

ECONOMIC BULLETIN



A quarterly update from Franklin + Andrews

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The Economic Engine: Ready To Accelerate?

The UK's economy is driving through the second half of 2003 in low gear, restrained by a weak global recovery.

In the second quarter of 2003 the economy showed a modest rebound, a rise of 0.3%, picking up from a decade low of just 0.1% in the first quarter. The growth was helped by strong spending in consumer activities, while other areas such as business services and manufacturing remained weak. In general, household spending has rebounded recently with consumer confidence in July reaching the highest since last November. August has proved not to be so robust.

The Bank of England in July cut rates by a quarter of a percentage point to a 48-year low of 3.5% in response to weaknesses in the global economy. Despite expectations of an interest rate rise at the end of this year, in view of the recent signs of a mild recovery, a further move is unlikely until the spring of next year. At that time the effect of the recovery, if sustained, would manifest itself and the economy is expected to be in upswing driven by stronger global demand. However,

unexpectedly strong consumer spending and borrowing figures at home may trigger an earlier move in interest rates.

According to the Office for National Statistics (ONS) latest data, inflation rose by 0.1% in July to an annualised rate of 2.9%, indicating higher clothing and footwear prices and a surprise surge in retail sales.

External circumstances are slightly worrying. The weak performance of cross-Atlantic economies is also putting pressure on the UK. The US economy continues to disappoint despite the recent signs of a rebound in demand largely due to its increased military expenditure in Iraq. Meanwhile, the threat of deflation in Germany and Japan is dragging down the overall picture of the world economy. The expected reconstruction of Iraq has as yet not commenced in any significant manner due to ongoing security issues.

The mid term economic prospects in the UK look particularly uncertain at the moment. Businesses, meanwhile, are going from strength to strength but still holding off from

large-scale investments. The revival of the economy is dependent upon a recovery in demand and profitability, which looks more doubtful. A further cooling of the consumer spending boom and a steadying of house prices is anticipated for the coming year.

The construction sector, which achieved growth of 8% last year, is expected to see continued growth in new work output in 2003, but at a much slower rate than 2002, followed by a further rise in 2004. Funding from the public sector will be the main driver behind the expected growth in output, primarily in the public non-housing and infrastructure sectors. With considerably strong growth in new construction output in 2003, input costs are also expected to increase.

Tender prices in the first quarter of 2003 increased by 8.2% from a year earlier. Material prices, meanwhile, rose by 4.1%, slightly ahead of retail price inflation. Demand on skilled workers, bricklayers in particular, rose in the first quarter of 2003. However, difficulty in securing skilled labour to meet demand signalled that the supply side is

also in trouble. The Construction Industry Joint Council (CIJC) has agreed a three-year wage settlement for building and civil engineering operatives, providing, on average, a 7.2% wage increase over the next three years.

Tender price inflation is expected to rise, on average, by 5.2%, well above RPI inflation throughout the next two years. Given that the RPI inflation rate would generally remain between 2.5% to 3.0%, construction material prices are expected to increase above this rate, by 3.1% on average over the next two years. Wage agreements are also likely to rise faster than RPI inflation over the same period.

Our latest forecast is that the UK economy will grow by around 2% this year, rising to 2.5% next year, a somewhat gloomier expectation than that indicated by the Chancellor earlier this year. 2003, is going to be a year of 'rebalance' for the UK's economy before heading back to more substantial growth in 2004.

Table 1 Construction costs index (Annual change)

	2001	2002	2003*	2004*	2005*
Building sector tender prices	7.8%	8.7%	5.9%	4.5%	4.0%
Building input costs	3.3%	4.3%	4.7%	3.7%	4.1%
Labour	5.0%	6.5%	7.1%	6.0%	7.1%
Materials	1.5%	1.9%	3.3%	2.8%	2.3%
Plant	1.8%	2.8%	5.8%	3.3%	3.7%
Retail prices	1.8%	1.6%	3.0%	2.9%	2.5%

*Forecast



A view from the Chief Executive

by Guy Leonard

2003 – A Challenge Year to Global Construction Economics

The global economy in 2003 has had to deal with a number of significant uncertainties, but despite this world economic growth is forecast to achieve 3.2% during 2003. This growth is largely dependent on the US and China, given the near standstill in the Euro area.

The US economy has weakened recently with GDP in the first two quarters of 2003 increasing by a mere 1.4% and 2.4% respectively in real terms, primarily reflecting upturns in federal defence spending and in non-residential fixed investment. Business investment has stabilised and household spending has slowed down due to the impact of higher energy prices on real incomes.

EU growth prospects remain lack-lustre. The economy has experienced virtually no growth in economic activity in the first half of 2003 and major indicators continue to suggest slow growth, at a rate of less than 0.5%. The stronger Euro and lower interest rates suggest a higher contribution to growth from domestic rather than foreign demand, which would support growth during the second half of this year.

In Germany growth is expected to be minimal at around 0.25% in 2003, with a significant risk of the economy falling back into recession this year. German deficits are forecast to be above the 3% Stability Pact limit again this year.

Growth in France is projected to remain moderate. After picking up sharply at the beginning of the year, GDP growth slowed to 1.6% in the second quarter. The French economy needs substantial budgetary savings in the near future to ensure the sustainability of public finances, particularly in the face of rising pension obligations.

In Italy growth continues to be sluggish because of flagging domestic confidence and weak export performance. A recovery is expected to begin in the second half of 2003, gathering strength in 2004, which is driven by low real interest rates, reviving confidence, and accelerating world demand. Inflation in Italy is expected to decelerate, stabilising at 1.7% by the end of 2004.

