



A Preliminary Construction Forecast for 2009

prepared for

**Department of the
Environment, Heritage and
Local Government**

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TABLE OF CONTENTS

Section 1	Introduction	1
------------------	---------------------	----------

Section 2	The Irish economy: review 2008 and outlook 2009	2
------------------	--------------------------------------------------------	----------

Section 3	Construction in 2009 - A preliminary assessment	7
------------------	--------------------------------------------------------	----------

Section 1: Introduction

This paper is one in a suite of economic assessments of the construction industry commissioned annually by the Department of Environment, Heritage and Local Government (DEHLG)¹, namely:

- A *Preliminary Forecast for Construction* which gives an indication of construction trends for the current year.
- The *Annual Construction Industry Review and Outlook (CIRO)* which reports on the outturn for the industry in the preceding year and provides a detailed assessment of the prospects for the current year and the medium term (looking forward 2-3 years).²
- *Quarterly Construction Indicators* which track current trends in the industry on an ongoing basis.³

This preliminary forecast for the year is set out as follows:

Section 2 presents the provisional outturn for the economy in 2008 and considers the outlook for the Irish economy in 2009.

Section 3 considers recent data on the Irish construction sector and assesses the prospects for the construction sector in 2009. It takes into account expected developments in the macroeconomy, information available from the April 2009 Budget, including the Exchequer and Public Capital Programme provisions, and recent data and trends in the non-residential sector. It concludes with a preliminary forecast for the volume of construction output in the main sub-sectors of construction in 2009. A more detailed medium-term forecast will be presented in the Department's *Annual Construction Industry Review and Outlook (CIRO)* later in the year.

¹ This suite of reports is produced by DKM Economic Consultants who were given editorial independence by the DEHLG to prepare their views, analysis, forecasts and economic commentary on data and statistical trends in the construction sector. The views expressed herein are DKM views and do not necessarily reflect the views of the Department.

² Latest available at

<http://www.environ.ie/en/Publications/StatisticsandRegularPublications/ConstructionIndustryStatistics/>

³ Latest available at

<http://www.environ.ie/en/Publications/StatisticsandRegularPublications/ConstructionIndustryStatistics/>

Section 2: The Irish Economy - Review 2008 and Outlook 2009

2.1: Irish economy 2008 - review

The Irish economy's difficulties, which commenced with a declining housing market at the end of 2006, were further compounded by rising interest rates between December 2006 and July 2008, tighter lending and credit conditions, combined with falling external demand (particularly from the US and Europe), an appreciating currency and a cautious Irish banking system.

The Minister for Finance in his 2009 Budget speech on 14th October 2008⁴ referred to the "changed economic realities" which had unfolded at a considerable pace over the previous few months, both globally and domestically. On the global front, he was referring to the sub-prime crisis in the US, which led to the ensuing turmoil in financial markets, global housing market downturns and soaring commodity prices. At home, the domestic economic situation was further damaged by a host of negative economic indicators, not least of which has been the sharp deterioration in the public finances over the past twelve months.

Even though Government stepped in to guarantee bank deposits in September 2008, the global financial crisis led to tighter credit conditions which resulted in less scope for consumers and businesses to borrow over the past six months. The subsequent bank recapitalisation and the recent measures announced in the April Supplementary Budget to address the issue of asset quality in the banking system, including the establishment of the National Asset Management Agency (NAMA) are intended to alleviate the credit situation for consumers and businesses and restore a supply of credit to the real economy. It remains to be seen what the full impact of such Government interventions will be. However in the meantime the continued lack of confidence amongst consumers and businesses has led to a further weakening in economic activity over recent months.

