

State of Trade Survey

July 2017 - £90



Mixed Picture for Q2 as Outlook Weakens

Headlines:

- 40% of heavy side firms and 55% of light side firms reported that **sales rose** during the second quarter of 2017, the seventeenth quarter of growth
- 29% of heavy side product manufacturers and 30% of light side product manufacturers reported that they **anticipated sales rising** over the coming year
- **Cost increases** were reported by 93% of heavy side manufacturers and 100% of those on the light side, the highest balance in nine years, driven by raw material costs
- 93% of heavy side firms and 90% of light side firms anticipated **costs rising** further over the next 12 months
- 30% of heavy side firms reported that **exports increased** in Q2

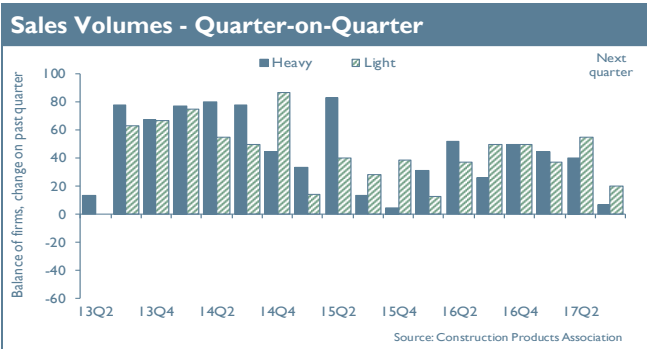
Despite slower UK economic growth in the first quarter of 2017 and ongoing uncertainty relating to Brexit and domestic politics, construction product manufacturers reported continued growth in Q2. On the heavy side, 40% of firms reported a quarterly increase in sales, down from 45% in Q1. On the light side, 55% of firms reported that sales increased during the quarter, up from 38% in Q1 and reaching the highest balance since 2014 Q4. Looking forward however, manufacturers' expectations for sales growth over the next quarter and year weakened. Only 7% of heavy side manufacturers anticipated an increase in sales over the next quarter, whilst a balance of 20% was recorded on the light side.

Manufacturers' cost pressures remained elevated in Q2, reflecting the ongoing pass-through of the Sterling's depreciation post-referendum. In Q2, overall cost balances for both heavy side and light side firms reached multi-year highs driven by an increase in raw material costs. Despite the weaker Sterling and healthy global economic growth, manufacturers did not report a marked impact on export sales.

Construction product manufacturers continued to experience growth in sales during the second quarter of 2017. On balance, 40% of heavy side manufacturers and 55% of light side manufacturers reported that sales had increased compared to Q1. On the heavy side, the balance weakened from 45% in the first quarter of 2017, whereas the balance for the light side strengthened from 38%, reflective of increased heavy side activity filtering through to the later stages of the construction supply chain. On an annual basis, 47% of heavy side firms reported that sales had increased in Q2, whilst on the light side, 45% of firms reported that sales were higher than a year earlier. Whilst the second quarter was a broadly positive performance, looking forward to manufacturers' expectations for the next quarter and year ahead pointed towards a slowdown, consistent with uncertainty clouding the economic outlook. On balance, only 7% of heavy side manufacturers and 20% of those on the light side anticipated an increase in sales in Q3, down from 68% and 47% respectively, recorded in the Q1 survey. Furthermore, 29% of heavy side firms and 30% of light side firms anticipated a rise in sales over the next 12 months. Both balances weakened significantly from those recorded in Q1.

