THE PERFECT STORM

WILL BREXIT KILL THE UK CONSTRUCTION INDUSTRY?

FIND OUT:

- HOW NEW IMMIGRATION LAWS COULD WORSEN THE SKILLS SHORTAGE.
- HOW IMPORT AND TRADE TARIFFS WILL IMPACT OPERATIONAL COSTS.
- HOW CUSTOMS DELAYS WILL AFFECT PROJECT DELIVERY.
- HOW YOU CAN PREPARE YOUR ORGANISATION BY HAVING THE RIGHT PEOPLE AND SKILLS IN PLACE TO MITIGATE THE RISKS.

ELLIS FOX
TOP TALENT FOR MAIN CONTRACTORS
INTRODUCTION:

Since the NO vote was announced following the Brexit referendum there has been endless debate regarding the consequences of leaving the EU. Rounds of talks in the interim have yielded little clarity, and now as the deadline looms closer, it appears sides are digging in, in an effort to protect their own interests. But what are these interests and how will they serve the British construction sector?

While early, very optimistic predictions were that no that much would change, most businesses leaders are no longer (though most never were) living under that illusion. With an increasing possibility that a no-deal Brexit might well be the reality, it is going to change the landscape significantly for British businesses, both big and small.

If there was a belief before that the British economy was strong enough to weather this storm, that confidence is now being seriously questioned. In the construction industry in particular, performance in the past decade has been poor, with major losses being posted by some firms while others are squeezing by on slim margins.

Project costs are rising and output is down, with many flagship projects announcing lengthy delays for completion. Legacy projects are proving to be a thorn in the flesh for many main contractors. Plus statistics reflect a major skills shortage in the construction sector which will be exacerbated when senior level employees retire from the industry in the future.

If all of this is happening while Britain is still part of the EU, what is going to happen when there is no longer free trade or free movement of workers? When tariffs are added to the supply chain and materials are held up in customs checks? If contractors wish to survive the pending storm, it is going to require a fresh approach to doing business, because with the rules changing, the game is never going to be the same.

This white paper takes a critical look at some of the most pressing issues facing the construction industry in the UK, and how their impacts may be compounded by Brexit. Will the industry be able to learn from the mistakes of the past and can skills, expertise and innovation be the driving force behind the change that is needed to keep the industry afloat?

ABOUT ELLIS FOX:

Ellis Fox recruits top talents for the top 50 main contractors in infrastructure and utilities.

Specialising in this senior niche of construction recruitment, it is critical that we stay up to date on industry happenings and the impact they have on various sectors of the industry.

It is only by doing this that we can ensure we’re identifying the right people with the right skills to place in senior positions, and who will have to navigate the changes the industry is experiencing.

These are our thoughts on Brexit and the possible implications for the construction industry – specifically relating to skills and expertise.
If there has been a consistent theme among all the headline stories of 2018, it’s that things need to change in almost every aspect of the construction industry, but most critically in terms of finances. The year started with lower construction output and new projects being slow to get off the ground.

While by mid-year the output was looking more positive, and the number of new contracts being awarded were increasing, profit margins in general were not.

**INDUSTRY PERFORMANCE**

The CN100 report, published in September, highlighted that increased turnover isn’t necessarily an indication of good financial health. Of the top 10 main contractors only 6 managed to post profits and even those were slim, with highest reported margins at 2.3%.

However, smaller contractors seem to be faring better, reporting average margins of 5% and above.

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*Source CN100 Report*

**POOR POLICY**

For the top tier contractors, reports of mismanagement, disproportionately big executive bonuses and poor payment policies have brought the industry sharp criticism.

Late payments and the retentions bill has come under the spotlight, further highlighting poor business practices that are having an adverse impact on the industry, and in particular smaller contractors and suppliers.
CARILLION COLLAPSE

The Carillion collapse highlighted major flaws in government outsourcing policies and tendering processes. Worse though, was the aftermath of Carillion – projects left undone and poorly done, and suppliers and subcontractors left unpaid.

Not to mention the thousands of people that suddenly found themselves out of work.

PROJECT DELAYS

Several high profile infrastructure projects have been delayed by a number of months adding significant costs to the budget.

The reasons cited may be valid, but the fact that the majority of projects fail to be completed on time or on budget is not inspiring much confidence from investors or for the industry as a whole.