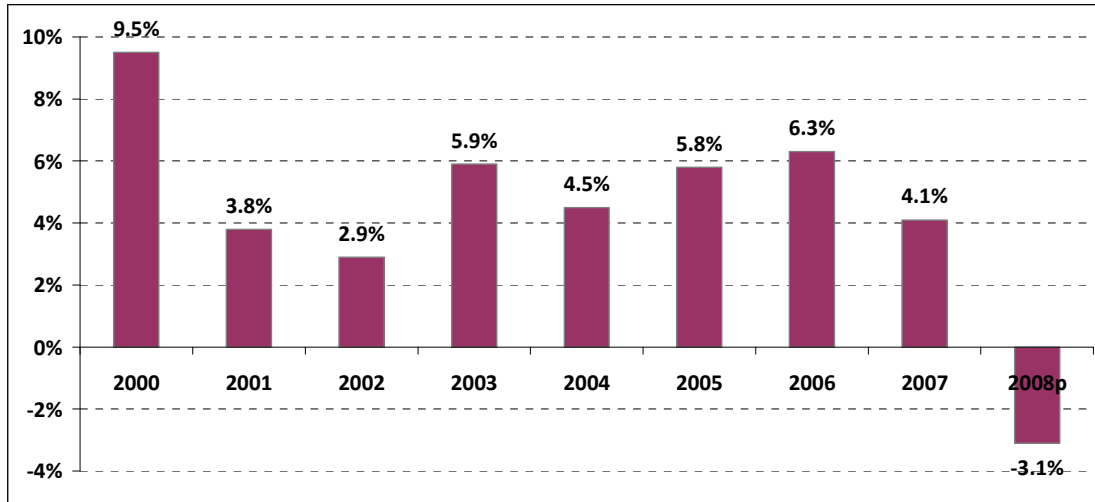
Economy remains in an extremely weak position

Looking at the most recent trends in economic growth⁵, National Accounts data confirmed that the economy contracted in 2008, with average GNP down 3.1% in volume terms compared with 2007. The corresponding decline in GDP was -2.3% in 2008. This was the first contraction in economic activity since 1983 and confirmed that the economy entered recession during 2008.

⁴ The 2009 Budget was brought forward by two months due to the unfavourable economic circumstances which had unfolded over the preceding few months.

⁵ Quarterly National Accounts, CSO, 26th March 2009.

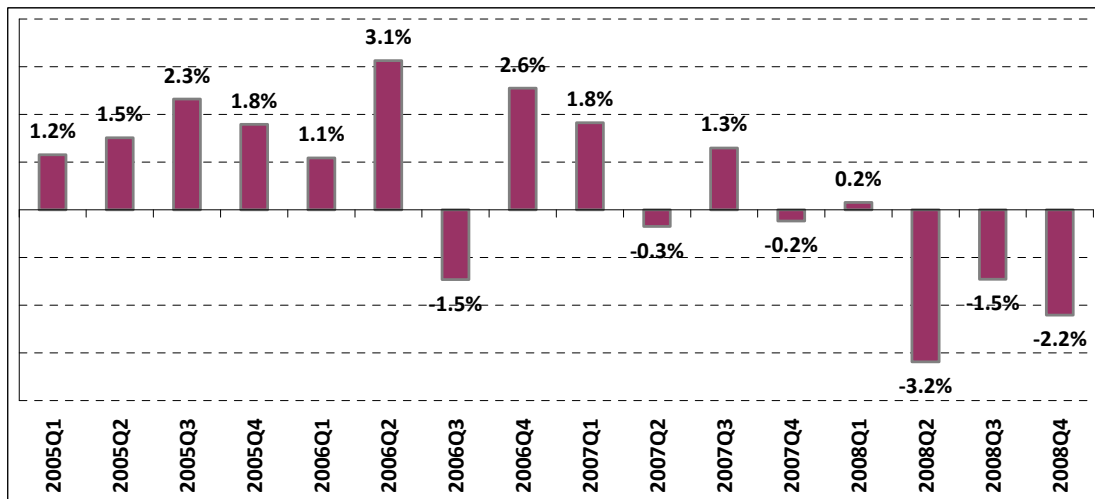
Figure 2.1: Real GNP % Growth 2000-2008p



Source: CSO National Accounts.

Looking at the quarterly seasonally adjusted movements in GNP volumes reveals an economy in which the volume of output peaked in Q3 2007 and was almost unchanged until Q1 2008. The economy weakened considerably thereafter, culminating in three successive quarters of negative growth, or a contraction of almost 7% (seasonally adjusted) in volume terms between Q3 2007 and Q4 2008. By the end of 2008, the quarterly volume of GNP had fallen back to levels which prevailed in Q1 2006.