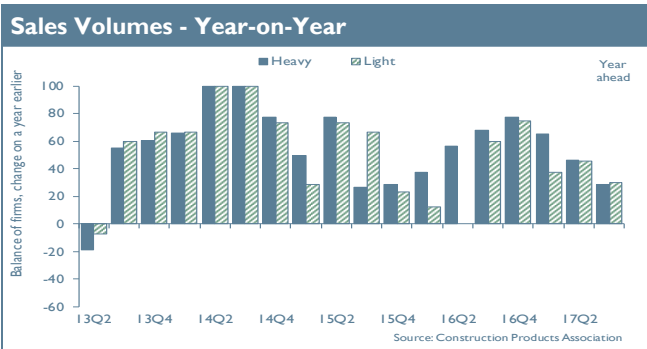
In contrast to recent Markit/CIPS data, inflationary pressures continued to intensify in 2017 Q2 as the pass-through of the weaker Sterling continued. 93% of heavy side manufacturers reported rising costs, the highest balance since 2011 Q2, whilst a balance of 100% was recorded on the light side, the highest in nine years. In Q2, the Sterling depreciated 8.5% against the Euro (in annual terms), marking a sixth consecutive quarter of decline. This has led to higher costs for imported raw materials and, in Q2, 87% of heavy side firms and 100% of light side firms (the highest balance since the series began in 2011 Q1) reported an increase in the cost of raw materials. Moreover, manufacturers expected overall cost inflation to persist over the next 12 months. Despite a favourable exchange rate for exports and increasingly strong global economic growth, the benefit to manufacturers was muted. 30% of heavy side firms reported an annual increase in export sales in Q2, whilst no light side firms reported growth.

Sales & Constraints



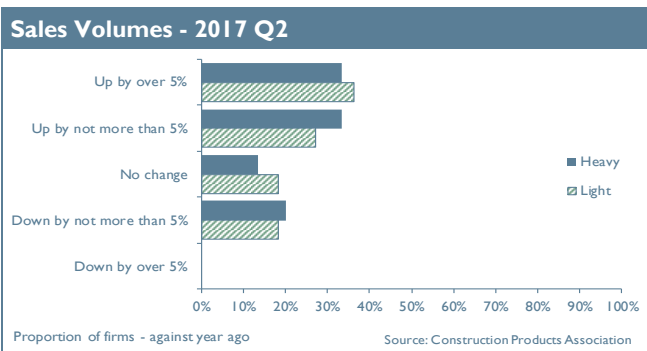
Quarterly product sales increased in Q2...

Construction product sales continued to increase in Q2, the seventeenth consecutive quarter of growth since 2013 Q2. In Q2, 40% of heavy side firms, on balance, reported an increase in quarterly sales, down from 45% in the first quarter. On the light side, 55% of firms, on balance, reported a quarterly rise in sales in Q2, up from 38% in Q1 and reaching the highest balance since 2014 Q4. Looking ahead however, only 7% of heavy side firms and 20% of light side firms, on balance, anticipated growth during the third quarter of 2017.



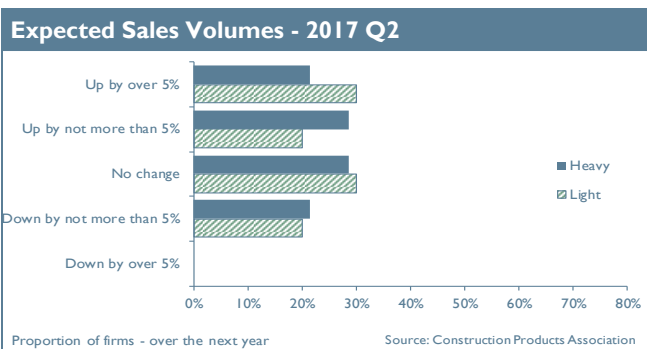
...with a similar performance on an annual basis...

47% of heavy side manufacturers and 45% of light side manufacturers, on balance, reported that product sales were higher than a year earlier in Q2. The heavy side balance fell from a balance of 65% in the first quarter, whereas the balance for light side manufacturers strengthened from 38% in Q1. Looking ahead, 29% of heavy side manufacturers and 30% of light side manufacturers anticipated an increase in sales in the next 12 months.



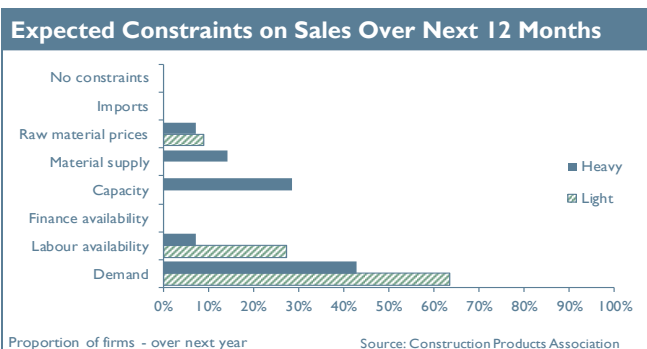
...and manufacturers reported continued growth.