HEALTH & SAFETY FAILURES

In 2017, following the Grenfell tragedy, there were several reports calling for a review of health and safety standards, both for workers and in terms of the materials and methods used for construction.

Yet even following the inquiries, it appears the industry has been slow to implement changes. On several major projects, main contractors have faced fines and prosecution following injuries that have occurred on site or evidence that incorrect materials have been used.

TECHNOLOGY ADOPTION SLOW

Technology promises greater efficiencies with innovative offerings being presented for better procurement and project management, as well as enhancing elements of engineering and health and safety.

But despite tender requirements including prerequisites for using BIM and the increased availability of other new technologies, the number of contractors investing in and adopting these new technologies are few, despite the obvious benefits being showcased.

GENDER PAY GAP

Lastly, but not least when the gender pay gap statistics were released, the construction industry was listed as one of the biggest offenders. Considering the massive skills shortage in the industry, soon to be compounded by the high number of skilled workers due to retire in the next decade and the migratory laws that may be imposed following Brexit, this doesn’t make sense. Yes change is needed.
PART 2 – WHO OR WHAT IS TO BLAME?

STORM FACTORS

If it was perhaps just one or two issues affecting construction, one might agree that things could turnaround of their own accord in time. But it is exactly this stance that has allowed the storm to brew.

Since the 2008 recession many tier one contractors have believed this to be true. The belief that volume can be the solution for low margins, the belief that bigger is better, the belief that things don’t necessarily need to change.

But if the Carillion collapse showed anything, it’s that ignoring change can lead to a hard fall that sends shockwaves through an already weakened industry.

Now with Brexit looming on the horizon, and a no-deal Brexit painting the storm clouds an even darker grey, industry leaders need to consider what that change needs to look like, and what the best ways are to go about implementing it?

In the light of all the industry happenings in 2018, many tier one top executives have come under fire, while others are proving that turnarounds can be achieved when one chooses to do things differently. This highlights the critical importance of having the right people at the top with the right skills and expertise to navigate troubled industry waters.

One of the few good things that’s come of the Carillion collapse is that it has highlighted the cracks in the industry and how legacy systems need to change. But several months down the line, is that change actually happening or is it all just talk?

RESPONDING TO THE COLLAPSE

Government’s response has been to hold inquiries, propose amendments to tender processes and suggest changes to legislation such as the retentions bill. There have been promises of funds being made available for housing and infrastructure as well as skills development, but if recent history is anything to go by, actually seeing the fulfillment of those promises in the near future is unlikely. Some of Carillion’s incomplete projects have become a burden for government and tax payers.

Private investors have walked away from projects due to the high costs of completing the project to the correct specifications, and because these are projects relating to public services such as hospitals, it’s been left to government to step in.

“’The world is changing very fast. Big will not beat small anymore. It will be the fast beating the slow.’”

– Rupert Murdoch

INDUSTRY REACTION

Within the industry there have been calls for greater collaboration, adoption of new technologies and changing outdated policies that are harming the industry – such as low cost bidding and late payments – to name a few.

But at a time where many main contractors are struggling with legacy projects that are draining
their coffers and at the same time feeling the pinch of smaller margins, are contractors even thinking of the bigger industry picture, or are they just focused on keeping their own heads above water?

While it’s easy in retrospect to point fingers at the Carillion executives for the poor decision making that eventually led to the collapse, the reality is that they weren’t the only tier one contractor engaged in the bad practices of lowest cost bidding or holding back payments to their supply chain. These have been standard industry practices for decades.

At times it appears it’s more important to be able to announce winning a high profile contract than actually having the capacity, resources, and expertise to actually deliver on those projects on time or on budget. Being able to do that has become the exception in the industry instead of the norm. It’s not a track record to be proud of.

**EXTERNAL FACTORS**

Granted there have been many external factors that have been beyond contractor’s control that have escalated project costs or caused lengthy delays.

But the question still needs to be asked: Is enough being done to mitigate these risks, or do executives simply shrug their shoulders? “It’s the construction industry, its normal, one can’t change or control it, and it’s going to happen.”

**KNOCK ON EFFECT OF BREXIT**

Perhaps it is precisely this attitude that is greatest cause for concern regarding Brexit. Here looms yet another external factor over which industry role players have very little control.