Figure 2.2: Quarterly GNP Volumes
(quarterly % change using seasonally adjusted data)



Source: CSO

Sharp deterioration in fiscal position

The deteriorating economic situation is having a significant adverse impact on the Exchequer finances. The most recent figures relate to the first four months of the year and showed total tax receipts down by 24% on the same period in 2008. After spending of almost €19 billion in the same period, the Exchequer deficit widened to €7.3 billion. For the full year, the 2009 tax take is projected to be down by 16% on 2008, implying some improvement in tax revenues over the coming months.

In an effort to address the widening deficit, the Government has announced a series of measures over the past year to restore order to the public finances:

- In July 2008, it introduced a range of measures worth €440m in 2008 and €1bn in 2009.
- The Budget last October delivered a range of revenue raising measures worth almost €2bn.
- In January this year further savings were announced which are expected to raise €2bn.
- In February the introduction of a pension levy for public servants was a key element in the total savings package announced of €2bn.
- In the April Supplementary Budget, an additional €1.8bn was raised over the remainder of 2009 from additional tax revenue (€1bn.) and €0.8bn from changes in PRSI and the Health Levy. Expenditure reductions of €886m in gross current expenditure and €576m in capital expenditure were also announced, generating a total package of savings equivalent to €3.3bn.

Despite the above measures, the General Government Balance (GGB) is forecast at €18.41bn or 10.75% of GDP. The recent report from the European Commission⁶ forecast that Ireland's GGB would reach 12% of GDP by the end of 2009 - in line with the ESRI projection last month - the highest in the Euro area.

The Budget contained a multi-annual plan to address the deficit, setting out further revenue raising and expenditure saving measures over the period to 2013. The overall Budgetary projection, according to the Department of Finance, sees the GGB reducing to -€5.9bn or -3% of GDP by 2013.

Table 2.1: Budgetary Projections, April 2009

	2009	2010	2011	2012	2013
General Government Balance (€m.)	- 18,413	-18,088	-14,959	-10,377	-5,929
% of GDP	10.75%	10.75%	8.5%	5.5%	3.0%

Source: Supplementary Budget, April 2009, Department of Finance.

⁶ Available at: http://ec.europa.eu/economy_finance/publications/publication15048_en.pdf

The Budget also published the Exchequer capital allocations for the period 2009-2013 which further reduced the capital allocations announced in the October Budget. The details for 2009 are set out in Section 3⁷.

Weak economic data the norm in recent months

Unemployment is on the rise, having reached 7.7% in Q4 2008 (September-November 2008) and is expected to climb towards 14% by the end of 2009. Using the Live Register measure suggests that the unemployment rate has already hit 11.4% in April. Much will depend, in terms of the forecast unemployment rate, on the prospects for outward migration and the extent of non-nationals who choose to return home, but there is no doubt that the unemployment level will increase in absolute terms by the end of 2009.

Confidence readings amongst consumers have been exceptionally low since mid-2008, despite a slight pick up in April, according to the IIB/ESRI Consumer Sentiment Index. Moreover, statistics on the volume of retail sales recorded a decline of almost 24% in the first two months of the year on the same period last year.

The weak confidence amongst consumers is also evident in the business sector, where investment levels are contracting by around 30% per annum.

Recession produces negative inflation and lower interest rates

Two positive developments over recent months have been the sharp fall in consumer price inflation and interest rates, which should support economic activity in a normal economic cycle. The monthly consumer price inflation index has been falling since October 2008, with annual inflation at -2.6% in March 2009. This is providing some relief for those whose incomes have been cut due to the recession and the taxation rises in the Budget. However, despite the recent reduction in Eurozone interest rates to just 1% on 7th May from 4.25% last October, confidence levels amongst consumers and investors remain severely damaged as a result of their weak assessment of the general economic conditions.

2.2: Outlook for 2009

The sharp deterioration in economic conditions over the past six months has led to forecasts for the Irish economy being revised substantially downwards to within the range of -7% to -9%, compared with consensus forecasts for 2009 last October of around +2%⁸.