Construction growth over the past year has been driven by private housing, commercial and private housing RM&I, which has benefitted most product manufacturers. 33% of heavy side firms and 36% of light side firms reported 'significant' rises in sales in Q2 (rises of over 5%) compared with a year earlier. 33% of heavy side firms and 27% of light side firms reported that sales had increased by up to 5% over the same period. However, 20% of heavy side firms and 18% of light side firms reported that sales fell by up to 5% during Q2.



Prospects for the next 12 months have weakened...

Amid ongoing political instability and uncertainty relating to Brexit negotiations, product manufacturers' expectations for sales growth over the next year weakened in Q2. 21% of heavy side manufacturers and 30% of light side manufacturers reported that they anticipated sales over the next year would rise 'significantly', by over 5%. A further 29% of heavy side firms and 20% of light side firms anticipated further rises in sales of up to 5%. However, 21% of firms on the heavy side and 20% on the light side anticipated a fall in sales during 2017.



...with demand remaining the key concern.

Demand was reported as the key constraint on sales growth over the next 12 months. 43% of heavy side manufacturers and 64% of light side manufacturers reported that demand was likely to be the key constraint on sales during the next 12 months. For heavy side firms, the other expected major constraints were; capacity (29%), material supply (14%), labour availability (7%) and raw material prices (7%). For the light side, 27% of manufacturers reported labour availability as a constraint and 9% cited raw material prices.

Costs, Employment, Capacity & Investment

Cost pressures accelerated in Q2...

Annual consumer price inflation in the UK was 2.9% in May, up from 2.7% in April. In Q2, cost increases were reported by 93% of heavy side manufacturers, on balance, compared to 73% in Q1 and the highest balance since 2011 Q2. Similarly, all light side firms, on balance, reported rising costs in Q2, increasing from 80% in Q1 and reaching the highest balance since 2008 Q3. Looking forward, manufacturers expected cost pressures to remain elevated over the next 12 months, with 93% of heavy side firms and 90% of light side firms anticipating increasing costs, on balance.

...with raw materials driving up cost inflation.

The key driver of cost inflation in Q2 was raw materials, owing to the weaker Sterling exchange rate and rising global commodity prices. Reflecting this, 87% of heavy side firms and 100% of light side firms reported that raw materials rose over the past year. For the light side, this was the highest balance since records began in 2011 Q1. Given the recent rise in global commodity prices, fuel and energy costs were also noted as a key pressure for both heavy and light side firms. Exchange rates were also cited by 78% of light side firms, the highest balance on record.

Employment growth and prospects remained positive...

