UK MARKET VIEW

Budget offers little for construction while 2026 may be a make-or-break year for new projects

Q4 2025

Introduction

As we head into 2026, the UK construction sector is navigating a landscape defined by both renewed momentum and persistent challenges. Strengthening new orders and a solid pipeline of government-backed infrastructure signal opportunity, yet wider economic uncertainty continues to shape market sentiment. Growth is uneven across sectors, labour pressures are intensifying, and questions remain about whether the industry has the depth of capability required to deliver the scale of programmes now coming forward.

With fiscal pressures rising and tax policy shifting, it's clear that clients and contractors will need to work more closely than ever, not only to manage risk, but to build capacity, reinforce capability and secure value over the long term. Collaborative behaviours, early engagement and best-practice delivery models will be essential if the industry is to convert today's pipeline into sustainable, confidence-building growth.

Oliver North
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While construction output increased 0.1% in Q3, the...

0.2%

decline in all new work shows the industry continues to face headwinds.

Construction wage growth has slowed to...

3.5%

below the rate of inflation, and is one of several indicators pointing to weakness in the labour market.

The wider economy is also facing difficulties, and GDP stuttered to just...

0.1%

growth in Q3.

New orders rose...

9.8%

in Q3 2025 which should help support growth in 2026.

The Monetary Policy Committee responded to weak growth and cooling inflation by cutting interest rates to...

3.5%

Tender prices

	2025	2026	2027	2028	2029
National Real Estate	3.5%	3.0%	3.5%	4.0%	3.5%
National Infrastructure	4.0%	4.0%	4.5%	4.5%	4.0%
London	3.5%	3.0%	3.5%	4.0%	3.5%

This table gives our current tender price inflation forecast. The figures should be treated as averages and there will be variations due to procurement methods, project type and local factors.

Setting the scene

The economy recorded growth of just 0.1% in the third quarter. This was in part due to a cyberattack on Jaguar Land Rover, causing it to temporarily stop car production and disrupting the wider supply chain. However, minimal growth also reflects ongoing problems facing the economy. Pay growth has slowed and household consumption is providing only limited support. Overall, the economy is on course for full-year growth in 2025 of around 1.4%, a level that the Office for Budget Responsibility expects to persist through to the end of the decade.

Published alongside November's Budget, the OBR's downgrade of its forecasts did not come as a surprise. Nonetheless, the ongoing weak economic backdrop will continue to hinder potential construction growth. This will particularly affect the private housing and commercial sectors, with the industry looking to infrastructure and public non-housing for support. Construction will therefore be relieved that the government reaffirmed its commitment to its capital spending plans. The volume of projects proposed as part of the Spending Review and Infrastructure Strategy meant the Budget announced little new funding. Of the spend, an initial £1.1bn will go towards Northern Powerhouse Rail to help with planning, development, and design however it will not be until the 2030s that most of the work takes place. Given the promises in the Spending, Review there are doubts about whether the industry can deliver the pipeline of work. Contractors may not have the capacity to deliver all of the large schemes. The complexities also pose questions about whether firms have the risk appetite and experience to meet the requirements. We discuss these challenges in this report and provide some suggestions as to how clients can navigate them.

By choosing not to cut spending, the government had to raise taxes. Set to reach a record high of 38.2% of GDP by the end of the Parliament, markets reacted positively to the increase in fiscal headroom. The government managed to do this and keep to its manifesto promise about tax. However, by avoiding changing income tax, VAT or National Insurance, the three largest revenue generators, the government relied on adjusting rates to many much smaller ones. Adjusting so many taxes raises doubts about whether it will raise as much as forecast. Similarly, with most of the additional revenue raised only coming in at the end of the Parliament, it is unclear whether political expediency will result in a change of course as we get closer to the next election. Arguably, the most damning criticism of the Budget came from the OBR itself, stating that none of the individual policies announced would have a material effect on the economic forecast. This highlights how it was a Budget of tinkering rather than a more ambitious transformation.