While there are voices shouting loudly from representatives of the industry, telling the UK government what the construction sector needs, Europe isn’t exactly listening, they have their own agenda to look after first.

So in the absence of being able to get the type of deal that the construction industry needs, what are contractors doing to mitigate the risks should a no-deal Brexit occur?

Already new provisions are being added to new tenders, insisting that bidders need to have a clear action plan to handle the fallout should a no-deal Brexit become a reality.

This is a good thing, it is sending a clear message: Be prepared and you will be able to make the most of future contract opportunities. Or sit back, hoping it never comes to that and face a future of escalating costs rendering projects undeliverable.
ADDED THREATS

To make matters worse, there’s currently a major skills shortage in the construction sector. While according to ONS data only 7% of skilled workers are from the EU, they represent the younger generation of expertise.

With 47% of UK construction workers set to retire in the next decade, where will the skills needed come from, if not from the EU?

To make matters worse, the construction sector is guilty of having one of the largest gender pay gaps and employing the fewest number of women in senior operational roles. Yes, change is long overdue and now could be exactly the right time to implement it.

“The greatest danger in times of turbulence is not the turbulence, it is to act with yesterday’s logic.” – Peter Drucker
There is a fair bit of debate as to why there is such a skills shortage in the construction industry. Some are of the belief that it comes down to the construction industry doing a poor job of marketing itself. The younger generation is looking for careers where they can be at the forefront of technology and innovation. They want flexible work environments and the opportunity for career progression and to collaborate with others so that they can broaden their expertise.

The construction industry offers all of that and more, yet it is not attracting people into the industry because other sectors such as finance, engineering and IT are doing a much better job at showcasing what their industries are about.

Construction is typically showcased as blue collar work, and there is certainly a shortage of labourers and skilled tradesmen, however, what is often overlooked is the many opportunities for professionals to crossover from other industries into construction, especially now with digital transformation causing an overlap of industry sectors. Commercial management offers any number opportunities for professionals from diverse backgrounds.

Many of the current industry leaders who hold a vast percentage of industry expertise are likely to retire in the next decade.

Questions are raised if enough has been done in terms of succession planning to ensure that their retirement doesn’t leave a gaping hole in the industry.

MOST NEEDED SKILLS

There is a shortage of labour in almost every skills level within construction, from site workers, through to tradesmen and senior executives.

Particularly within commercial management there is a great need for civil engineering skills as well as quantity surveyors and skilled project managers.

The infrastructure and utilities sectors of the construction industry are experiencing difficulty in finding the right people with the right level of experience to fulfill key roles. Rail, roadworks and heavy civils are particularly hard hit and top
candidates are often snapped up the minute they become available – unless of course they are headhunted first.

**SKILLS STIMULOUS**

In October 2018, parliament announced a budget of £20bn had been earmarked for skills development in the construction industry. In addition there have been amendments proposed to the apprenticeship levy which will allow the benefits to filter further down the supply chain.

While the funding is sorely needed, and the thinking behind changing the conditions of the apprenticeship levy is heading in the right direction, at this stage how exactly this will work out in practice is still to be seen.

There are industry organisations such as CITB that are making a concerted effort to grow the awareness of the construction industry in the UK and the career opportunities represented. In partnership with government and other industry role players, they actively work within the industry to provide the stimulus for skills development.

They also have a strong focus on technology and helping to develop the skills needed in construction for effective digital transformation.

There are ways in which contractors could support these industry efforts through collaboration on industry events and earmarking internal budgets to help develop skills in the industry.

Some contractors are using social media very effectively to showcase the projects they’re working on and generate more of an interest in the construction industry. All of these efforts, no matter how small can contribute to attracting more skilled workers into the construction industry.

**SKILLS SHORTAGE IMPACT**

What does the skills shortage mean for main contractors and delivery requirements that much harder.

Regardless of innovation and technology, workers remain the backbone of the industry. Even with using intelligent machinery that aims to make processes more efficient, people are still needed to oversee their operation.

Without the skills needed the construction industry may find itself operating under difficult circumstances, putting pressure on existing employees to work
harder, take on more responsibility and delivery more with fewer resources and manpower. This type of squeeze is costly. It’s when mistakes and accidents happen that can result in major setbacks in projects that come with an expensive price tag. Simply put, the skills shortage needs to be addressed now, before it becomes a crisis.