Last October, the 2009 Budget was framed against a GNP growth rate of -1% in 2009. In January, this was revised down to -4%. Early in March, the Governor of the Central Bank forecast that the economy would contract by 6% at least. A day later, the Taoiseach put the figure at -6.5%. Independent economists subsequently forecast that GNP would contract by 8% this year. In the

⁷ The 2009 *Construction Industry Review and Outlook* (CIRO) will explore in detail the prospects for publicly funded construction projects over the medium-term.

⁸ The average GNP forecast for the Irish economy in DKM's November 2008 edition of the *Economy Watch* was 2.1% for 2009. Available at www.dkm.ie

April Supplementary Budget the Department of Finance projected a contraction in GNP of -8% this year followed by -2.8% in 2010, with the majority of risks alleged to be on the downside. The most recent forecast from the European Commission this week predicts that the Irish economy will contract by 9% this year in GDP terms, which is worse than the ESRI forecast issued the previous week of a contraction of 8.3% in the volume of GDP this year.

Table 2.2 sets out macroeconomic projections for 2009 from four official sources, with the preliminary outturn for 2008.

Table 2.2: Macroeconomic Forecasts for the Irish Economy in 2009						
	GDP	GNP	Consumer Expenditure	Fixed Investment	<i>of which Build. & Const.</i>	CPI Inflation
	%	%	%	%	%	%
2008 (preliminary)	-2.3	-3.1	-0.8	-19.9	-1.2	4.1
2008 Projections						
Dept of Finance (April 2009)	-7.7	-8.0	-7.8	-27.0	N/A	-3.9
Central Bank (Q2 2009)	-6.9	-7.1	-5.0	-32.5	-35.3	-4.0
ESRI (Spring 2009)	-8.3	-9.2	-7.0	-31.2	-34.5	-4.6
European Commission (May 2009)	-9.0	N/A	-7.9	-29.2	N/A	-3.9

The Department of Finance forecasts were presented with the April 2009 Supplementary Budget.

Sources: 2008 represents outturn data are per CSO Quarterly National Accounts Quarter 4 2008 and Year 2008 (Preliminary).

2.3: Conclusions

The Irish economy remains in an extremely weak position with most risks on the downside. There is little scope to see any recovery yet in domestic demand as reduced disposable incomes, further job losses and fiscal retrenchment continue to dampen economic activity, despite the fall in inflation. The further contraction of investment in 2009 is another factor prolonging the recession this year. On the traded side, much will depend on international economic developments, but at present the prospects are for a marked decrease in export volumes this year which drags down the level of GNP. However, with imports projected to be weaker, due to the lower domestic demand, the external sector makes some contribution to growth this year. Meanwhile consumer and investor confidence levels are likely to remain in weak territory for some months to come. The role of NAMA in restoring confidence cannot be underestimated and much will depend on how the new agency evolves over the coming weeks as it is established.

Section 3: Construction in 2009 - A Preliminary Assessment

3.1: Construction performance in 2008

The only measure of total construction investment in the economy is available from the CSO National Accounts. Estimates for 2008, published 26th March 2009, confirmed the sharp contraction in construction investment during 2008. Following the modest decline reported in 2007 (-1.9%), the decline gathered momentum during 2008, culminating in a contraction in construction output volumes of 20%⁹. While new residential construction output declined for the second year in a row, the volume of other new building and construction declined for the first time since 2003. The only sub-sector still growing was the renovation sector, where growth accelerated in 2008 compared with 2007.

The value of construction investment was €30.4bn last year or €28.6bn when transfer costs are excluded. Thus construction, which accounted for almost 25% or one-quarter of all economic activity at the peak in 2006 had fallen to 19.4% of GNP by the end of 2008. The prospects for 2009 are set out later in Table 3.7 which shows that the industry is expected to shrink much further by the end of the year.

Table 3.1: Latest National Accounts Fixed Investment Data: 2006-2008p

2008p Current Prices €m.		2006	2007	2008p	2006	2007	2008p
		Constant 2006 Prices €m			volume % changes		
38,289	Gross Fixed Capital Formation <i>of which</i>	47,632	48,203	38,600	4.0%	1.2%	-19.9%
30,351 19.4%	Building and Construction B&C as % of GNP *	37,967	37,235	29,800	6.0%	-1.9%	-20.0% 19.4%
28,601	B&C excluding Transfer Costs	33,799	33,863	27,970	5.0%	0.2%	-17.4%

P = preliminary. * based on current prices.