Beyond the Budget's limited announcements for construction, recent data releases have also provided little cause for optimism. Repair and maintenance helped construction output grow 0.1% in Q3 2025, while all new work saw a small decline. Nonetheless, new work is up 1.8% on Q3 2024, with public non-housing and private industrial both more than 20% higher than a year ago. Meanwhile, new orders rose almost 10%, driven by a large one-off private industrial project and the best quarter for private commercial since 2021. On a rolling four-quarter basis, new orders are at their highest since Q2 2023, and this should lead to faster output growth in 2026. More concerning than official statistics, November's S&P Global UK Construction PMI offered a very downbeat assessment of the industry. According to this survey, activity in the sector was at a level usually only reserved for significant recessions.

Respondents were particularly negative about the infrastructure sector and reported both delays to starting new projects and a lack of them. Lengthier pre-construction service agreements are also becoming more common and represent just one of the issues slowing industry progress. Nonetheless, the negativity of this survey will hopefully be a blip, and as the government approves more large projects growth will accelerate over the next few years.

We have left our tender prices unchanged from our Q3 report. Despite pressures from wage growth having eased, and relatively soft output growth, in 2025 contractors remained resistant to taking on onerous terms and, especially in infrastructure, were able to push through higher rates. Nonetheless, some of these issues will limit tender price growth in 2026. While the Bank of England cutting interest rates at its final meeting of last year, alongside the government's ambitions for construction, should support a rise in new projects getting sign-off in 2026, only in 2027 will this lead to an acceleration in tender prices.

All new work shrinks for first time in over a year

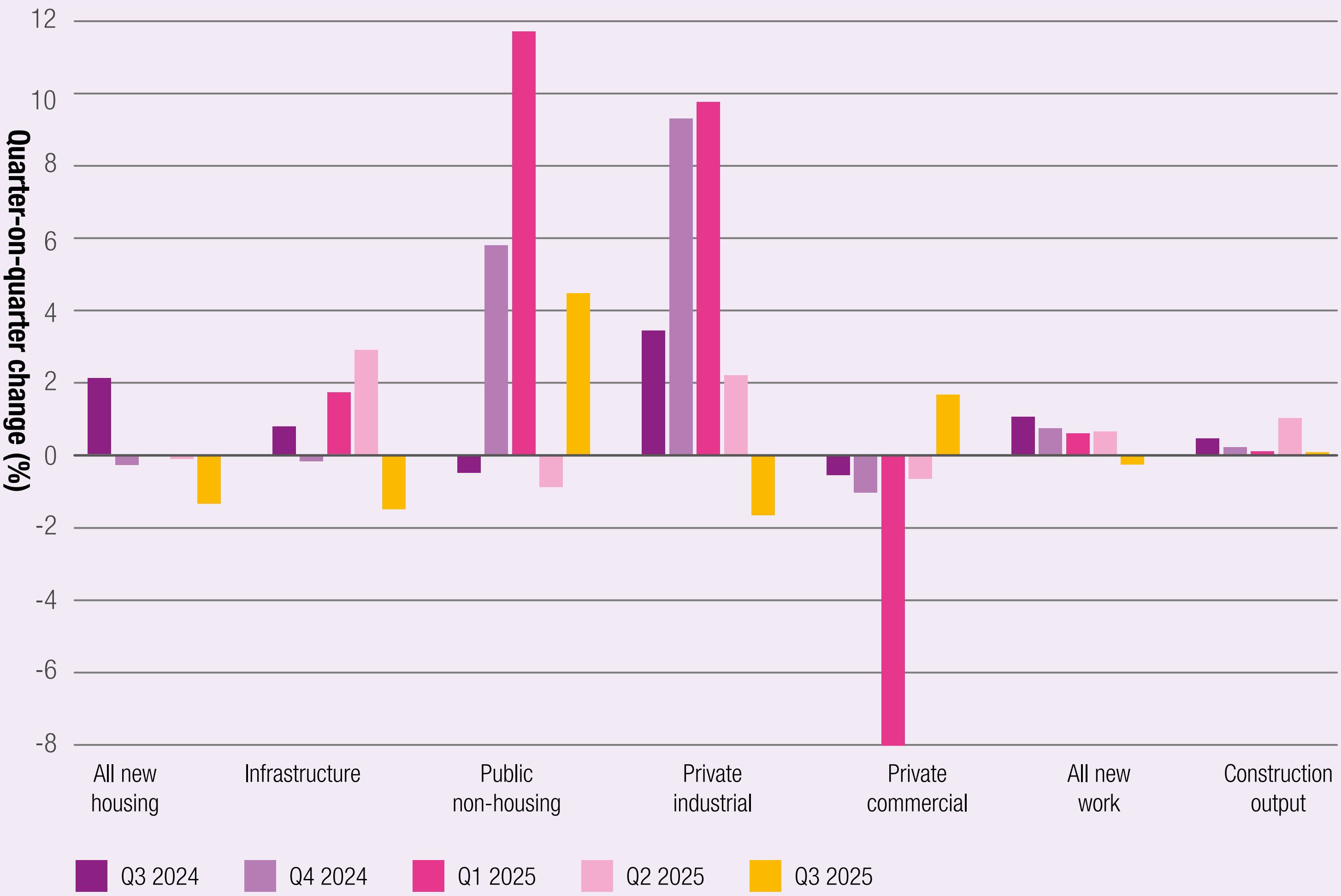
The 0.1% increase in construction output in Q3 was moderately disappointing. While repair and maintenance rose 0.6%, all new work declined 0.2%. The first time all new work has slipped since Q2 2024, this part of the industry is still 1.8% higher than 12 months ago, and it is likely a case of momentum stalling rather than stopping. A lack of consistency across sectors underscores how all new work is yet to truly turn the corner. Having declined in Q2, output in private commercial, public housing and public non-housing rebounded. Meanwhile, after growing in Q2, private housing, infrastructure and private industrial all saw output shrink in Q3.