FILLING THE GAPS

In recent years, with the British economy performing marginally better than many of its European counterparts, there has been a migration of workers into the UK construction industry. This has been particularly successful as it has been the source of many skilled workers on all levels of the construction industry.

In particular, European tradesmen and artisans are well known for their craftsmanship, accuracy, and attention to detail. Technical knowledge of middle and upper management, gained through experience on the continent, has also proven invaluable. Europe has successful implemented many infrastructure projects that the UK can learn from.

In other words, in the past, the free movement of workers from the EU has provided a convenient source to fill the skills gap in the UK construction industry. And because of this there has not been a major push to develop local skills within the UK. Now if new immigration laws throttle the influx of European expertise, the UK construction industry will need to look to other sources to fill the skills gap.

One avenue is to transfer skills from other industries. As technologies are applied to more industry sectors this is a strong possibility. Workers trained in robotics, AI, VR and other emerging technologies can be used to customize and implement these technologies within the construction industry. Scanning and mapping drone technologies can be used to improve project accuracy and efficiency.

IT and business modelling expertise can also be incorporated to help improve procurement and planning phases of construction. Even top management skills from related sectors present an opportunity to bring in fresh perspectives that can improve the industry.

Studies show that greater diversity has a direct correlation to improved productivity and productivity. So whether it’s focusing on employing more women in the industry, or importing technical expertise from other industries, contractors need to start thinking outside of the box if they want to ensure that they have the skills needed to deliver on the projects they’ve fought hard to win.
Considering all the challenges that the construction industry is already facing, the uncertainties of Brexit are likely to add to the headaches. It is not just the skills or labour force that may be impacted by new immigration laws.

Almost every aspect of the construction industry is likely to be hindered in some way when Britain exits the European Union. For more than a decade the UK has enjoyed free trade and free movement of people and materials across European borders.

Now while there are still many unknowns regarding Brexit, the only certainty at this stage is that all of that is going to change. In what way and by how much, is yet to be determined.

ON TIME DELIVERY

Currently the majority of the industry is hard pressed to deliver projects on time, even with all the benefits of Brexit.

Now as new trade regulations come into play, project delays will be unavoidable unless main contractors take specific steps to mitigate the risks.

Contractors will find themselves navigating significantly more red tape as part of their supply chain and may have to employ specific customs expertise as well as invest in additional software to manage this effectively.

While the initial thought is that these are simply added administration tasks and expenses, there is an upside to consider. Making improvements in managing the supply chain could not only help contractors mitigate the risks of Brexit, they could also highlight multiple areas for improvement that could result in achieving the elusive on time delivery.

ON BUDGET DELIVERY

Achieving on budget delivery appears to be even more challenging than on time delivery. Because traditionally the construction industry is plagued by lowest cost bidding, many tenders are won on the slimmest of margins.

This leaves no room for maneuvering when engineering specifications change or when material costs escalate more than initially projected. How much more will trade tariffs,
customs and import duties add to project costs?

Industry leaders have been making various attempts to project more accurate costs when bidding with some executives claiming that they would rather walk away from deals that will not be beneficial for the business in the long term.

British skills are in short supply in the UK construction industry. Bottom line is that finding the right people, especially at a senior level is going to cost more.

It’s going to cost more because those that have the skills can afford to be choosy and demand higher salaries with added benefits. If an organization is not willing to pay what they’re asking, one can be almost certain competitors will.

Even if one chooses to go the route of importing EU expertise - that too is going to cost more. Not only in terms of the salary expectations and recruitment costs but also in terms of relocation expenses and visa costs.

To retain existing EU employees may require additional legal expertise to ensure that they are now compliant with new immigration laws. Once again the result is more time consuming administration and added costs.

HIRE LOCAL?

While in an ideal world the skills needed would be locally available, the reality is that

Now as material and operational costs are set to increase as a result of Brexit, business development managers will have their work cut out, demonstrating sufficient value in their offering to get the buy in of clients and investors.

MARKET SHRINKAGE

While the majority of UK contractors have a local client base and tender exclusively on local projects, there has up until now been the opportunity to bid for tenders or enter joint ventures beyond UK borders. This has been facilitated by the free trade marketplace within the EU and many contractors have taken advantage of this.