Economic performance in Asia Pacific (excluding Japan) has been impressive, particularly in China, with real GDP increasing on an upward trend and expected to continue in 2004.

African GDP growth is forecast to pick up in 2004, underpinned by continued policy strengthening, the global recovery and higher non-fuel commodity prices. However, this growth is critically dependent on an early improvement in political stability in West Africa.

Middle East GDP growth has been forecast to pick up this year. However, the ongoing security issues in Iraq continue to cast a shadow of uncertainty onto any economic predictions made.

The global economic outlook is expected to improve next year, which should prompt stronger growth in the construction sector in 2004. The outlook for the construction industry in 2003/4 varies from one region to another. In the EU there are a few bright spots with both the UK and Spain construction markets performing well.

In Asia Pacific region construction investment is expected to increase, given that major contributors in the region such as China and Japan are experiencing increasing construction demand and infrastructure development.

UK economic growth in the construction sector has slowed down and GDP is expected to remain stronger than other major European economies in 2004. Growth is forecast to achieve a target of around 2% this year, underpinned by the stepping up of Government spending. However, the Government faces a challenge in ensuring that higher spending is fully translated into better public services.



RPI...RIP?

What inflation index is your contract linked to?

The current method for calculating UK consumer retail price inflation is about to change (subject to confirmation at the time of the Chancellor's Pre-Budget Report in autumn). This change will result in the adoption of the European Standard methodology – a system that to date has resulted in calculating inflation values of up to one half of that recorded by using the existing UK approach. We explore what this could mean to your RPI index linked construction contracts.

Long-term construction contracts and service agreements frequently embody a mechanism for calculating and recovering price fluctuations. One widely adopted approach is to link contract values to the Retail Price Index (RPI) figures published by the Government. In his statement on the Government's policy and economic union on 9 June 2003, the Chancellor announced that, subject to confirmation in the pre-budget report, he intends to change the definition of the target for UK inflation from the RPIX to the HICP (Harmonised Index of Consumer Prices).

The Chancellor has stated that the current procedure for updating pensions and benefits and index-linked gilts will remain for now, but it is extremely unlikely that the Government will continue to fund the updating in this way in the long term. A number of economists see this move as another sign of Britain preparing itself for joining the Euro.

So what are the main differences

Although similar in their methodologies, the main differences for calculating these two methods of retail inflation are listed below:

- HICP excludes inflationary elements of housing and council tax.
- HICP includes additional inflationary elements of university accommodation fees, overseas student fees, unit trust and stockbroker charges.
- The HICP Index is calculated using a geometric mean, RPI uses an arithmetic mean. The principal difference between these two calculations is in the use of the weightings assigned to each commodity. The arithmetic mean assigns weightings that change on an annual basis only, whilst a geometric mean allows for changes in the weightings due to any changes in price.
- The HICP Index is based upon the International classification system, thus allowing fair comparison against other countries.

The table below highlights the differences between the three main measures of consumer price inflation in the UK over the last 8 months. The use of HICP consistently generates a lower inflation factor than RPI or RPIX.

Our recommendation is review your contract inflation recovery clauses before the autumn statement. If HICP is adopted, contracts currently linked to Government inflation reports could well witness a significant under-recovery. The effect will obviously vary depending upon the fluctuation clauses and formulae stated within the contract but the amount recovered could halve, based on the current index performance highlighted above.

Date	All items (RPI)		All items excluding mortgage interest payments (RPIX)		Harmonised index of consumer prices (HICP)		% Difference of annual inflation of RPI & HICP	% Difference of annual inflation of RPIX & HICP
	Index	% over 12 months	Index	% over 12 months	Index	% over 12 months		
Nov	178	2.6	177.0	2.8	108.9	1.6	1.0	1.2
Dec	179	2.9	177.2	2.7	109.3	1.7	1.2	1.0
Jan-03	178	2.9	177.1	2.7	108.6	1.4	1.5	1.3
Feb	179	3.2	177.9	3.0	109.0	1.6	1.6	1.4
Mar	180	3.1	178.7	3.0	109.4	1.6	1.5	1.4
Apr	181	3.1	180.0	3.0	109.7	1.5	1.6	1.5
May	182	3	180.2	2.9	109.7	1.2	1.8	1.7
Jun	181	2.9	180.0	2.8	109.6	1.1	1.8	1.7

Spotlight on the UK Construction Sector

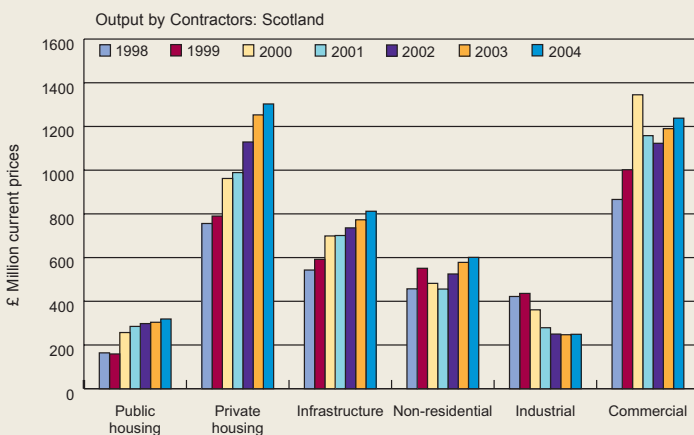
UK Regional Analysis

Franklin + Andrews' annual regional output analysis explores what is on the horizon for the UK Construction Industry.