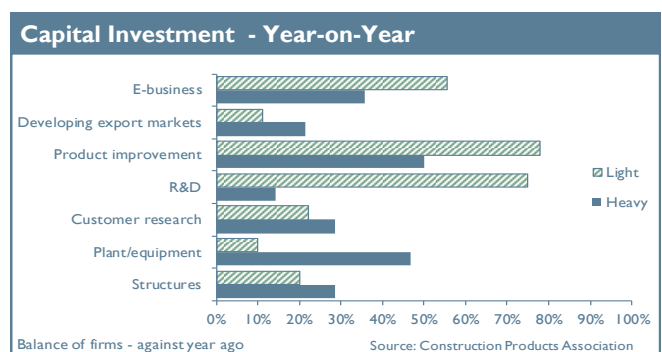
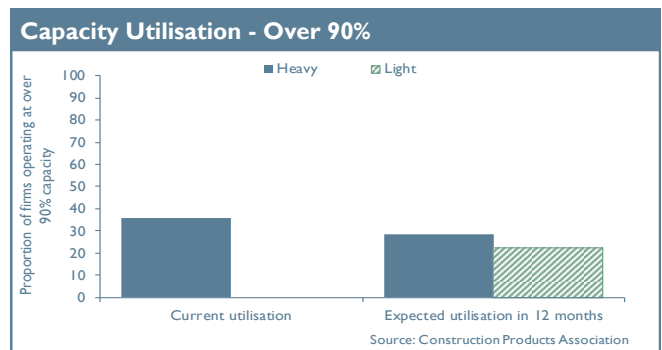
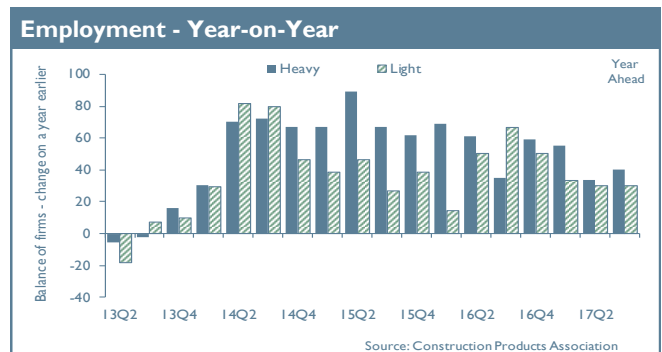
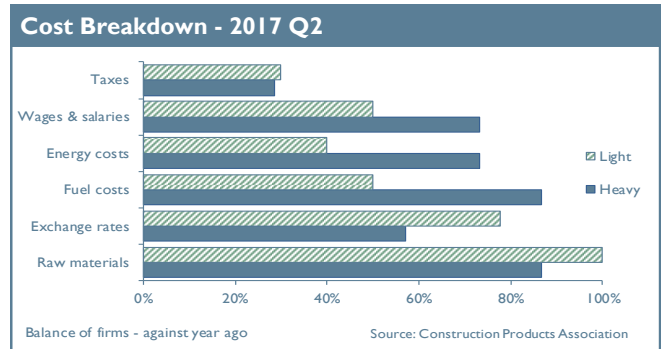
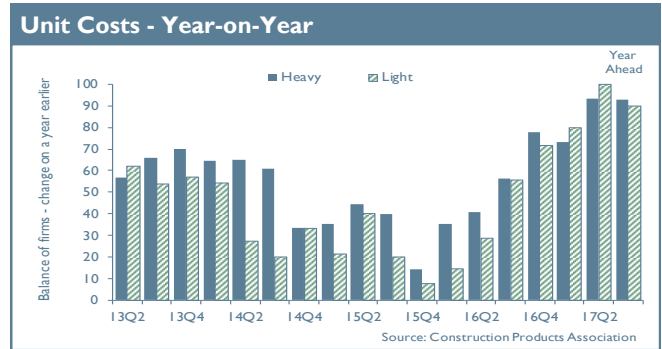
The rise in sales during 2016, together with expectations of further increases during 2017, has seen product manufacturers increase employment. In Q2, one-third of heavy side manufacturers and 30% of light side manufacturers, on balance, reported that employment rose on a year earlier. Looking ahead, hiring intentions continued to remain positive. On balance, 40% of heavy side firms and 30% of light side firms anticipated increasing headcount during the next 12 months.

...but little concern over capacity.

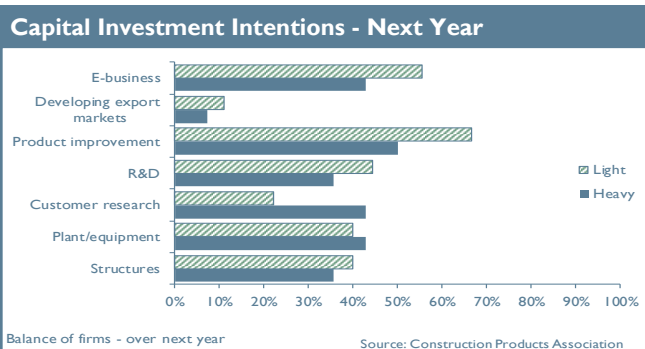
Overall, capacity levels were reported to be sufficient in Q2, given current construction output and demand. 36% of heavy side firms reported that they had operated at between 90% and full capacity over the last 12 months, compared to 32% in Q1. For the light side, no firms reported that they had operated at 90% capacity or over, although 33% reported capacity utilisation over 80%. In 12 months' time, capacity utilisation is anticipated to be 90% or higher according to 29% of firms on the heavy side and 22% of manufacturers on the light side.

Capital investment remained one of the key priorities...

In Q2, on balance, 50% and 47% of heavy side firms reported that investment in product improvement and plant & equipment, respectively, was higher than a year earlier. Furthermore, a balance of 36% reported increased investment in e-business, whilst a balance of 29% was reported for structures and customer research. 78% of light side firms, on balance, reported increased investment in product improvement, whilst investment in research and development (R&D) and e-business was higher for a balance of 75% and 56% of light side firms, respectively.

