RIBA Quarterly Economics Report

The Architectural Market

Autumn | 2023

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Introduction

This economic report brings together information from a range of primary sources. It aims to help practices place their work within a broader economic context.

The UK economy is weak with high but falling inflation. Interest rates have risen and are likely to stay high. Anaemic GDP growth is forecast for the next two to three years.

Forecasts for the construction industry suggest contraction this year, but a return to modest growth in 2024 and 2025.

The Housing, and Housing Repair and Maintenance Sectors are performing poorly, and this is disproportionately affecting architects.

External pressures continue to suppress the architects' market as interest rate rises continue to make project financing more difficult for both domestic and commercial clients. The architects' market is currently underperforming and the coming two to three years are likely to see only modest growth.

RIBA is always here to offer help and advice where it can. RIBA Business and Career Resilience Hub and regular Professional Features provide helpful information on navigating challenging times.

RIBA Future Trends Workload Index now stands at

-11

The UK Economy

UK Gross Domestic Product

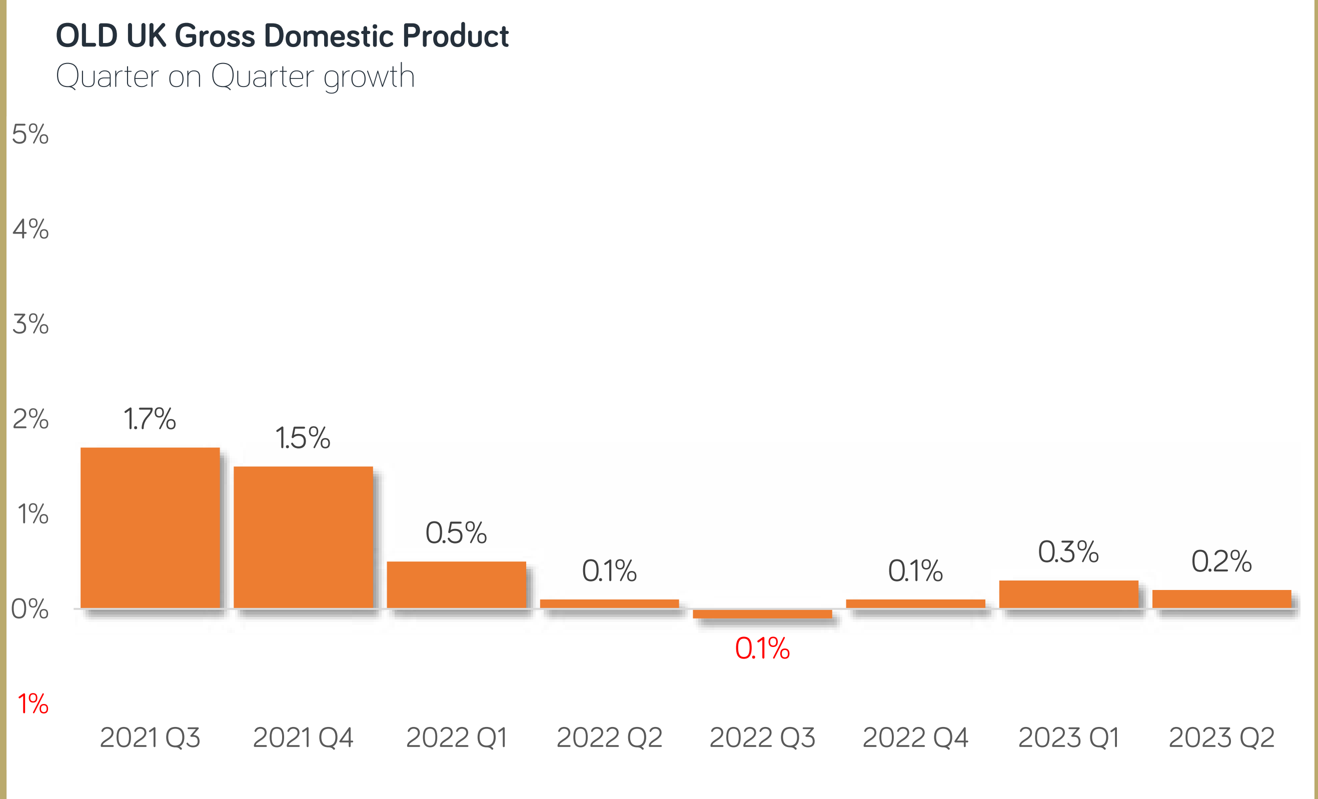
The UK economy continues to grow, but only weakly.