Scotland

Performance in Scotland was poor last year compared with most other regions in the UK. New construction output rose by 5% in 2002 to £4.06 billion, and new orders increased by 9% to £2.97 billion, compared with £2.72 billion in 2001. Private housing and public non-residential construction showed strongest growth in the region last year.

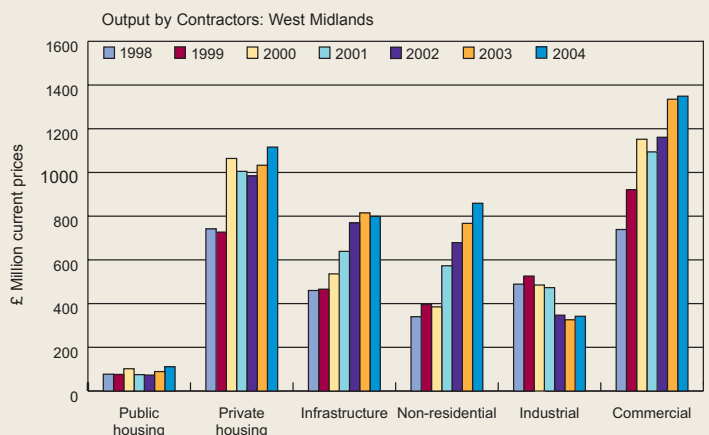
Overall, construction output is forecast to rise slightly this year by 5.5%, and by 3.8% in 2004.



West Midlands

Construction output in new work last year reached £4.01 billion in current prices, a moderate 4% growth, compared to £3.86 billion in 2001. New orders in 2002 rose by 19% to £3.14 billion.

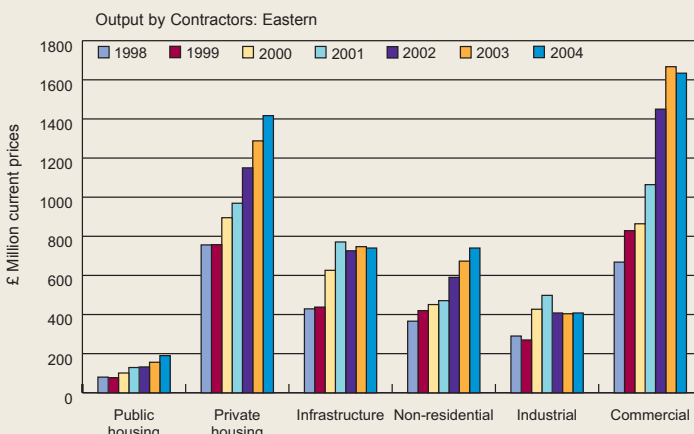
Output in the region is forecast to show steady growth over the next two years: projected growth is set at 8.8% for 2003, and 4.8% in 2004.



Eastern

Construction output in new work in the Eastern region (including East Anglia and Beds, Essex and Herts) showed exceptional growth last year. New work reached £4.46 billion in current prices – 14% higher than in 2001 – and new orders overall set a record in 2002, reaching £3.46 billion – an increase of 21% on 2001.

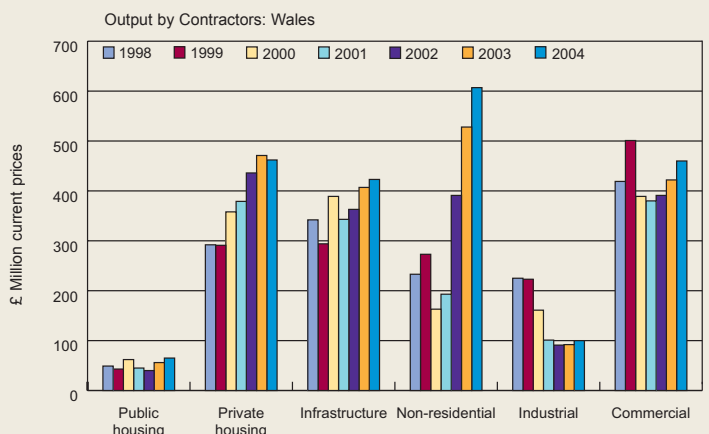
Output overall in Eastern is anticipated to continue to grow by 10% this year, and by 4% in 2004.



Wales

New construction output rose strongly in 2002 by 19% to £1.71 billion in current prices, compared to £1.44 billion in 2001. New orders also increased last year to £1.38 billion – 36% higher than in 2001. Output in the public non-residential sector demonstrated the highest growth rate in the region, with more than doubled growth in 2002.

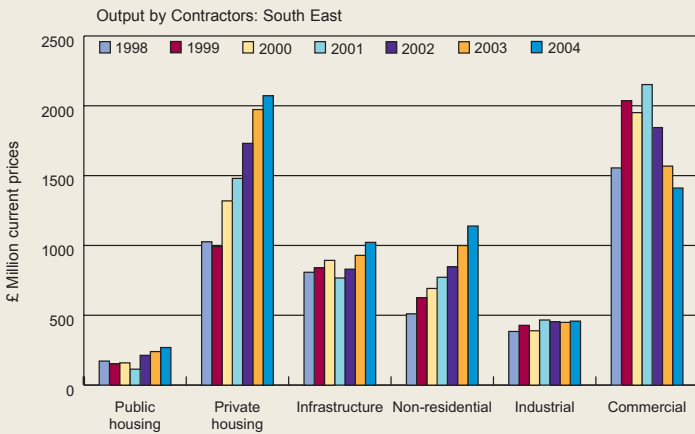
Overall, construction output in Wales is forecast to sustain the upward trend in 2003, with 17% growth, and a moderate rise of 8% in 2004.