Source: CSO

Taking the value added concept of measuring output, which is the difference between the value of gross output and the cost of materials or intermediate inputs, construction output represented

⁹ This figure includes transfer costs, which include all transactions taxes associated with the transfer of land and buildings. When the latter are excluded the rate of decline was -17.4% in 2008.

10.4% of GNP at the peak in 2006 as opposed to 24.9% of GNP using the investment measure set out in Table 3.1. This value added measure excludes the value added by building material suppliers (included under manufacturing) to the construction industry as well as the value added by firms providing services to the construction industry (included under other services). Both elements, plus the value of imports for the construction sector, would be included in the 'gross' investment measure in Table 3.1. The 2008 GVA measure for construction shows that the construction industry, in value added terms, represented just 8.7% of GNP in 2008 compared with 26.6% for manufacturing industry.

3.2: The current situation

Construction confidence at an all time low

The current economic situation is severely impacting on an already very weak construction sector. Confidence in the sector is at an all time low as new business continues to weaken, the pace of employment losses accelerates and companies remain pessimistic about the future outlook. The Ulster Bank Construction Purchasing Managers' Index (PMI) - a seasonally adjusted index designed to measure the overall performance of the construction economy - recorded a further considerable deterioration in operating conditions in April. Employment declined substantially, while the falls in activity and new business remained sharp. Although the index reading rose slightly in the month of April (to 32.9), it remained well below the no-change mark of 50 that divides expansion from contraction.

Direct employment already down almost 40% from the peak

According to the QNHS, the numbers directly employed in construction had already fallen by 52,400 in Q4 2008¹⁰ (Sep-Nov quarter) to 233,800 persons from the peak recorded in Q2 2007 (March-May 2007) or by almost 20%. Over the last four months, there have been further significant increases in the numbers becoming unemployed in construction as indicated by the Live Register performance. The total on the Live Register reached 388,600 (seasonally adjusted) in April 2009, up 94% from a year earlier. Construction related job losses continued to dominate the Live Register increase with males accounting for almost 70% of the total increase of 188,800 in the Live Register over the past twelve months. If an estimated 65% of the 89,800 males who joined the Live Register since October 2008 had previously worked in construction, this would imply a further 58,370 workers became unemployed between October 2008 and April 2009, bringing the total jobs lost in construction to around 110,770 since the peak in Q2 2007. This would imply that the total number of persons directly employed in construction at the end of April was only 175,430, 39% below the peak in Q2 2007.

¹⁰ The latest data (seasonally adjusted) available published in February 2009. At that time 84% of all construction workers were Irish citizens, and 16% were from the EU Accession States.

Table 3.2: Estimated Job losses in construction

<i>(Seasonally adjusted data)</i>		Direct	Indirect	Total
		<i>Numbers employed</i>		
Peak Q2 2007	Mar-May'07	286,200	114,480	400,680
Q4 2007	Sep-Nov'07	279,300	111,720	391,020
Q4 2008	Sep-Nov'08	233,800	93,520	327,320
Current estimate	April-09	175,430	70,172	245,602
Forecasts y/e Dec 2009		150,000	60,000	210,000
Relative to peak:				
Total jobs lost by Q4 2008		-52,400	-20,960	-73,360
total jobs lost by end 2009 (est)		-136,200	-54,480	-190,680

Source: QNHS from CSO and DKM estimates

While the current employment estimate is based on the Live Register and suggests unprecedented job losses over the past twelve months, the forecast is for direct construction employment to fall to 150,000 by the end of 2009.

When indirect employment is included, which captures the employment generated by firms that provide the materials for construction projects, the total number of persons employed at the peak was around 400,000. That figure is projected to almost half by the end of 2009.

Private construction activity weakening

The prospects for private construction output are equally disappointing, as private sector activity appears to have slowed significantly. We understand, despite the rescue package announced for banks, that the lack of finance is the primary reason for the delay/postponement of projects by the private sector.