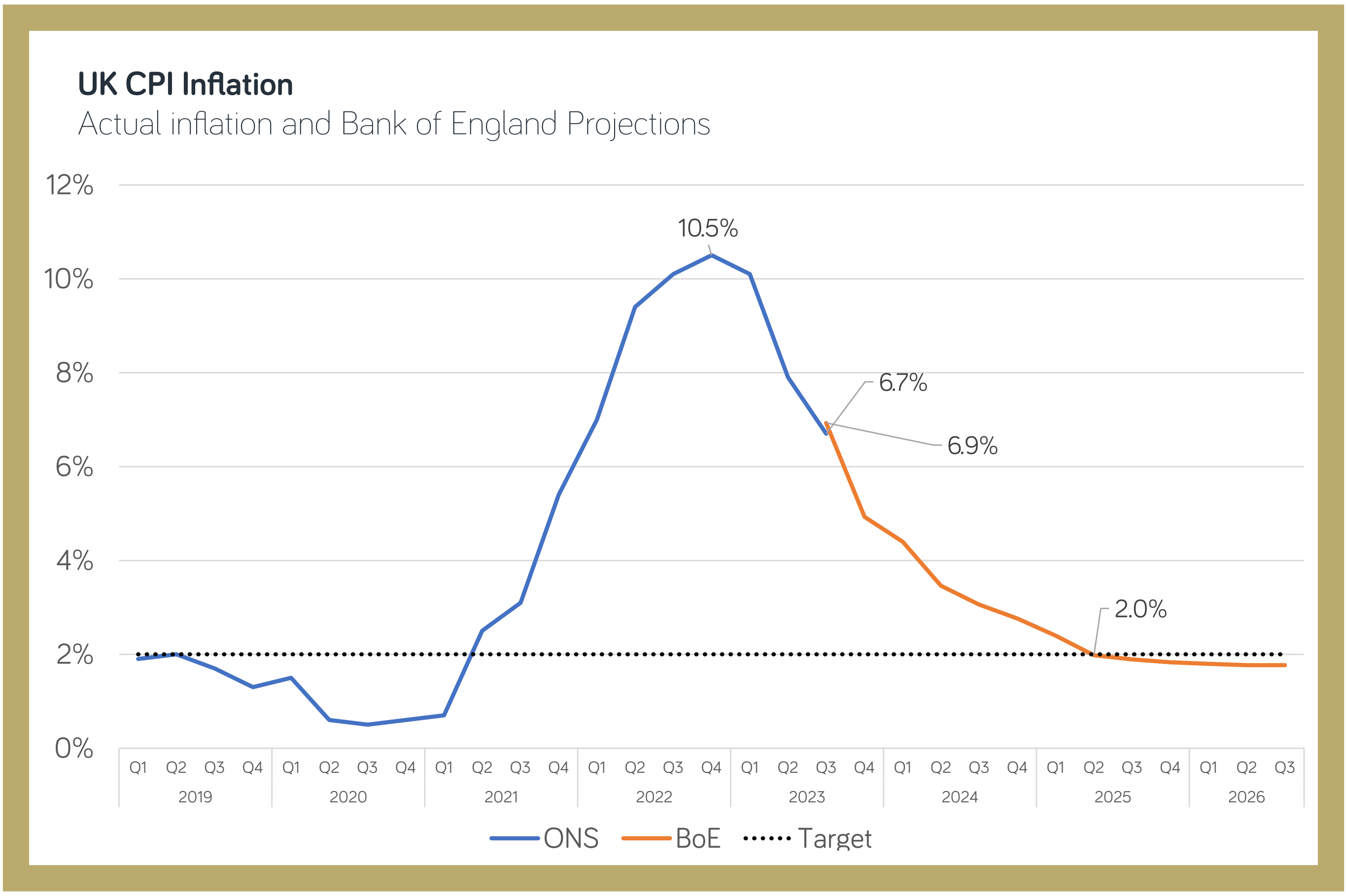
UK Gross Domestic Product had grown to be 1.8% greater than the pre-pandemic level by the end of Q2 2023, a stronger recovery than seen in Germany and France, but weaker than Italy, Japan, Canada and the US.

In the last four quarters (to Q2 2023) UK GDP has, on average, grown by just 0.125% per quarter. This is a slight improvement on previous data, bolstered in part by an upward revision of GDP figures by the Office of National Statistics, with Q1 2023 growth revised up to 0.3% from the previous estimate of 0.1%.