South East

Construction output in new work rose by 3% in 2002 to £5.92 billion at current prices, the lowest growth rate of any region. New orders increased by only 2% in 2002, following a 17% rise in the previous year.

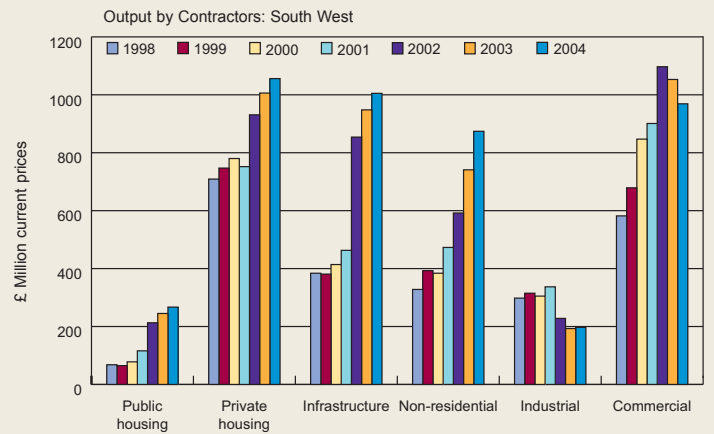
Considering the strength of private housing and public non-residential construction in the region, it is forecast that construction output will continue to grow – by 4.1% in 2003 and 3.5% in 2004.



South West

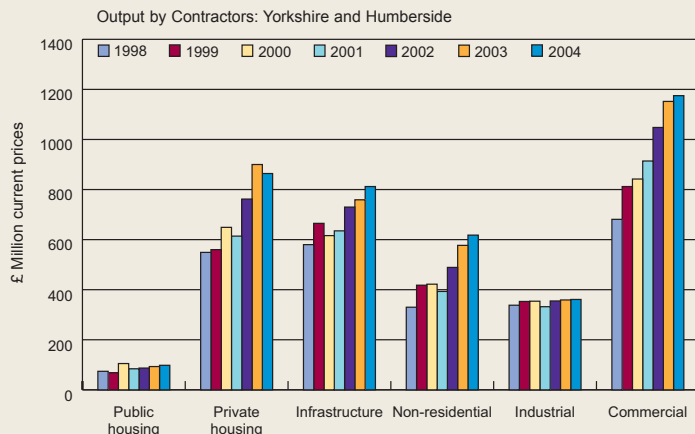
The South West was the most buoyant region of the UK in 2002, with particularly strong growth in construction, mining, utilities and most service sectors. New construction output rose by 29% to £3.9 billion, the highest growth rate of all the regions, and new orders also increased strongly by 28% in 2002, compared with a modest rise in 2001.

The strength of new orders in 2002 suggests the upward trend in output is likely to continue over the next few years although the increase may be smaller than previous years. Construction output in the region is forecast to rise by 6.9% in 2003, and by 4.4% for 2004.



Yorkshire and Humberside

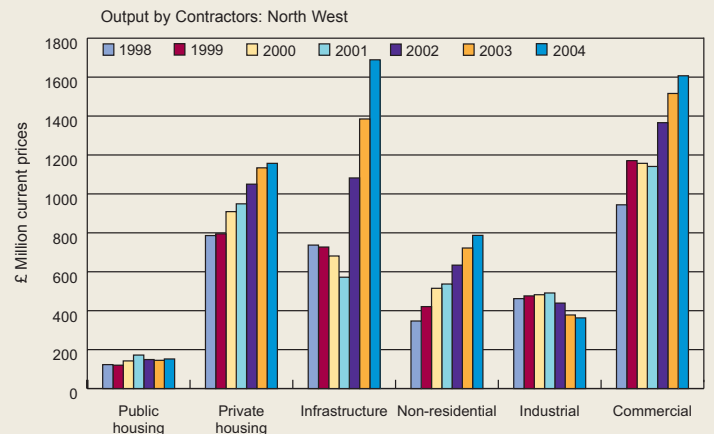
New construction work in Yorkshire and the Humber last year rose by 17% to £3.47 billion, and new orders in 2002 increased by 16% to £2.42 billion. Public non-residential construction saw the highest growth rate in output as a large number of new health and education projects came on stream. Overall, construction output in the region is forecast to moderate, with growth of 10.6% and 2.3% in 2003 and in 2004 respectively.



North West

New work in the North West region last year grew by 22% to £4.72 billion. All sectors saw significant growth except public housing and private industrial construction, and new orders in 2002 remained very robust, reaching £3.39 billion.

Output in the region is forecast to grow by 12% in 2003 and by 9% in 2004.





A Spotlight on Egypt

Egypt's economy is the 39th largest in the world. Located in the northeast corner of the African continent, the republic, with an area of around four times of the size of the UK, provides the link between Africa and Asia. Its official language is Arabic with English and French widely used in business circles.

Country profile

Name: Egypt, Arab Republic of

Area: 1 million km²

Population: 65.99 million (est. 2002)

Official language: Arabic

GDP: LE387.5 billion (US\$89.8 billion, est. 2002)

Exchange rate: (floating regime)

1US\$= 6.1300 Egyptian Pound (LE); (Aug.2003).