Thus the prospects for private non-residential building will be extremely weak over the next two years leading to a severe contraction in construction output. This will have serious consequences for construction employment and wider economic activity as well as for the Exchequer finances. It will ultimately result in a deeper and longer economic recession.

Other options for funding public infrastructure projects

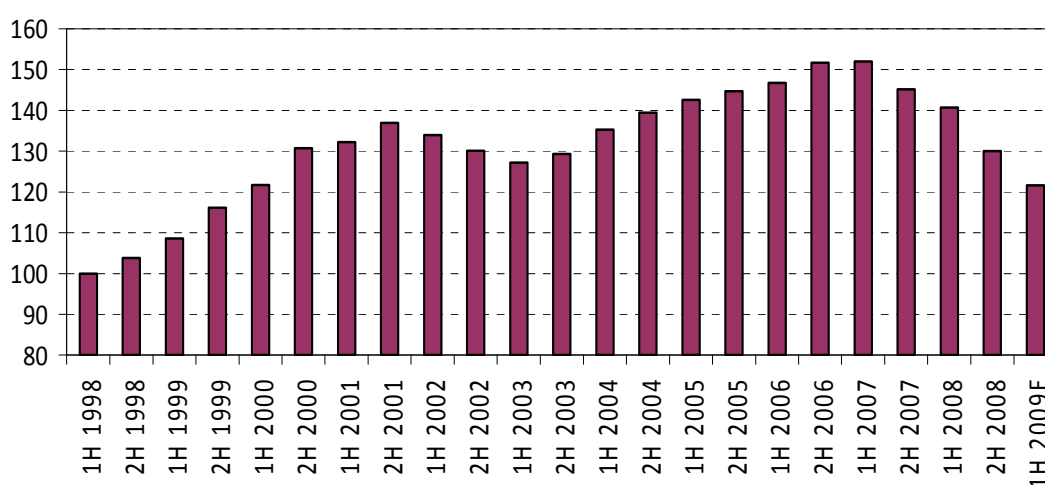
The Minister for Finance did, however, refer to other options to fund infrastructure which are being examined by the Department of Finance. In particular he referred to the following: 1) raising funds from the pension industry, 2) the disposal of assets, 3) sale and leaseback arrangements, 4) franchising arrangements and 5) the proposal from ICTU for a National Recovery Bond. The hope is that there will be some positive news over the coming months which provide more funds for infrastructure over and above those provided for in the Budget. In the absence of such funding initiatives, the prospects for construction activity are exceptionally weak over the next few years.

The best value for money available in ten years

The current contraction in construction output has generated the best value for money that has been available for a decade. The contraction in new orders and the acceleration in job losses have generated considerable competition for the work that is put out to tender. This is evident from the recent trend in tender prices from other sources as well as the SCS.

The next chart displays trends in the Tender Price Index according to the Society of Chartered Surveyors. The data suggests that tender prices are back to levels recorded at the end of the last decade.

Figure 3.1: Trends in Tender Price Index
Index 1H 1998 = 1000



Source: Society of Chartered Surveyors

The next Table shows the dramatic decline in tender prices during 2008, which is expected to continue at a more moderate rate in 2009.

Table 3.3: Recent trends in tender prices for general contracting work*

	2007	2008	2009E	Cumulative 2007-2009
Society of Chartered Surveyors (SCS)	-4.3%	-10.5%	-5.0%	-18.6%
Bruce Shaw	0.0%	-12.0%	-5.0%	-16.4%
Davis Langdon PKS	-1.0%	-13.5%	-4.0%	-17.8%
Average	-1.8%	-12.0%	-4.7%	-17.6%

* % change year to December.

The latest Tender Price Index from the SCS shows that tender prices fell by 7.6% between June and December 2008, and by 10.5% over the full year to December 2008. The most recent Annual Reviews from Bruce Shaw and Davis Langdon PKS estimate that tender prices fell by between 12% and 13.5% in 2008, although in some cases declines of over 20% were recorded. The likelihood is that tender prices from 2007 will be down 20% by the end of 2009.