Projects that are mid phase could be in jeopardy if there are no clear plans to mitigate the risks as new regulations come into play.

Additionally, accessing new international opportunities will become harder, meaning that the focus will return to the local marketplace where the competition is already tough.

As contractors scramble to gain a larger piece of the pie, there will be the temptation to enter into lowest cost bidding just to gain ground in the marketplace.

It’s a double edged sword. One that could not only harm the
contractors that engage in these practices but also the industry as a whole. Have we learnt nothing from Carillion? 

INDUSTRY RESPONSE:

While there is a great deal of talk regarding Brexit and the associated risks, it’s difficult to determine at this stage if the industry is in fact taking the appropriate steps to prepare themselves.

Those contractors adopting a “wait and see” approach may find themselves facing escalating expenses that will quickly eradicate what little margins they have.

“Do not let what you cannot do interfere with what you can do.”

– John Wooden

Granted, it’s not easy to plan for risks that are not yet defined. But at this stage with the outlook appearing to be relatively gloomy, the best probable course of action is to plan for the worst case scenario – a no-deal Brexit. And the imposition of trade and labour regulations that will represent a major hindrance to the construction industry.

At best there may be moderate import tariffs on materials and some delays in the supply chain. Retaining top European talent may require jumping through a few hoops and finding local skilled workers will require extra effort.

A proactive approach, taking into consideration all the possible risks will not only protect the business, it may also attract new business.

Already tenders are being advertised containing a provision that bidders include a clear plan for navigating a no-deal Brexit scenario. Clients are wary, and they won’t be willing to accept additional project costs and delays just because contractors have not adequately planned for possible risks.

One thing is certain though – the quality of people employed and their ability to make the right decisions amid difficult circumstances will make all the difference in how main contractors will be able to weather the oncoming storm.

“Do not let what you cannot do interfere with what you can do.”

– John Wooden
Adopting a wait and see approach to Brexit, is akin to battening down the hatches and attempting to ride out the storm. But with this approach there is a strong possibility that when the storm has passed, contractors will find themselves adrift with a broken mast, no power banks, and a disabled or injured crew. That is, if the storm doesn’t sink them – which is a strong possibility.

PLAN & COMMUNICATE

Regardless of the unknowns, the only real choice that main contractors have is to start preparing a plan to mitigate the risks of Brexit, taking into consideration worst case scenarios.

A task force made up of divisional heads and their 2IC’s would be best positioned to provide insights, identifying areas of the operation that could be most impacted. Feeding this information into a central database would enable analysts to identify which are the most critical risks and then be able to calculate the impacts in terms of cost and project delivery. This information could then be feedback to relevant departments so that they could start implementing changes to mitigate the risks. The information could also be integrated into costing structures and project plans to support more accurate future bids.

It is quite likely that some operational structures and processes will need to change. And part of this process will involve training employees on the new policies and structures. There’s little doubt that the uncertainties of Brexit will cause employees to be nervous, making them wonder about how secure their jobs really are.

Few things are more important during a change event than communication from leaders who can paint a clear and confidence-inspiring vision of the future.

– Sarah Clayton

It’s been proven to be more cost effective to retain good employees than to have to replace them. If main contractors want to keep their
best people, there needs to be clear communication as to what is changing, why it’s changing and what the impacts will be to employee roles.

When employees have a sense of security it frees them up to focus on their daily tasks and more pressing matters such as preparing for Brexit risks.

### DRIVE CHANGE

Some of the most ground breaking innovations are born out of trying times and Brexit could represent just such an opportunity.

If financial reports are anything to go by there is a great deal of room for improvement in organizational policies and operations for Main Contractors. Why not use Brexit as an opportunity to implement changes that will drive organizational improvement.

Change of any kind is generally met with differing levels of resistance. But with the potential negative implications of Brexit for all areas of organisations, making the case for change will not be difficult and neither will getting the buy in from employees once they understand the risks of not implementing change. After all their jobs are at stake if inaction causes the business to flounder.

Even if the projected risks don’t materialize, the business will be stronger and perform better having implemented positive changes.