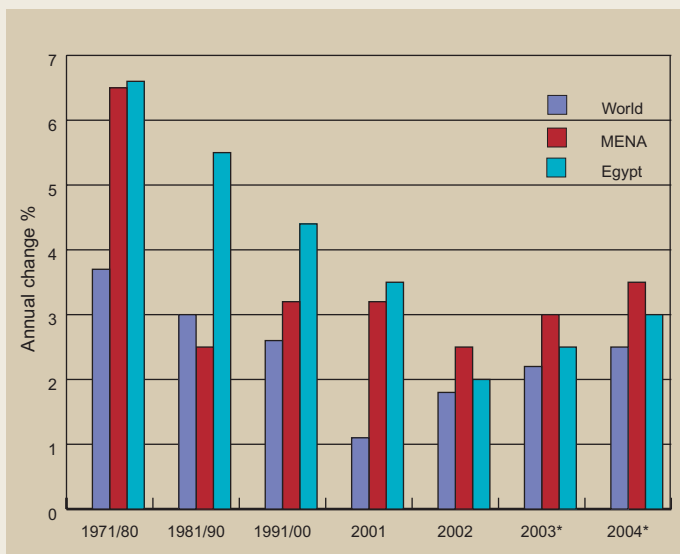
1GBP£ = 9.8765 Egyptian Pound (LE)

With a population of 65.99 million, Egypt achieved GNI per capita US\$1530 in 2002, classifying itself as a middle-income economy worldwide. Egypt remains the second largest recipient of US aid after Israel, and has strong links to EU countries, which represent its major export market. The country has a pivotal role in the region as a leader of the Arab world and a key player in the Middle East peace process.

Economic review

Egypt's economy grew strongly in the late 1970s and early 1980s largely due to buoyant foreign exchange receipts from oil exports, workers' remittances, and tolls from the Suez Canal and tourism. However, slow global growth and the fall in world oil prices in the mid-1980s caused massive fiscal and current account deficits to the Egyptian economy.

Real GDP Growth



(MENA: Middle East & North Africa; Data source: World Bank; *: F+A Forecast)

Following the implementation of the Economic Reform and Structural Adjustment Programme (ERSAP) aided by the International Monetary Fund (IMF), the Egyptian economy began to grow again in the earlier 1990s. The ERSAP project had significantly reduced inflation and improved the current account balance, allowing for large-scale investment in infrastructure and key projects. However, economic performance weakened in the late 1990s as a result of domestically slow structural reforms and external factors such as a temporary downturn in tourism, reduced oil prices and tightened global finance following the Asian Crisis.

Recent economic development

The energy sector continues to play a major role in the economy, contributing 8% to GDP. In addition to exporting oil, Egypt enjoys a strategically important position controlling both the Suez Canal and the Sumed pipeline – two major export routes for oil from the Gulf. However, transportation and revenues from these two routes have fallen with competition from a new route via the Cape of Good Hope and in response the Suez Canal Authority has recently lowered its charges to halt the decline. Natural gas is expected to overtake oil as the main source of both the energy sector growth and export revenue when its exports start in 2005.

Economic policy and challenge

The Egyptian economy has not suffered from inflationary pressure since the mid-1990s and inflation has steadily fallen, from 9.9% in 1995 to 2.4% in 2002. However, the devaluation of the Egyptian Pound is expected to push the inflation rate to above 3% in 2003. After 10 years of being tied to the US dollar (at LE3.4/US1\$), the Central Bank of Egypt (CBE) has adopted a floating exchange rate: the Egyptian pound was devalued sharply to about LE6.12/US1\$ in August 2003 and since early 2002, the currency market has effectively been paralysed by the CBE's inability to supply foreign currency, pushing banks and bureaux to rely on their own resources. This shortage of foreign currency is a serious obstacle to the country's economic growth.

Imports, including capital goods such as machinery and transport equipment and consumer goods, are increasingly hitting local products. Exports are at the mercy of world prices – mainly comprising raw materials such as crude oil, raw cotton and farm crops – and the US has recently suspended plans to advance free trade talks with Egypt, in response to its decision not to join the US in a complaint against Europe's ban on Genetically Modified (GM) foods. It is likely to affect the country's initiatives to stimulate exports by forging new links on trade.

Financing schemes such as BOOT (Build-Own-Operate-Transfer) and BOT (Build-Operate-Transfer), mainly restricted to large-scale infrastructure projects, have not proved advantageous, and they continue to weigh on the state budget. The Government has preferred to set up financially independent holding companies, and has retained a monopoly in many service industries as well as in banking and insurance, and remains dominant in the textile, steel and aluminum industries.

Egypt has made significant progress in reducing non-monetary poverty and its health indicators, in particular, are much higher than the African average.

The Government is keen to attract foreign investors by increasing transparency, protecting investor rights, and ensuring equality of treatment. But regional insecurity and the country's poor economic performance militated against these efforts. However, Egypt is trying to tackle all of these challenges and its structural weaknesses through continued policy reforms and institutional strengthening.

The construction sector overview

The construction industry is considered one of the most capital and labour intensive industries of the Egyptian economy. Domestic companies are major players in Egypt, undertaking about 70% of all construction work.

Egypt is currently involved in a huge infrastructure project over the next 20 years intended to create a new river delta parallel to the Nile Valley which will open up tracks of land for agriculture, industry and settlement. The core of the project is a 310 km long canal taking Nile water from Lake Nasser to the Western Desert.