For private commercial, growth of 1.7% ended its run of four successive quarterly declines. However, such growth does little to rectify the recent difficulties faced by the sector. Output remains 8.0% lower than in Q3 2024 and 34.1% below its level in the final quarter of 2019. Having struggled for so long, even if we have now reached a bottom, and a jump in new orders to their best level in over four years adds to this impression, the recovery will be slow. Similarly, public housing rising 1.0% ended a sequence of three successive quarterly declines. However, it too has had a terrible 12 months and is 16.4% lower than in Q3 2024.

More positively, public non-housing grew 4.5% in Q3 and is 22.5% larger than 12 months ago. With the Budget reaffirming the plans laid out in the Spending Review, this sector should continue to expand. While infrastructure should also fare strongly in the coming years, its latest outturn was less positive. Down 1.5% for the quarter, it is 3.0% up over the last year. Often a volatile series due to the involvement of many of the UK's largest projects, the sector will only report moderate growth for 2025 but should continue to expand in 2026.

REVERSAL IN FORTUNES FOR THE SECTORS

Source: ONS



New orders

New orders had a strong third quarter, rising by 9.8%, its highest level in over a year. On a rolling four-quarter basis, new orders have now had their best period in two years, a fact which is even more impressive given the ongoing struggles for the housing sector.

One large contributor to this quarter's positivity was the £1.25bn Port Talbot steelworks project which drove private industrial output to more than double its Q2 figure. This project accounts for around 5% of the total of new orders in Q3. The second quarter in a row where a large, single project has boosted the figures, there are a number of other such schemes likely to come to market in the next few years. Such projects boost output just as much as any other, but by their very nature they are difficult to forecast and often unrelated to wider economic conditions. They therefore mean we must be careful about overstating how the industry is faring based on them.