However, the overall picture remains that the UK is in a period of low growth, and the slight momentum the economy gathered post-pandemic is dissipating as high inflation and increased interest rates put a break on household and business investment, and day-to-day spending.

The latest (August) PMI survey on UK business activity indicates the fastest reduction in output since the lockdown period of January 2021. The risk of a recession, of two-quarters of economic contraction, has significantly receded but remains.





UK Quarterly CPI: Source ONS and Bank of England

Consumer Price Inflation is showing signs of abating, falling from a peak of over 10% in late 2022, to 6.7% in September 2023. The BoE expect inflation to return to the 2% target level by the first half of 2025.

Looking at their last full forecast (in August), the Bank of England (BoE) noted that while the economy has avoided a recession, growth forecasts are extremely weak, with less than 1% growth per annum from 2023 to 2025, and just over 1% by 2026.

According to OECD forecasts for the G20 economies, only Germany and Argentina will show weaker growth than the UK in 2023, and in 2024, only Argentina.

The Bank of England's central forecast for UK GDP growth from 2023 to 2025 is:

0.8% in the year to Q3 2023

0.3% in the year to Q3 2024

0.4% in the year to Q3 2025

1.1% in the year to Q3 2026

Construction Output

Monthly Construction Output by Main Sector: £million, Seasonally Adjusted

Monthly Construction Output, source ONS

In their latest release of Construction Industry data, the Office of National Statistics (ONS) show an industry coming under continued pressure as the general economy remains weak and interest rates rise.

The most poorly performing sectors are private new housing and private housing repair, maintenance and improvement (rm&i). In the latest month for which data is available, July 2023, ONS estimates monthly construction output to have decreased by 0.5% overall. The main contributors to the monthly fall are private housing repair and maintenance (-3.9%), and private housing new work (-2.2%).

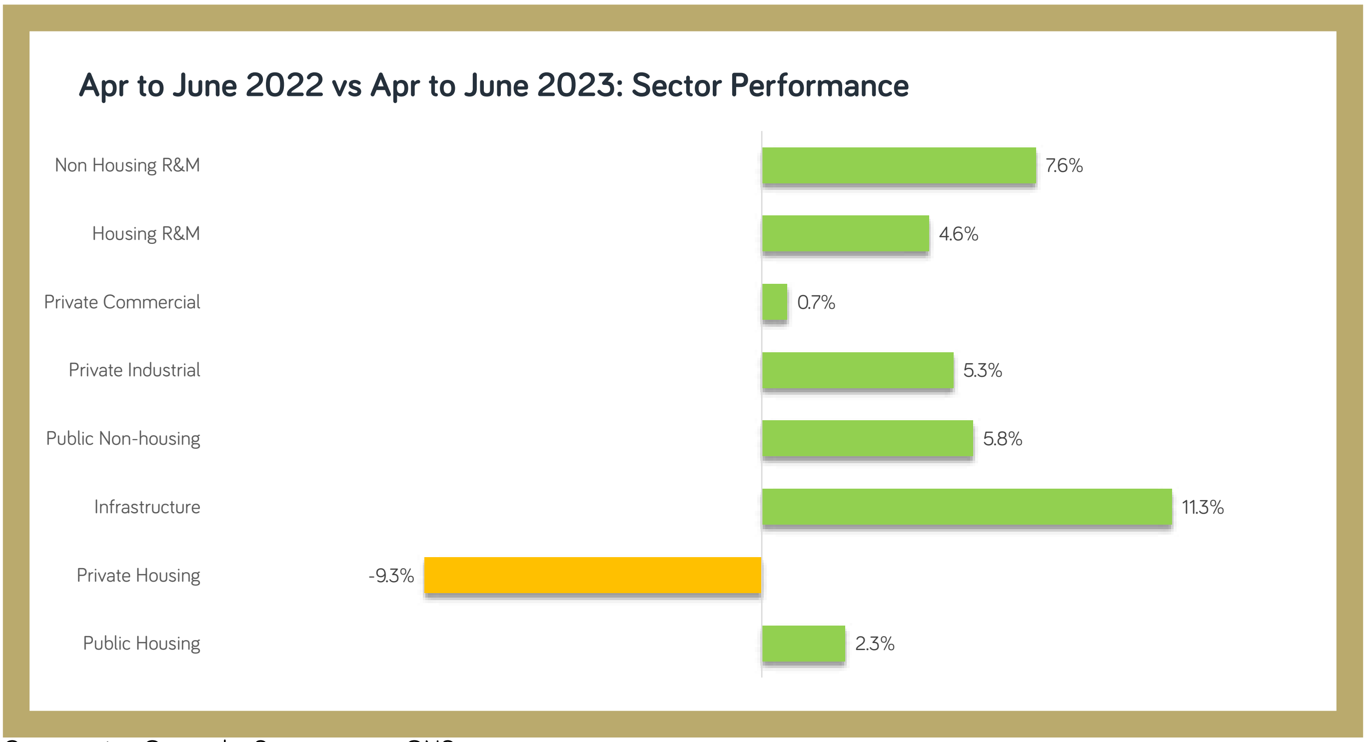
These sectors are the largest and the most important to architects. Small practices typically rely on housing work to ensure business viability. Housing is sensitive to mortgage rate rises; client demand tends to fall as mortgage costs rise.

