A highways market insight

Edward Day, head of bespoke delivery and infrastructure at the Royal Institution of Chartered Surveyors (RICS), discusses the economic perspective of the road market over the past five years and the outlook for the next five

The highways sector is experiencing a boost in output over the next five years of 20 per cent as highlighted in the latest National Infrastructure Plan (NIP). This is in stark contrast to the halving of output during the period 2010-2012. The Building Cost Information Service (BCIS) investigates recent sector costs and the impact of increased workload on prices and contractors' margins

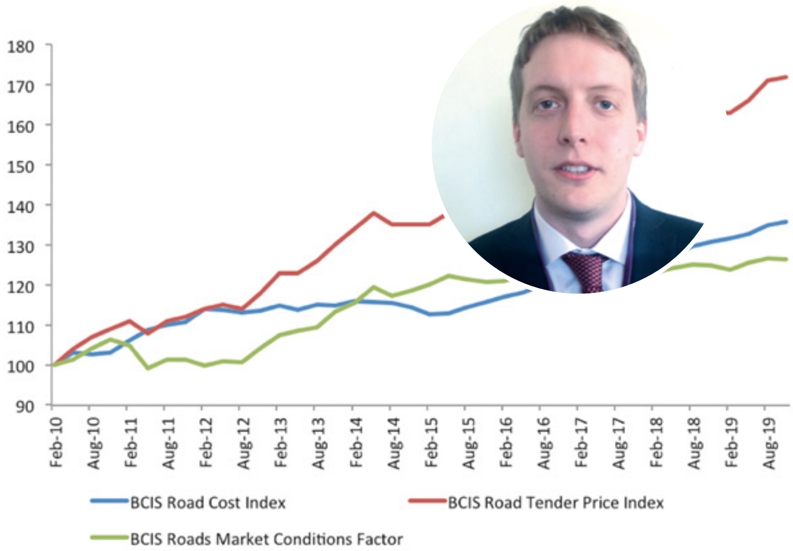
The NIP 2014 set out a pipeline of over £460 billion of planned public and private investment from 2015 to 2019. Based on the NIP the highways sector will experience an increase in new work of 20 per cent. Just under half of the investment will be channelled through Highways England. A similar amount is to be invested by local authorities, who are responsible for 98 per cent of the highways network. Highways England is expected to invest £1,767 million in 2015/16 rising to £2,959m in 2019/20.

Scotland and Wales are also expected to increased highways budgets with the Scottish Draft Budget 2015-16, highlighting a rise from £375.2m in 2014/15 to £401.7m in 2015/16. Wales similarly has announced an increase for spending on motorways and trunk roads from £71.5m in 2014/15 to £92.6m in 2015/16.

Throughout the UK, investment in the highways sector looks set to increase significantly over the next five years.

Cost trends

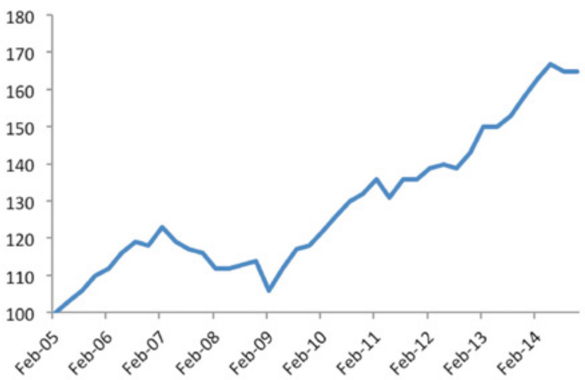
The BCIS track cost and price changes for common resources and work activities associated with the highways sector. Our Road Tender Price Index (RTPI), which is supported by the submission of project data from the sector, highlights these changes.



Looking at the sectors recent cost changes in more detail, labour costs, as measured by average weekly earnings in the construction industry, rose by two per cent compared with the same quarter a year earlier. Similarly the BCIS Labour and supervision costs indices rose slightly high by 2.6 per cent over the same period.

For civil engineering materials prices our BCIS Civil Engineering Cost Index fell by around 0.25 per cent compared with the same quarter in 2013. In most instances, individual materials prices changed between -1 per cent and 0 per cent over the last quarter. However, the price of European Brent crude oil fell by 30 per cent compared with a year earlier. Oil prices fell by around 44 per cent between June 2014 and December 2014 alone.

The commodity price of steel billet has risen, in contrast, by 97 per cent in fourth quarter 2014 compared with the same quarter a year earlier. This does, however, follow the significant falls in steel commodity prices of around 75 per cent between third quarter 2011 and second quarter 2013. However, it should be noted that the BCIS Index for 'steel for reinforcement' only fell by 10 per cent over the same period, highlighting the difference between commodity prices and actual industry costs.



Sector forecasts

The BCIS produce five-year forecasts for highway costs, prices (the contractors cost plus their margin) and market conditions.

Our roads cost forecast highlights increases over the next five years totalling a 19 per cent increase, significantly higher than third party forecasts of RPI. Tender prices are also predicted to increase over the forecast period at approximately 28 per cent, which equates to 5.6 per cent annually. This is likely to be driven by increases in underlying resource costs and contractors increasing margins in line with rising workload opportunities. Margin increases are highlighted in our market conditions forecast for the sector which estimates margins will grow seven per cent over five years.

Summary

Increases in output from 2012 have been followed by a sharp increase in tender prices and market conditions even though underlying resource costs have remained stable, and even declined over the last six months due to the oil price crash. Sustained increases in output for the sector over the next five years will likely herald increasing margins for contractors, nonetheless, underlying resource costs will also increase albeit at a lower rate.

*All data providers to the RTPI benefit from receiving a complimentary roads report which includes our five year forecast of demand costs and prices. To find out more information about what we require and the associated benefits visit **www.rics.org/bcisrtpi**. *