Public investment is forecast to continue growing with the Government launching a programme to increase the country's habitable area, from the current 5% to more than 25% of the total country's area by 2017.

BOOT and BOT programme

The Egyptian Government intends to generate significant growth in the construction sector by transferring large-scale infrastructure development projects to the private sector. The programmes include power stations, airports, roads, water projects and oil and gas schemes.

Sidi Krier II, Egypt's first venture into private sector BOOT power generation, a US\$ 400 million project to generate 650 MW, is now one of two power generation plants under construction. A total of 15 BOOT power projects are planned for offer to the private sector in the coming two decades, intended to meet an annual 7-8% increase in demand for electricity.

A glance of the country's large-scale projects

- Construction of Toshka Canal Project, which aims to double the size of Egypt's arable land in 15 years' time at an estimated cost of US\$88.5 billion
- The National Sinai Development project with a total expected investment of US \$74.7 billion
- The establishment of a new port and economic zone in the Gulf of Suez (LE 150 billion)
- The establishment of a new port, and free zone in the East of Port Said (LE 150billion)
- Naga Hammadi Dam Project; building of 44 new cities; Urban housing for 10 million people
- The new Media City on the outskirts of Cairo at an investment cost of US \$323 million

Regional relations

The great challenge to countries in this region remains to create enough jobs for the rapidly growing work force in the coming decade.

Economic transitions could be the solution for the region creating new models that are more reliant on trade and private investment. Early reformers such as Jordan, Tunisia and Morocco have been taking greater steps at trade and investment reforms. Many countries are also seeking to strengthen their trade partnerships with Europe, their largest trade partner.

	Population 2001 (million)	2002 per capita 2001 (US\$)	Total GDP 2002 (US\$ million)	Real GDP growth 2002 (% Change)	World rank by size of GDP
MENA	301	2,220	693,526	2.5	NA
Algeria	31	1,650	55,666	3.1	50
Egypt	65	1,530	89,845	2	39
Iran	65	1,680	107,522	6	34
Iraq	24	2,400*	58,000	-3	NA
Jordan	5	1,750	9,296	4.9	89
Lebanon	4	4,010	17,294	2.0	70
Libya	5	6,090*	34,137	1.7	57
Morocco	29	1,190	37,263	4.5	55
Saudi Arabia	21	8,460	186,489	2.1	23
Syria	17	1,040	21,872	2.7	64
Tunisia	10	2,070	21,169	1.9	66
West Bank, Gaza	3	1,350	3,015	-22	127
Yemen	18	450	10,395	4.3	85

Data source: World Bank, IDSC, Egypt *. Estimation



Inflation analysis

Inflation Cost Driver Analysis – Retail Facilities

Updating the cost of construction projects built in the past to reflect current cost levels is often undertaken using indices that track price movements. This process often begins with the assumption that inflation drivers are the same, regardless of the type of project. This leads in almost all cases to the use of one index to update projects that are in fact subject to very different inflation drivers. To highlight this point Franklin + Andrews has conducted a number of project specific inflation studies on different building facility types.

In this report we examine the inflation drivers of retail facilities.

The study examines the cost input inflation of building material components, labour and plant since January 2001. The results have been rolled up and summarised into elements to allow ease of comparison.

The results of this study indicate that each project has experienced different levels of inflation. During the study period, the material cost of steel has remained relatively stable throughout. However, by

comparison, concrete has witnessed inflation of approximately 22%, due in part to the introduction of the Aggregates Levy in 2002. This has impacted on the elemental costs of the frame construction. For example, a department store frame constructed out of reinforced concrete increased by approximately 12.7% over the study period, whereas the steel frame structure of the other facility types increased, on average, by only 8.4%, primarily due to labour increases witnessed during the study period.

Services elements once again witnessed some deviances in inflation increases. Disposal installations in a supermarket increased by a modest 3.2%, whereas in a department store disposal installation costs increased by 8.1%.

In order to highlight the impact of inflation in monetary terms, we have displayed these increases as a cost per m2 of sales area or a cost per m2 gross floor area. For example, the percentage increase witnessed for services equipment in both a supermarket and a department store were roughly the same. However, in monetary terms this equates to an increase of £51.16 per m2 of sales area for a supermarket and £2.87 per m2 of sales area for a department store.

The study has identified that all of the facilities have increased by more than 5%, with an average facility increase around 7% for the inflationary study period. This equates to a cost increase of £174.87 per m2 of sales area for a supermarket, and a £154.06 per m2 gross floor area increase for an enclosed mall style shopping centre.

The average cost inflation (using a generic building cost index) for the same period indicates an inflation adjustment of 11%, whereas our study clearly indicates a far lower figure dependant upon specification and weighting of design layout.