Taking a longer view, construction output was 4.8% higher in the 12 months to July 2023 than in the 12 months to July 2022 but is on a downward trajectory.

Construction output in 12 months to July 2023

4.8%

higher than to 12 months to July 2022

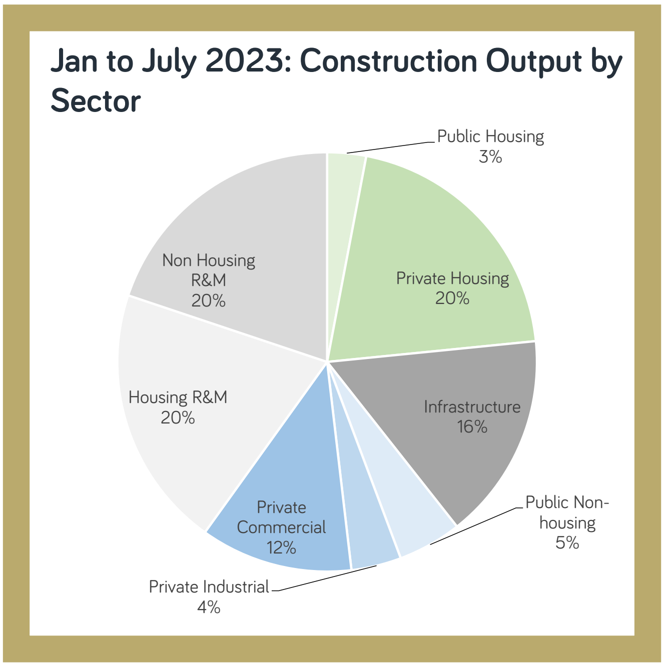


Construction Output by Sector, source ONS

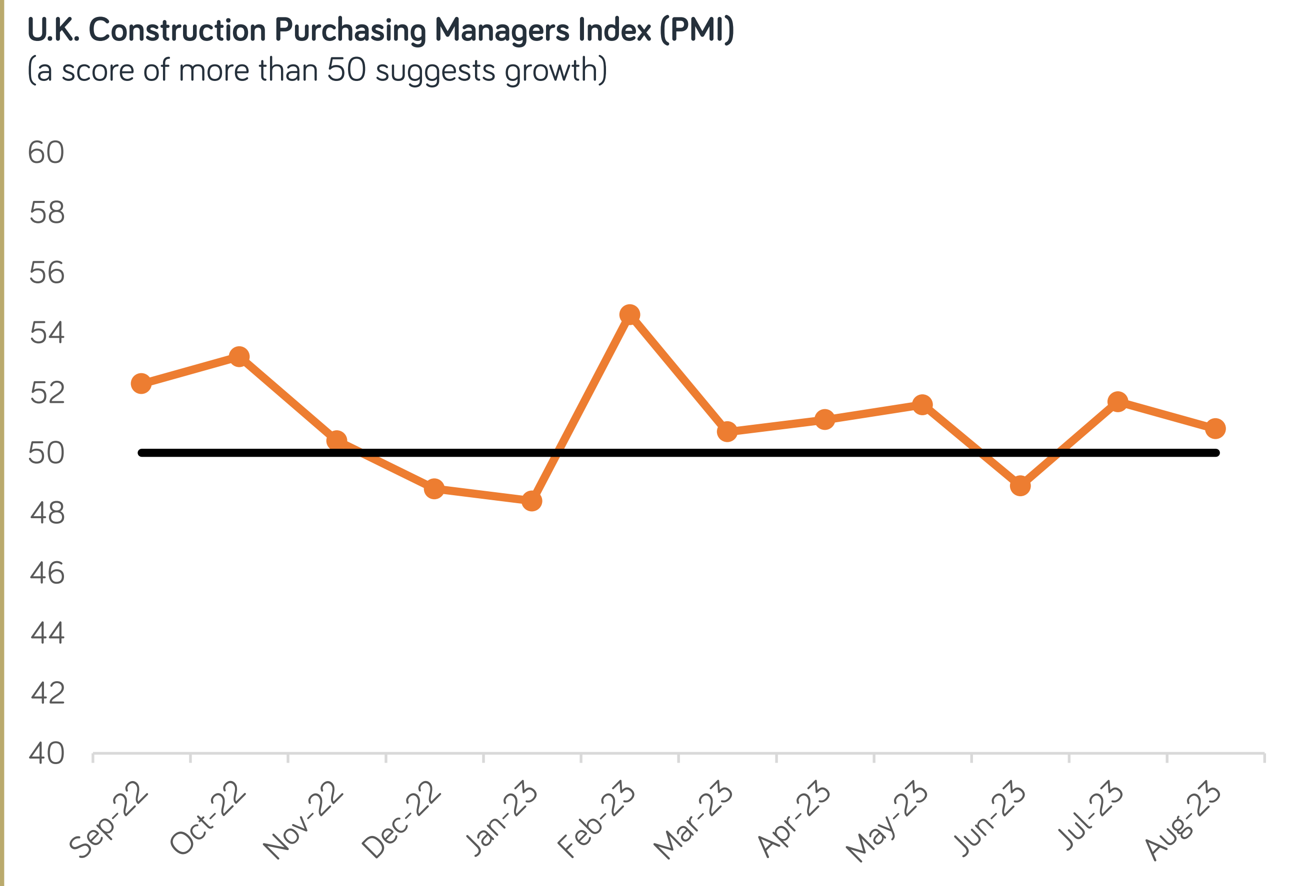
Comparing January to March 2022 with the same period in 2023, Infrastructure has been the best-performing sector. However, while infrastructure makes up 16% of total construction output, transport, for example, generates just 2% of Chartered Practice Revenue. The Repair and Maintenance (R&M) sectors have also seen growth, although Private Housing R&M fell in Q2 this year.

Private Housing accounts for around 30% of Chartered Practice revenue, and a majority of revenue for practices with 10 or fewer staff. This sector has seen the sharpest decline, with output falling by almost 10% when comparing April to June 2022 vs. April to June 2023, and by 4% in Q2 2023.

Looking at the overall mix of the construction sector from January to July 2023, Private Housing makes up around a fifth of the total value, as do both housing and non-housing R&M. Infrastructure (16%) and Private Commercial (12%) are the other two large sectors. Together, Public Housing, Private Industrial, and Public non-housing account for 12% of the industry's output by value



Construction Output, Sector Contribution, source ONS



Construction PMI, source S&P Global / CIPS

Confidence in the Construction Industry

S&P Global / CIPS monitors activity in the UK construction sector through its monthly Purchase Manager's Index (PMI). A PMI score of over 50 indicates growth since the previous month, and a score below 50 indicates comparative contraction.

The August 2023 PMI Index was above the 50.0 no-change mark for the second successive month, with a balance score of 50.8 in August, down from 51.7 in July.

However, rising borrowing costs and concerns about the wider economic context are contributing to a fall in New Orders, especially from residential clients.