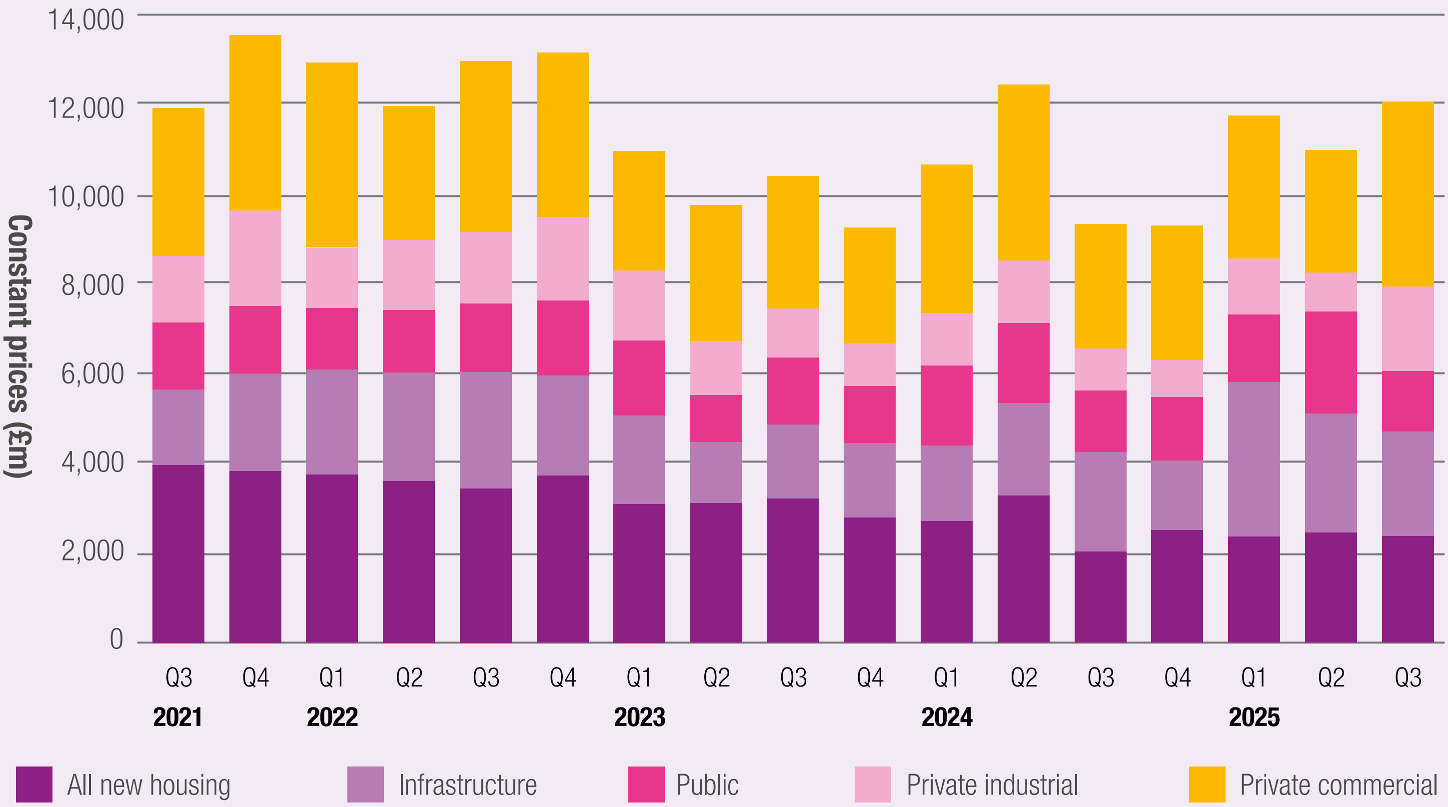
A clear example of one-off projects boosting a sector in one quarter and then slipping back in the next comes from public non-housing. Supported by the Department for Environment, Food & Rural Affairs' Science Capability in Animal Health programme in Q2, the sector slumped by 40.5% in Q3. 6.0% up on a rolling four-quarter basis compared to Q3 2024, it seems almost certain that output growth will be unable to continue to keep rising at its current pace next year.

Despite infrastructure dropping 12.5% in Q3, the past four quarters have been the sector's best since the pandemic, helping explain why further growth is expected next year. What's also noticeable about recent infrastructure new orders is the lack of public sector projects, and the potential for further strengthening. In the third quarter, the private sector, mainly through electricity projects, accounted for 80% of new orders. For roads and railways after a good Q1, Q2 and Q3 were much weaker. Nonetheless, government plans suggest there's strong potential for new schemes, even if it will take time for some to start construction. In particular, the Lower Thames Crossing will be the largest roadbuilding project for a generation, while East West Rail and the TransPennine Upgrade also have sizeable contracts coming to market in the next few years.

