Brexit: Infrastructure

Slower pipeline today, but that may help in long run

September 2016

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At a glance:

- UK construction is very domestic, fragmented, inefficient and ripe for consolidation
- A fall in the pound and industry pressures will accelerate acquisition opportunities
- The industry is ripe for tech innovation but lacks the margins to invest in it

Britain's construction industry will probably be one of the worst affected by the Brexit vote, certainly in the short term. Construction demand correlates closely to economic growth, but also overreacts to economic sentiment. So whatever slowdown in growth we see, the impact in construction is likely to be worse.

Indeed the Markit/CIPS UK construction survey in July showed output falling at the fastest pace since 2009 in the immediate aftermath of the vote, though it did bounce back in August.

It might be less seriously affected than construction, but government-led demand for infrastructure will feel the impact of Brexit too. Existing programmes, especially in highways and rail, are likely to continue as planned. Most regulated utility programmes should also remain on track (though in the longer term if interest rates rise that may put pressure on the financial robustness of more highly leveraged players).

The major risk on infrastructure is where significant political or Treasury decisions are required. The coming 12 to 24 months is likely to be one of the most challenging periods in decades for the UK Government and it is not unreasonable to assume it will be distracted by stabilising the economy, focusing on the best Brexit deal and forging relations beyond Europe.

Pipeline uncertainty

The government has already delayed a decision on South-East airport capacity to the autumn. In the near term, we expect a significant fall in demand and uncertainty over the pipeline of projects.

This is not necessarily bad news from an external investor perspective. The UK construction industry is very domestic, fragmented, inefficient and ripe for consolidation. The fall in the value of the pound and the pressures in the industry are likely to accelerate the opportunity for acquisition.

Investment needed

The industry is conscious of significant technological opportunities but lacks the margins to invest. It is also characterised by an ageing workforce, a lack of diversity and a lack of modern skills. There is widespread expectation that either offsite, prefabricated construction, or on-site 3D printing and robotics could transform the industry in the medium to long term. But it seems likely that external investors and/or alliances with technology businesses will be needed to trigger that change.

There is a welcome trend among clients to procure more effectively, on the basis of long-term alliances and relationships rather than cost-driven tenders. Public policy will continue to require transparent competition for work, but exit from the EU could lead to some changes in tendering rules.

There are early signs that investor interest in the infrastructure market is being maintained despite the Brexit vote. We are also seeing signs that the UK will continue to be an attractive market thanks to its commitment to long-run infrastructure development and an acute shortage of housing, which will eventually re-ignite demand.

Now seems like an opportune time for ASEAN companies to maintain their interest and in particular look for opportunities to buy into existing businesses looking for offers, as the market tightens.

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CREATE | CRT070328B | October 2016.