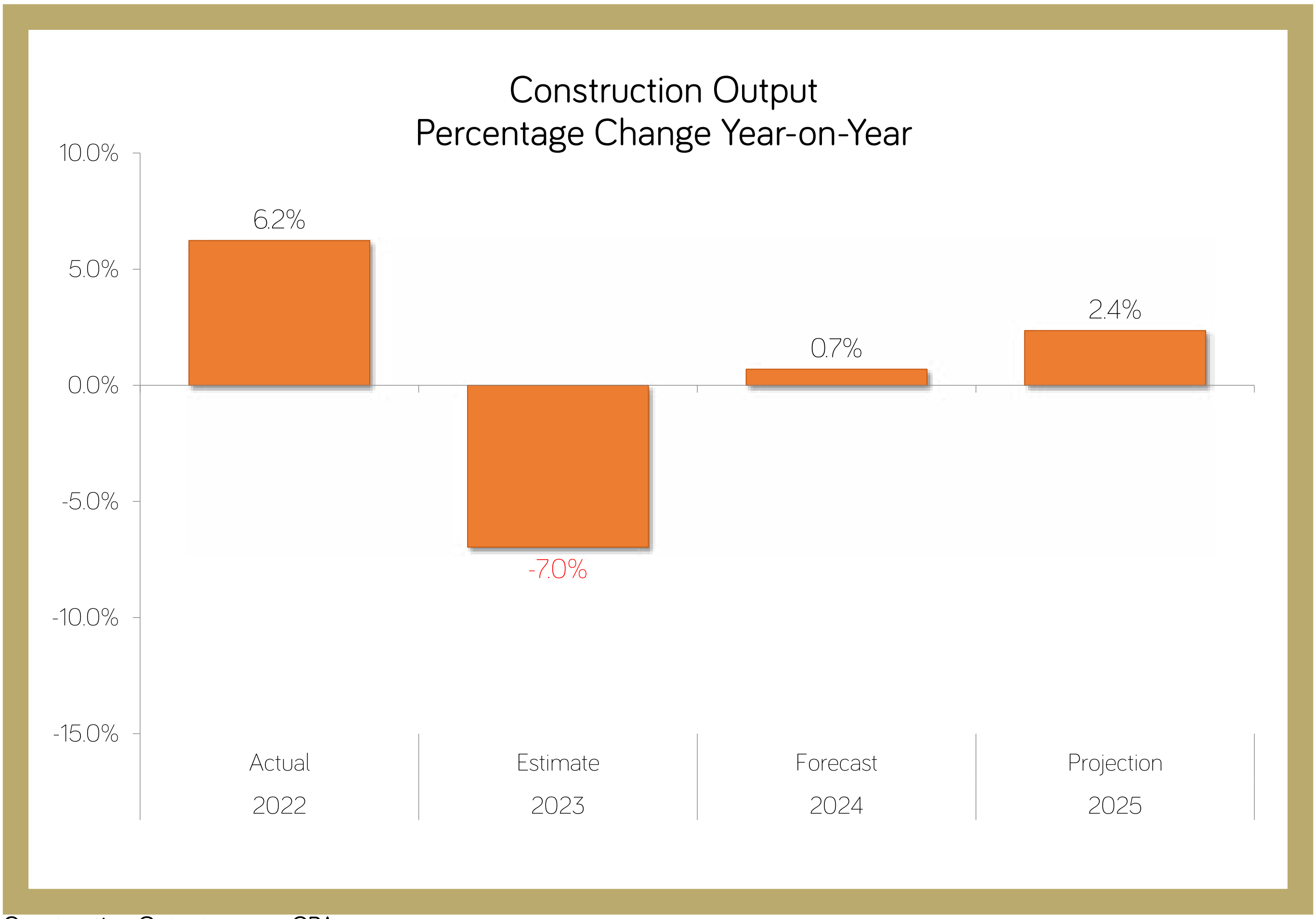
On balance, construction firms saw a marginal increase in activity during August, however, this was driven by growth in the commercial and civil engineering sectors. House Building has slumped with a PMI sector Index of 40.7, the second fastest downturn since May 2020.

As construction product price inflation begins to fall, Construction PMI respondents note that both the delivery times and availability of construction products are improving.

Overall the S&P Global / CIPS continues to note an industry that is weakly optimistic overall, but markedly pessimistic about the residential sector. Concerns for the year ahead remain.

"August data indicated that construction companies are relatively cautious about the outlook for business activity during the next 12 months. The degree of positive sentiment slipped to its lowest since January, with concerns about the impact of rising borrowing costs and subdued housing market conditions often cited during the latest survey period."

Construction Output: Future Projections



Construction Output: source CPA

The Construction Products Association's (CPA) Construction Industry Forecasts 2023-2025 provide a detailed view of the performance of the construction industry based on the value of construction output.

The CPA forecast an 'acute recession' this year with overall construction output falling by 7.0%, mainly due to sharp falls in activity in the two largest construction sectors: private new housing and private housing repair and maintenance.

Private housing starts are forecast to fall by 25.0% in 2023. Completions and output are expected to fall by 19.0%, before a recovery starting in the second half of next year.

2024 is forecast to see only modest growth in overall output with 0.7% growth. 2025 is forecast to see 2.4% growth. Given architects' work comes before construction output, however, the recovery in the architect's market may come sooner.