Despite the Office for National Statistics having started to publish its producer price indices again, the Department for Business and Trade is yet to update its construction material price index. However, it resumed publishing data on specific materials, with the average growth rate of these 26 products at 2.9%. This figure doesn't take account for weightings, and BCIS suggests annual material inflation in September

NEW ORDERS SHOULD BOOST OUTPUT IN 2026

Source: ONS

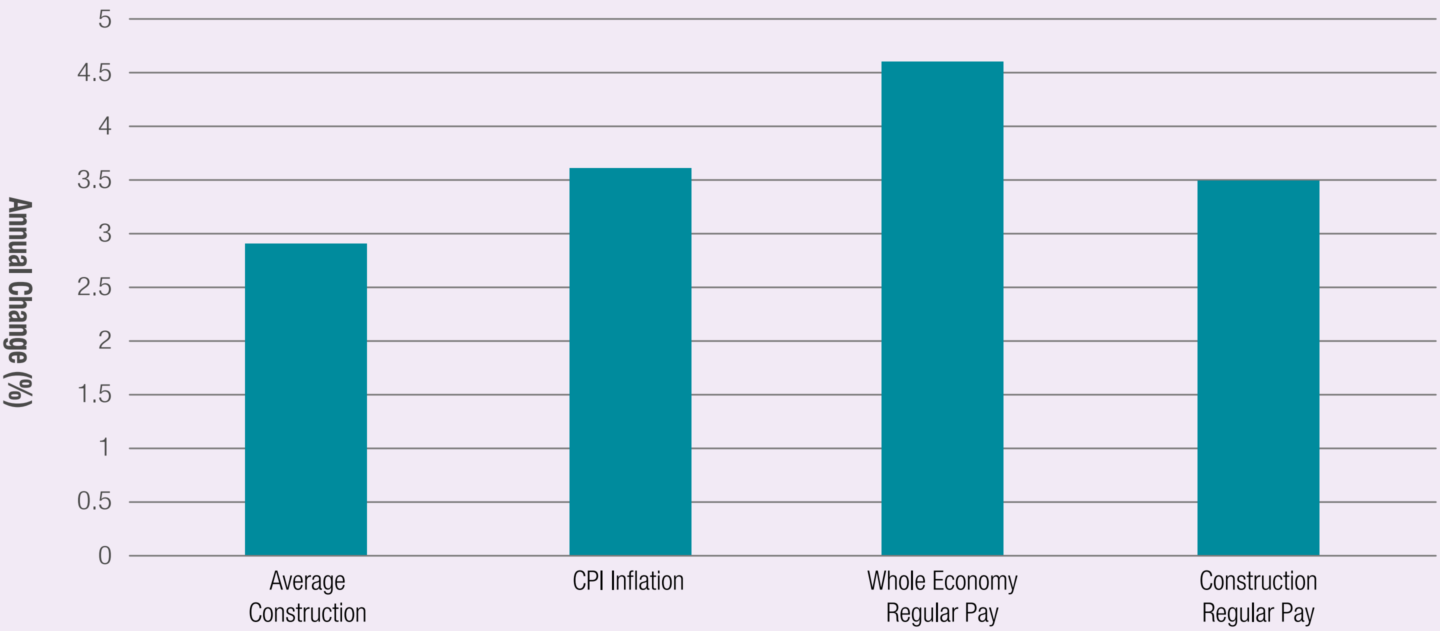


was 0.9%. Following declines during 2024, material prices are now starting to increase, albeit slowly and at a weaker pace than consumer price inflation. Lower oil prices will be helping keep a lid on material prices, however, despite moderate global growth, other commodities have seen substantial recent price rises. In particular, copper has surged on the back of concerns about supply shortages. Worry about new tariffs is causing some stockpiling of the metal, and along with disruptions at important mines, this has pushed prices up. Reaching record highs, this is likely to add to costs, most notably in the MEP and data centre space.