Input cost increases from January 2001 to June 2003

Facility Type	Supermarket		Department Store		Shopping Centre			
	Cost (£/m2 Sales Area)	%	Cost (£/m2 Sales Area)	%	Enclosed Mall		Open Arcade	
					Cost (£/m2 GFA)	%	Cost (£/m2 GFA)	%
Substructure	23.81	14.6%	16.75	14.8%	18.08	13.5%	15.17	13.7%
Frame	13.16	8.3%	3.26	12.7%	10.30	8.4%	9.46	8.5%
Upper floors	–	–	11.34	13.3%	4.86	14.0%	5.54	13.5%
Roof	12.91	9.5%	3.95	10.1%	25.48	3.7%	19.18	5.8%
Stairs	–	–	0.84	11.9%	7.51	5.5%	5.39	5.6%
External walls	3.23	4.5%	6.78	8.0%	6.25	5.5%	11.81	4.0%
Windows and external doors	1.56	3.3%	0.14	1.3%	3.39	4.7%	1.21	5.8%
Internal walls	2.77	6.7%	2.32	8.7%	2.45	6.3%	–	–
Internal doors	0.60	3.0%	0.74	4.1%	–	–	–	–
Wall finishes	0.60	3.2%	0.77	8.6%	8.55	4.6%	3.17	6.0%
Floor finishes	1.49	2.3%	0.66	2.2%	11.70	5.6%	13.42	8.6%
Ceiling finishes	3.44	6.3%	1.67	4.5%	6.44	6.9%	3.38	6.9%
Fixtures and fittings	18.85	7.7%	10.39	7.0%	10.59	8.2%	8.34	9.0%
Sanitary fittings	0.47	3.2%	0.07	4.3%	–	–	–	–
Services equipment	51.16	7.4%	2.87	8.0%	–	–	–	–
Disposal installations	0.55	3.2%	0.50	8.1%	1.02	7.2%	1.28	6.9%
Water installations	2.30	7.3%	0.49	7.7%	0.22	7.9%	0.23	8.1%
Heat source	–	–	1.14	7.3%	–	–	–	–
Space heating and air treatment	19.05	7.2%	5.62	7.0%	9.91	6.7%	–	–
Ventilating system	–	–	–	–	–	–	–	–
Electrical installation	9.90	4.2%	4.69	4.4%	8.87	4.9%	6.37	5.0%
Gas installation	–	–	0.22	8.1%	–	–	–	–
Lift and conveyor installations	0.70	6.6%	3.52	6.2%	6.14	5.5%	8.00	6.4%
Protective installations	2.55	6.5%	2.96	7.5%	1.22	7.4%	0.11	7.8%
Communications installations	0.92	4.6%	0.16	4.4%	3.35	4.2%	2.94	4.6%
Special installations	–	–	0.28	8.1%	5.57	7.2%	6.44	7.8%
Builders' work in connection	4.84	7.5%	1.42	7.0%	2.16	6.6%	1.48	7.2%
Facility increase	174.87	7.3%	83.55	8.2%	154.06	5.9%	122.93	6.8%

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SPECIAL REPORT

Economic Bulletin



October 2003

Railway cost driver analysis

Franklin + Andrews has developed a unique set of indices to reflect both cost and tender price movement of railway construction.

Analysis and discussion with leading specialists within the sector established a need for the indices. The indices are offered as an alternative to the existing use of the Retail Price Index (RPI) to inflate and deflate project budgets. A regular review and updating of the indices with forecasts for future cost and tender movements will be published on a half yearly basis.

Cost Components

The following were established as being typical of cost significant components of major railway projects.

- Signalling
- Telecommunications
- Electrification
- Permanent Way
- Stations and Civil Engineering

Through use of weighting existing public domain indices for

historical movements and linear regression techniques for predictions, cost indices have been created for each of the five components from a base year of 1995. These indices have been weighted to replicate a typical major infrastructure project in order to generate a Railway Project Cost Index.

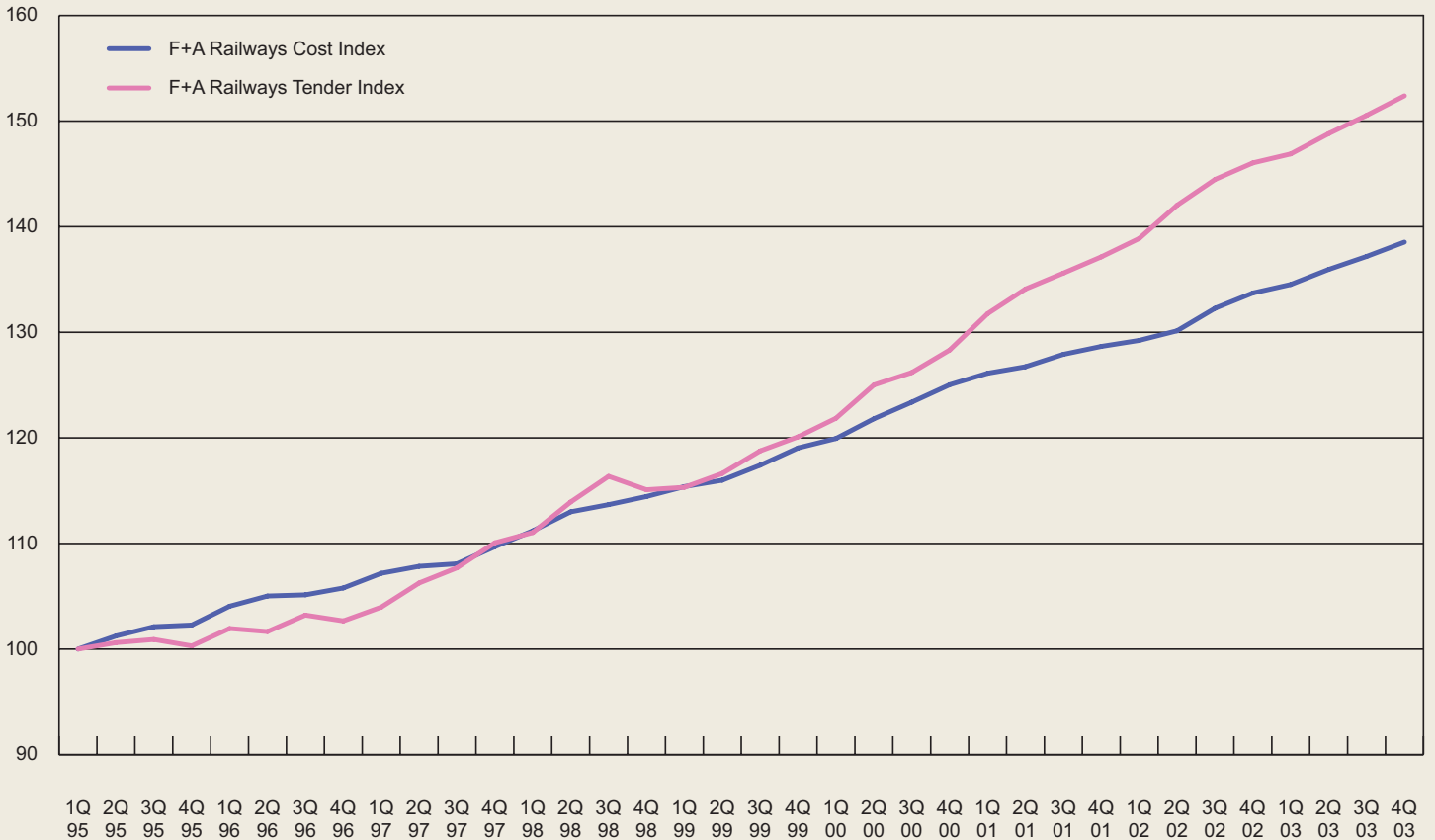
As a number of the cost components are subject to market forces, a series of tender indices have also been included. These tender indices have been weighted to produce a Railways Project Tender Index.