Construction Output 2023:

-7%

Construction Products Association

Architectural Workload

RIBA Future Workload Index*

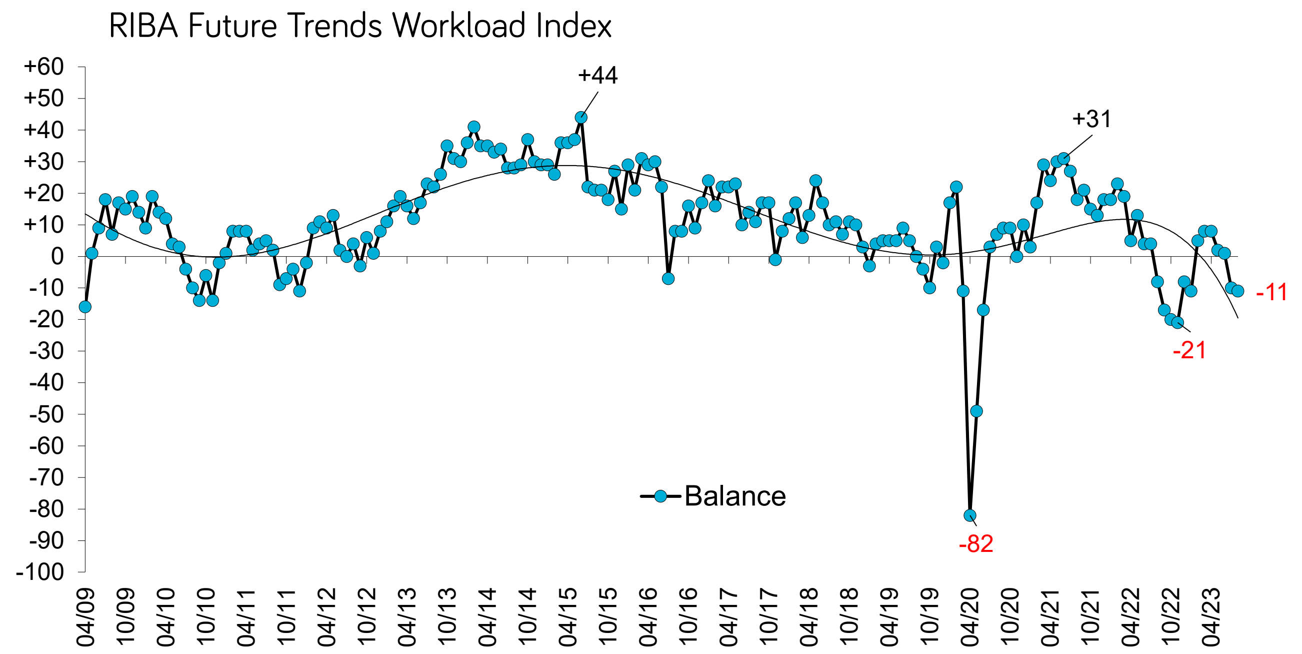
The third quarter of 2023 has seen architects become pessimistic about coming workloads, with July and August both returning negative RIBA Future Trends Workload Index figures. The Index now stands at -11, with a negative figure indicating an overall expectation of workload contraction in the coming three months.

This expectation of reduced workloads comes as interest rates rise and consumer budgets tighten. With rising interest rates causing project financing to be both more expensive and more difficult to obtain, the UK construction sector is weak and forecast to shrink this year.

In line with a poorly performing housing sector, the outlook among Small (1 - 10 staff) practices has consistently been more negative than that of Medium and Large (11+ staff) practices. Housing work typically accounts for a majority of work for practices with 10 or fewer staff.