Whereas material prices are slowly starting to tick up, construction pay continues to decelerate rapidly. Standing at 3.5% in September, construction pay growth is now just below the rate of consumer price inflation, meaning workers are seeing a slight fall in real terms pay. While pay growth earlier in the year of over 6% was never likely to be sustainable, it has been an exceptionally marked slowdown. Reflecting broader industry challenges, other indicators also point to a weakening labour market, including falls in workforce jobs and the number of construction employees, and vacancies dropping to their lowest level since the pandemic. With November's S&P Global UK Construction PMI reporting a steepening in the pace at which firms are cutting staff numbers, this poor performance looks likely to have persisted through to the end of the year. In the immediate term, the slowdown may help contractors control costs, yet firms choosing to let staff go may create problems in the years to come. Some workers will choose to retire or leave the industry, resulting in worsening skills shortages. Leading to greater wage pressures down the line, delivery of future projects may also become harder. From an individual business perspective, not enough work warrants reducing headcount. However, at an industry level, this trend is likely to be storing up problems for the future.

CONSTRUCTION WAGE GROWTH CONTINUES TO COOL

Source: ONS, DBT



Note: Average construction material price is based on the 26 products published by the Department for Business and Trade.

Budget offers little new but reaffirms government commitment to capital projects

After several months of speculation and uncertainty that surveys suggest dampened investment, the Budget took place on 26 November. In the build-up, much of the concern centred around whether income taxes would rise and if Labour would have to break one of their manifesto promises. As it turned out, Rachel Reeves, Chancellor of the Exchequer, avoided this, in part by freezing tax thresholds. This will result in 780,000 more people paying the basic rate of tax and 920,000 paying the higher rate, raising an additional £8.0bn in 2028-29. Other changes to the tax system include pension contributions, gambling reform, income tax rates on property, savings and dividends, and a council tax surcharge on high-value property. As a result, taxes are set to climb to their highest ever level, reaching 38.2% of GDP in 2029-30.

In total, new taxes will raise £26.1bn by 2029-30, helping double the Chancellor's fiscal headroom from £9.9bn to £21.7bn. One reason there was so much pre-Budget speculation was due to the relative lack of budget surplus and doubts the government could meet its fiscal targets. By increasing the fiscal headroom, the Chancellor hoped markets would react positively and borrowing costs wouldn't increase. If this was the goal, it appears to have been achieved; however, the risks haven't disappeared. While taxes are set to rise, much of this will occur towards the end of this Parliament. However, by delaying it to near the time of a general election, there are questions about the political feasibility of pushing through the tax rises. By contrast, the spending increases in the Budget, including the removal of the two-child cap, are more front loaded. This means that improvements to the fiscal position will be slow, one thing businesses don't need is another lengthy period of alarmism leading up to a future Budget.