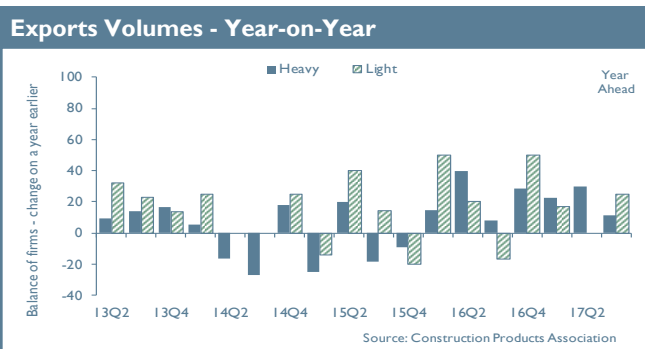


Investment Intentions & Exports



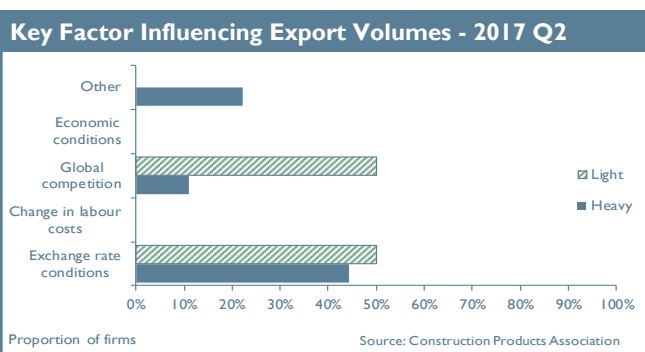
...with product improvement the focus of investment.

On the heavy side, product improvement was the focus of capital investment intentions for the next 12 months, with half of manufacturers, on balance, anticipating increasing capital investment in this area. Furthermore, 43% also anticipated investment to increase in each of plant & equipment, customer research and e-business. For firms on the light side, 67% and 56% anticipated investment to increase in product improvement and e-business respectively. 44% of light side firms, on balance, also anticipated increasing investment in R&D.



Mixed performance for export sales in Q2...

In Q2, 30% of heavy side manufacturers reported a rise in exports compared with a year earlier, against a balance of 22% reported in Q1. On balance, no light side firms in Q2 reported an increase in export sales compared with a year earlier. This compares to a balance of 17% reporting a rise in Q1. Looking forward, 11% of heavy side manufacturers and one-quarter of light side manufacturers anticipated a rise in exports, on balance, over the next 12 months. On the light side, this was the lowest balance in three years.



...reflecting economic conditions and Sterling weakness.

40% of heavy side product manufacturers and 55% of light side firms produced solely for the domestic market in Q2. The heavy side proportion was the lowest in two years. Of those that did export, exchange rate conditions was the key factor influencing export volumes, according to 44% of heavy side firms and half of light side firms. Other conditions, such as intra-group activity were also cited by 22% of manufacturers on the heavy side, whilst half of light side firms noted global competition as another key factor influencing export volumes in Q2.

Information about the Construction Products Association and the State of Trade Survey

The **Construction Products Association** represents the UK's manufacturers and distributors of construction products and materials. The sector directly provides jobs for 300,000 people across 22,000 companies and has an annual turnover of more than £55 billion. The Association acts as the leading voice to promote and campaign for this vital UK industry.

The State of Trade Survey, conducted quarterly, provides insight into current and expected future industry trends. The survey analysis includes the use of 'balance of respondents' to assess survey results and identify trends. Balance of respondents is a percentage of firms reporting a rise less those reporting a decline. No weighting is given to allow for the extent of the change of the size of the firms involved.

Analysis is divided into heavy and light construction products. **Heavy side products** are typically structural materials used early in the construction process and include materials used in transport and other civil engineering projects. Heavy side materials include: aggregates, cement, ready-mix concrete, structural and reinforcing steel. **Light side products** are typically installed later in the construction process and include internal fittings and services. Light side products include: heating and ventilation systems, plumbing, electrical and lighting, doors and windows, kitchen furniture and thermal insulation.

The State of Trade Survey is one of a range of publications produced by the Association, including the Construction Trade Survey and Construction Industry Forecasts. For further information on the content and availability of these publications please contact:

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