sectors reflects the greater weighting in the former of steel, which suffered a price collapse in 2008/9. The increase in materials prices over the last six months shows a recovery in a number of materials as detailed below.

	% change, Jan 09-Jan 10	July 09-Jan 10
Mechanical services materials		
Housing	-2.0	1.0
Non-housing	-2.2	0
Electrical services materials	6.3	5.1

Materials showing significant price shifts over the last 12 months and the latest six months are shown below (Data sources: ONS and BIS.

January 2010 figures are provisional):

	% change, Jan 09-Jan 09	July 09-Jan 09
Imported copper	68.1	31.9
Gas oil fuel	24.3	19.1
Insulated wire and cable	17.1	15.3
Timber	13.0	13.9
Crushed rock	12.3	-3.0
Macadam	11.3	4.0
Safety glass	4.8	12.1
Sand and gravel	-5.7	1.9
Ready mixed concrete	-7.2	-2.6
Reinforcing steel	-14.3	-2.1
Metal sections	-15.8	-0.5
Structural steelwork	-18.3	0.5
Sheet steel piling	-21.0	-0.6

Labour Redundancy and pay freezes are prevalent but electricians buck the trend with an increase

05 / EXECUTIVE SUMMARY

- Average earnings in construction in the last three months of 2009 were 0.8% higher than a year previously ¹
- Average pay in construction last December was £557 per week ¹
- 34,000 people were made redundant in the construction industry in October-December 2009, down from the peak of 50,000 in January-March and the lowest figure since the July-September 2008 quarter ¹
- Pay freezes in operation for builders, plumbers and heating and ventilating operatives
- Wage increases in January for electricians and engineering construction workers
- Local authority craft workers face pay freeze from April (' = ONS data)

Earnings data

The normal wage review anniversary for plumbers in England and Wales is in January. This year there were no changes to rates of pay or allowances and the rates that came into effect in January 2009 will remain in place until January 2011.

Similarly rates of pay for plumbers in Scotland and Northern Ireland have been frozen at their June 2009 levels and will remain at that level until June 2011.

Heating and ventilating operatives' wage rates, effective since October 2008, have been frozen until October 2010.

Electricians however have benefited from a three-year agreement

that was promulgated in September 2007, the third and last part of which provided for a 5% increase in rates and allowances from 4 January 2010. The new national standard rates are as follows:

Grade	Transport provided £/hour	Own transport £/hour
Technician (or equivalent grade)	15.38	16.16
Approved electrician (or equivalent grade)	13.59	14.35
Electrician (or equivalent grade)	12.45	13.23
Electrical improver/senior graded electrical trainee	11.20	11.92
Labourer/adult trainee	9.89	10.62

London rates remain 12% higher than the figures shown above.

Employees under the National Joint Council for the Engineering Construction Industry have also benefited from an increase in wage rates and allowances from 4 January. Base, shift and overtime rates, welding proficiency payments, radius/accommodation allowances and NAECI sick pay all increased by 2%.

Agreement was reached last December on 2009 rates of pay and allowances for local authority craft and associated employees. A 1-1.25% pay increase was backdated to April 2009. The Local Government Association has now decided to impose a pay freeze for 2010-11 on all local authority employees. Unions want a re-think.

Wage agreement summary

The following table summarises the wage agreements currently in force for the principal wage-fixing bodies in the construction industry

Operatives	Agreement body	Current basic hourly rate	Effective since	Details in	Date of next review
Builders and civil engineering operatives	Construction Industry Joint Council	Craft rate: £10.30/hour	30 June 2008	Cost Update 30 May 2008/ Spon's Architects' and Builders' Price Book 2009	Wage rates have been frozen since June 2008; no increases programmed
	Building and Allied Trades Joint Industrial Council (BATJIC)	S/NVQ3 qualified operative: £10.41/hour	9 June 2008	Cost Update 5 September 2008/Spon's Architects' and Builders' Price Book 2009	Wage rates for 2009/10 frozen at June 2008 levels; next review June 2010
Plumbers	The Joint Industry Board for Plumbing Mechanical Engineering Services in England and Wales	Advanced plumber: £12.73/hour	5 January 2009	Cost Update 27 March 2009	3 January 2011: rates will increase by RPI at June 2010; rates for 2010 held at 2009 levels.
	Scottish and Northern Ireland Joint Industry Board for the Plumbing Industry	Advanced plumber: £12.64/hour	1 June 2009	Cost Update 29 May 2009/Spon's Architects' and Builders' Price Book 2010	6 June 2011 (rates will increase by 2%)
H&V operatives	Joint Conciliation Committee of the Heating, Ventilating and Domestic Engineering Industry	Craftsman: £11.16/hour	6 October 2008	Cost Update 5 September 2008/Spon's Mechanical and Electrical Services Price Book 2009	4 October 2010 (rates will rise by 2%); no increase in wage rates for 2009
Electricians	The Joint Industry Board for the Electrical Contracting Industry/Scottish Joint Industry Board for the Electrical Contracting Industry	Approved electrician: £14.35/hour (own transport)	4 January 2010	See above / Spon's Mechanical and Electrical Services Price Book 2010	January 2011