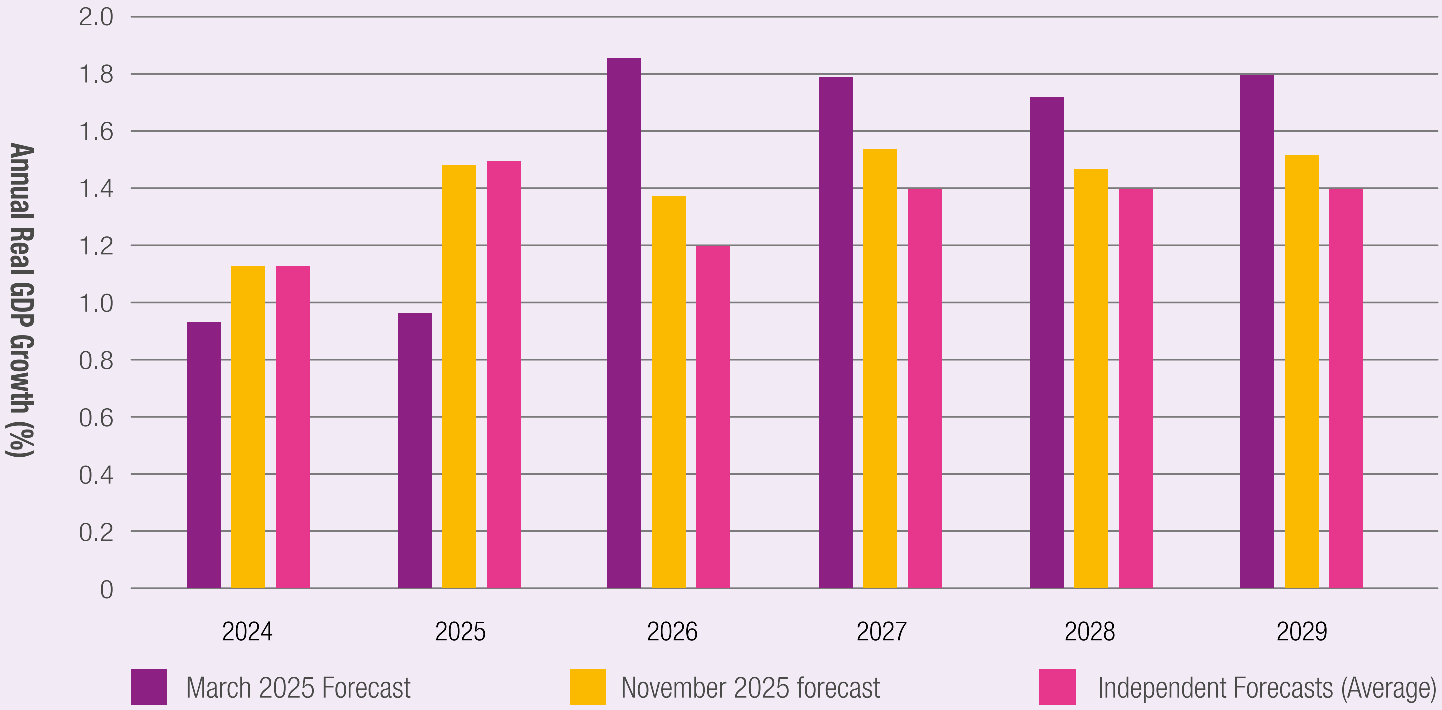
Given the bond markets' desire to increase the fiscal headroom, one alternative to higher taxes was cutting spending. Following the summer's Spending Review and Infrastructure Strategy, doing so could have posed a significant risk to construction projects. That such moves didn't happen is therefore a relief to the industry and one of the biggest takeaways from the speech. By protecting the additional £120bn of funding previously announced, the government is clearly fully committed to its capital expenditure programme. Further emphasising this commitment, the Budget allocated almost £900m to the Lower Thames Crossing, while the day before the Budget, the government backed Heathrow's £49bn plan for a new runway. However, while another mega project is good news for construction, it raises further questions about market capacity.

SHORT-TERM SPENDING INCREASES BEFORE TAX RISES HAVE A LARGER IMPACT

Source: OBR, HM Treasury

OBR DOWNGRADES GROWTH FORECASTS, BUT THEY ARE POTENTIALLY STILL TOO OPTIMISTIC

Source: OBR, HM Treasury



As well as political risks about tax rises and the impact not delivering these would have on the fiscal position, there are also risks around the economic forecasts. The OBR's productivity forecasts had been more optimistic than other forecasters for some time, and as widely expected, they have now been downgraded. By doing so, the OBR also revised down forecasts for economic growth. Even at a relatively modest 1.5%, there is a risk forecasts are still too optimistic and further downgrades are necessary. The OBR is more optimistic than other forecasters and were weaker economic growth to occur it would lead to lower tax revenues, making it harder for the government to meet its fiscal targets. Even if accurate, such modest growth suggests the construction sector will continue to face headwinds from a lacklustre economy.

Alongside adjustments to the macroeconomic outlook, the Budget included several announcements relevant to the construction industry. One change likely to particularly affect consultant fees is the change to the salary sacrifice scheme. The change caps the level at which pension contributions are exempt from National Insurance Contributions at £2,000. Yet while employees on over £50,270 have a 2% National Insurance rate, employers must pay 15%, making them much more exposed. This change is not set to come into effect until April 2029, so firms have several years to decide what to do. The OBR estimates employers will attempt to pass on 76% of the additional costs to the employee through lower employer pension contributions and lower salaries. However, skills shortages in construction, which will only worsen based on the pipeline of domestic and international projects mean employers may find reducing total remuneration hard and instead pass on higher costs through raising fees.