### STAY CONNECTED

No main contractor is going to be able to avoid the implications of Brexit. Keeping informed of the latest developments and ensuring that the business is represented in industry organisations will all contribute to being better prepared.

Industry organisations potentially have the ear of government and can raise their voice airing industry concerns. How much actual impact this will have on negotiations is debatable, but government is currently the only one in the driving seat and a collective voice is certainly more audible.

There is also an opportunity for collaboration and to learn from joint venture partners and even competitors. Understanding industry best practice and being able to see how other companies implement this effectively can create the impetus needed to drive change.

### HARNESSING TECHNOLOGY

Already technology has provided a number of tools to improve processes and operational
efficiency, yet industry wide adoption rates remain low. Possible reasons for this could be three-fold.

Firstly technology costs, and while it is becoming cheaper as economies of scale ramp up, it still requires a sizeable investment. While the long term returns may make the case for investment, in the short term, while companies are feeling the pressure of losses or, at best, scraping by on minute margins, it’s a hard sell.

Secondly, there are a great number of different programs and technologies promising fairly similar benefits. The challenge is that to be most effective, main contractors need their clients, suppliers and sub-contractors to use the same software or technology. This is very difficult to achieve because businesses will buy what meets their immediate needs before taking into consideration what may be important for others.

The third reason adoption may be slow, is that a lot of technology is still in the testing phase and will take some time for commercial release. In the meantime business needs are changing and technology is evolving. Finding the common point where all these needs meet is yet another challenge.

Business leaders have the difficult task of not only discerning what technology is right for the business today, it needs to be fit for purpose taking into account future business needs as well. When there are major unknowns such as Brexit looming on the horizon, this makes decisions even harder.

Having said this, technology is driving change and businesses that do not engage in digital transformation will find it difficult to remain competitive in the marketplace of the future. Having the right skills in place to be able to drive digital transformation is going to become a critical success factor.

If the skills are not available within the construction sector, there’s no reason they can’t be imported from other industries, provided the technology can be applied to the construction industry. In fact, this type of expertise may well give organisations a competitive edge, by being able to use technology to demonstrate greater value to potential clients, and winning contracts in the process.

**PROGRESSIVE LEADERSHIP**

Navigating these troubled waters is going to take strong and visionary leadership. One of the critical factors of surviving Brexit is going to be an organisation’s ability to respond quickly to developments and risks as they arise.

“Companies that change may survive, but companies that transform thrive. Change brings incremental or small-scale adaptations, while transformation brings great improvements that ripple through the future of an organization.

— Nick Candit

Leaders need to be empowered to be able to make these decisions for change quickly and this will only happen if they have the trust of shareholders and the support of their management teams.

Realistically, if at this point in time leaders do not already have that support, then organisations need to consider if they really have the right senior people in place. And if not, could now possibly be the time to bring in stronger leadership with a track record that does inspire confidence?”
CONCLUSION:

Trying to plan for unknown risks that could have far-reaching implications when one is already struggling to keep one’s head above water is no small feat. Yet this is exactly what is being demanded of the UK construction industry.

Already troubled by major industry failures and being plagued by rising costs and project delays, the coming months are going to determine which companies will sink or swim.

The companies that will survive will be those with strong leadership at the helm, not afraid to make difficult decisions to ensure the organisation gets through the transition.

Companies that will thrive will be those that are proactive in their approach to Brexit and aim to transition early, adopting technologies to facilitate this and ensuring that they have the right people with the right skills in key positions that can drive the change.

It is visionary leaders that will be able to future-proof businesses by surrounding themselves with highly skilled management teams and using technology to their advantage.

With so many uncertainties on the horizon, one of the best investments organisations can make at this time is in their human resources to ensure that they have the right people with the right skills to get the job done at this critical time.

There is little margin for error and people are the assets that can make a significant difference in how successful the business is in navigating the changes that are to come.

While technology may provide the tools, it is human insights, expertise and decision making abilities that will have the most impact on an organisation’s performance in the year ahead.

If you feel the need to have the conversation with a recruitment partner to determine if your organization has, in fact, the right people in place, or if you can already identify gaps that you know can only be filled with the top talent in the industry, then talk to us at Ellis Fox.

We know the industry and can work with you to uncover your true recruitment needs.

Contact us via email at team@ellisfox.co.uk or call us on Tel: 020 7183 0255.