Cost Indices													
	Oct-02	Nov-02	Dec-02	Jan-03	Feb-03	Mar-03	Apr-03	May-03	Jun-03	Jul-03	Aug-03	Sep-03	Oct-03
Signalling	135.38	135.28	135.59	127.17	136.54	137.01	137.48	137.96	138.43	138.91	139.38	139.86	140.33
Telecoms	133.00	132.94	133.16	133.53	133.90	134.27	134.65	135.02	135.39	135.76	136.13	136.51	136.88
Electrification	133.00	132.94	133.16	133.53	133.90	134.27	134.65	135.02	135.39	135.76	136.13	136.51	136.88
Permanent Way	137.14	136.60	137.38	137.89	138.39	138.90	139.40	139.91	140.41	140.92	141.43	141.93	142.44
Stations and Civils	132.77	132.41	132.82	133.30	133.79	134.28	134.76	135.25	135.73	136.22	136.71	137.19	137.68
Typical Railways Project Cost Index	133.00	132.94	133.16	133.53	133.90	134.27	134.65	135.02	135.39	135.76	136.13	136.51	136.88

Tender Indices													
	Oct-02	Nov-02	Dec-02	Jan-03	Feb-03	Mar-03	Apr-03	May-03	Jun-03	Jul-03	Aug-03	Sep-03	Oct-03
Signalling	133.31	134.26	134.43	137.44	137.81	137.77	138.15	138.69	138.68	139.69	141.94	142.08	142.92
Telecoms	131.28	132.03	135.29	138.55	138.89	138.69	139.12	139.68	139.62	140.66	141.06	141.16	142.05
Electrification	131.28	132.03	135.29	138.55	138.89	138.69	139.12	139.68	139.62	140.66	141.06	141.16	142.05
Permanent Way	135.83	136.33	135.23	137.32	137.02	137.10	137.65	138.28	140.90	141.87	142.51	141.92	141.90
Stations and Civils	130.33	130.73	130.14	132.05	132.18	132.33	132.88	133.69	135.61	136.37	136.91	136.47	139.66
Typical Railways Project Tender Index	130.43	131.06	131.76	133.80	134.01	134.10	134.52	135.01	135.60	136.39	137.17	137.14	137.58

Base Jan 1995 = 100

Railway cost driver analysis



Cost Indices Annual Inflation							
	2002	2003	2004	2005	2006	2007	2008
Signalling	4.39%	4.15%	3.02%	3.48%	3.41%	3.32%	3.23%
Telecoms	2.46%	3.32%	2.70%	2.82%	2.74%	2.66%	2.59%
Electrification	2.46%	3.32%	2.70%	2.82%	2.74%	2.66%	3.59%
Permanent Way	6.90%	4.35%	2.99%	3.69%	3.62%	3.52%	3.43%
Stations and Civils	7.24%	4.37%	3.87%	4.05%	3.98%	3.89%	3.81%
Typical Railways Project Annual Cost Inflation	4.20%	3.98%	3.25%	3.39%	3.31%	3.22%	3.14%

Tender Indices Annual Inflation							
	2002	2003	2004	2005	2006	2007	2008
Signalling	6.48%	6.23%	5.40%	5.68%	5.49%	5.28%	5.10%
Telecoms	4.45%	4.21%	4.95%	4.69%	4.51%	4.33%	4.18%
Electrification	4.45%	4.20%	4.75%	4.61%	4.43%	4.26%	4.11%
Permanent Way	9.00%	5.67%	4.75%	5.45%	5.28%	5.07%	4.89%
Stations and Civils	9.36%	6.13%	5.65%	5.93%	5.75%	5.55%	5.37%
Typical Railways Project Annual Tender Inflation	5.72%	5.02%	4.74%	4.80%	4.65%	4.49%	4.35%

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