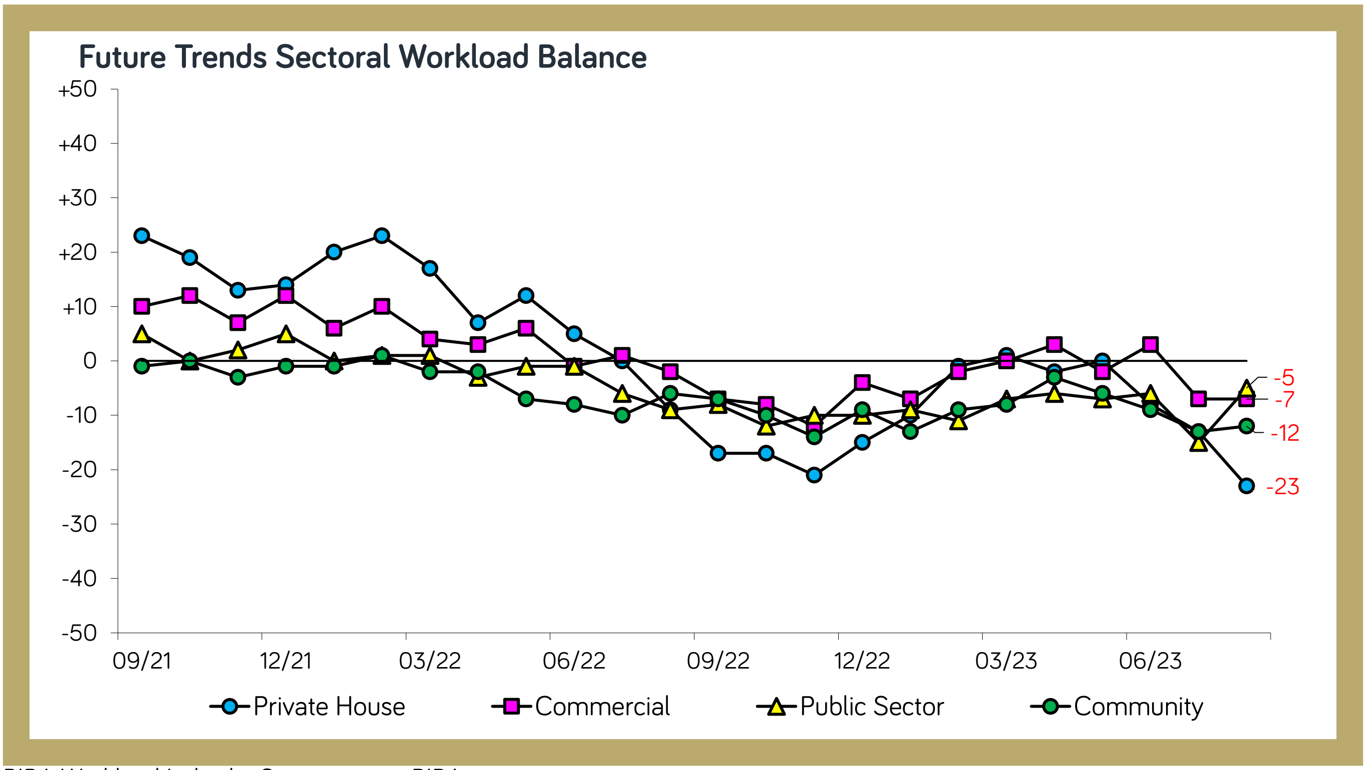
In contrast, Medium and Large-sized practices, typically with a wider portfolio of work and less reliance on housing remain optimistic about coming workloads.

The 2023 Future Trends reports can be seen here.



*The RIBA Future Workload Index figure is the difference between those expecting more work and those expecting less.

Architectural Workload Index* by Sector



RIBA Workload Index by Sector, source RIBA

Looking in more detail at the four work sectors monitored through RIBA Future Trends, all have weakened this quarter, and housing has fallen significantly. The modest rally in confidence that followed the Truss mini-budget dip, has now petered out.

The **Private Housing Sector is** the worst-performing sector with a Workload Index figure of -23 in August, and a negative balance score every month this quarter. The sector is now at its lowest level of confidence since the early days of the pandemic. The sector is likely to continue to perform poorly for the remainder of the year, as high borrowing costs, falling house prices and constrained household budgets translate into reduced new build and fewer repair and improvement projects. However, high-end projects commissioned by asset-rich clients are likely to be unaffected by current market conditions.

Architects' assessment for future work in the **Commercial Sector** has fluctuated, with a positive balance in June (+6) followed by two months of a negative (-7) Workload Index score.

Workload predictions for the **Public Sector** remain weak, with the sector Index being negative for over a year. There has, however, been an uptick in outlook in August, as the poor state of public sector buildings becomes clear. With increasingly unsafe schools, hospitals and prisons making up our public estate, urgent repair work is needed short-term, with a longer-term programme of renewal following.

The **Community Sector** includes work for not-for-profit organisations; work with churches, charities and trusts, for example. With ongoing financial pressure within the sector, the workload index figure remains low and currently stands at -12 On balance, practices have been expecting falling workloads in the sector since March 2022.