In a Budget that offered few direct measures for the sector, the planning system will benefit from another £48m to boost capacity, including support for 350 extra planners. The Planning and Infrastructure Bill has also now become law, while the government has also approved 29 major infrastructure projects over the past 16 months. Another decision welcomed by the industry is the choice not to converge Landfill Tax to a single rate. Were the lower rate of £4.05 to have increased to the standard rate of £126.15, it would have been a huge jump for the cost of disposing of products such as concrete and bricks and the industry pushed hard for this move not to happen. Given announcements earlier in the year, such as £15.6bn for major city-region transport, there was little new funding. However, an additional £1bn for fixing potholes should please motorists and support the repair and maintenance segment of the industry. Other recommitments where more detail was provided included for the regions, such as Manchester, Liverpool and Yorkshire, which would gain from Mayoral Revolving Growth Fund and Local Growth Fund. The general impression from the Budget adds to what we have known for a while. Namely, that with weak economic growth, government backed projects will be vital to supporting the construction sector.

How will the market deliver the upcoming pipeline of work?

Although the Budget introduced few new measures, the government's commitment to infrastructure remains clear. The additional £120bn announced in the Spending Review, combined with progress on the Planning and Infrastructure Bill and the approval of 29 major projects, confirms that a substantial pipeline will move forward over the next decade. Key programmes include the New Hospitals Programme, New Towns, East West Rail and Heathrow's expansion.

This pipeline will place sustained pressure on the market in terms of capacity, skills and risk appetite. Each one of these issues poses slightly different challenges for delivery and may require different responses from clients and the supply chain to meet them. Revenue data from major UK contractors shows that while several firms are capable of delivering large schemes, the scale of upcoming projects means that capacity constraints are likely, particularly where programmes overlap. While the graph shows all these firms have construction revenues over £1bn, the size and scale of some proposed schemes mean that a single project could account for a substantial share of most contractors' income. Therefore, as well as thinking about how to best manage each project and which strategies will result in efficient outcomes, one of the challenges with delivering all the plans in a reasonable timeframe will be finding enough contractors.

To secure delivery within required timeframes, clients may need to consider early engagement strategies and broaden procurement approaches to encourage interest from a wider pool of UK and international contractors.

Supply chain capacity presents a similar challenge. In addition to known labour shortages, some specialist sectors may experience constraints relating to experience or technical capability for first-of-a-kind projects. The government has billed the Lower Thames Crossing as the largest roadbuilding project in a generation, and while Heathrow and Gatwick both have

LARGEST CONTRACTORS MAY NOT BE ABLE TO BUILD EVERYTHING

Source: Annual Reports

plans for new runways the last one built in the UK was in 2001. Experienced teams tend to better understand requirements, spot problems earlier and improve the likelihood of projects finishing on time and on budget. This echoes findings from Mace's Future of Major Programme Delivery (FMPD) report, which highlights a global scarcity of mega-programme leadership experience and recommends knowledge transfer and capability-building through long-term delivery partnerships and structured PMO/CMO functions to mitigate these risks.

Early engagement with the supply chain will also be important as fuller order books reduce contractors' capacity to take on additional major schemes. In some cases, clients may benefit from widening the field to include international contractors with relevant experience, where this can help increase competition and capability. However, additional interest at the Tier 1 level alone will not address wider capacity constraints unless supporting subcontractors and supply chain partners are also able to operate in the UK market.

Market conditions also continue to influence contractor risk appetite. Large projects are inherently risky. They have more potential points of failure, and when things do go wrong, especially if costs escalate, the consequences can be severe. Part of the reason Carillion failed, when it was the UK's second largest construction company when it declared insolvency in 2018, was cost overruns on two hospital projects. Clients with clear scopes, balanced risk allocation and predictable governance processes are more likely to attract competitive interest. As highlighted in the Construction Playbook, collaborative approaches and aligned incentives support better market engagement and reduce the risk of delays. This aligns with the Future of Major Programme Delivery report's ten pillars of collaborative delivery, which emphasise trust and transparency, shared risk/reward frameworks, integrated 'one-team' structures and technology-enabled governance to create a single version of the truth and drive best-for-programme decisions.

All of this means clients cannot assume that having a large project will automatically attract contractors. While clients will still want to maintain commercial strength to achieve optimal value outcomes, securing the right partners will require more. They will need to engage with contractors and the supply chain early in the process and be able to provide clarity on the scope. Overall, while the pipeline presents significant opportunities for industry growth, successfully delivering it will require coordinated planning, realistic scheduling and constructive engagement between clients, contractors and the wider supply chain.

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