The fall in tender prices partly reflects the moderation in the cost of labour and material inputs as follows.

- In regard to construction earnings, average earnings in the construction sector increased by only 1.2% on average in 2008, down from 5.8% in 2007.
- Building materials inflation, on average, was 3.9% in 2008 compared with 5.3% in 2007, but prices starting falling in February and recorded an annual decline of 2.4% in March.
- The composite index of labour and building materials costs, the Capital Goods Price index, increased by 3.7% in 2008 compared with 4.6% in 2006. The latest figure for February shows that the annual rate started to decline in February and had reached -1.4% in March 2009.
- Construction costs, according to the SCS Construction Cost Index, increased by 3.9% in 2008 compared with 4.5% in 2007, but were unchanged in February 2009 compared with February 2008.

The expectation is that there will be further reductions in construction earnings and building material prices over the remainder of the year as the reduced volume of work available and further job losses result in even keener pricing amongst contractors. However, by the end of 2009 tender prices will have fallen for three successive years by close to 20% on average¹¹ and the scope for cutting prices further in 2010 may be limited, unless there is a marked reduction in costs.

We consider the prospects for 2009 in the next Section.

¹¹ Tender prices for building projects in a number of instances are reported to have fallen by substantially more than the average.

3.3: Prospects for Sub-Sectors of Construction

3.3.1: Housing

Indicators display a market in free-fall

Whichever housing indicator one looks at, it is clear that all of them portray a housing market in decline from unprecedented activity levels recorded at the peak. Table 3.4 summarises recent trends in key housing indicators as published.

Table 3.4: Recent trends in key housing indicators

	2006	2007	2008	2009 data to date	2008/2007 % change	2009/2008 Yr to date % change
Planning permissions:	78,755	84,397	67,584	N/A	-20%	
Houses	60,008	62,828	47,806		-24%	
<i>of which</i>						
- Multi-unit developments	40,851	44,273	33,052		-25%	
- One-off houses	19,157	18,555	14,754		-20%	
Apartments	18,747	21,569	19,778		-8%	
Total commencements	75,602	48,876	22,852	752	-53%	-72%
<i>of which</i>						
Single units	17,412	15,757	10,856	592	-31%	-44%
Total registrations:	66,649	38,351	12,676	1,166	-67%	-73%
<i>of which</i>						
Houses (est)	47,473	27,667	9,145		-67%	
Apartments (est)	19,176	10,684	3,531		-67%	
Total completions:	88,219	78,027	51,724	5,272	-34%	-47%
<i>of which:</i>						
Individual houses	21,531	19,663	17,386	2,111	-12%	
Scheme houses	47,457	39,273	21,127	1,856	-46%	
Apartments	<u>18,831</u>	<u>18,691</u>	<u>12,811</u>	<u>1,305</u>	<u>-31%</u>	
Total	87,819	77,627	51,324	5,272	-34%	
Difference (1)	400	400	400		0%	
Number of loans	110,790	84,194	53,616		-36%	
<i>of which</i>						
First-time buyer	37,064	30,469	19,946		-35%	
Mover purchaser	45,585	32,864	20,444		-38%	
Residential investor	28,141	20,861	13,226		-37%	
Average house price (€)	299,130	301,768	273,355	253,546	-9%	-10%

2009 figure for commencements is for January only.

2009 figure for completions is for first two months.

2009 figure for registrations is for three two months.

2009 figure for average house price is for March, based on permanent-tsb/ESRI data.

Source: Department of the Environment, Heritage and Local Government, CSO, Irish Banking Federation, Permanent-tsb/ESRI house price index.

1) The difference relates to 400 conversions which are included in the completions figures each year.

The extent of the decline in housing activity was evident at the end of 2008 when the number of commencements reported was down by 53% on the previous year, the number of registrations was down by 67% and both the numbers of completions and mortgage loans associated with a property transaction were down by 34% and 36% respectively. Although also down, the number of planning permissions recorded a much lower decline at 20% while average house prices fell by 9%, although in a number of instances house prices fell well below the average.

The data excludes the build up of unsold new stock, estimated at around 35,000 by the Construction Industry Federation (CIF) during 2008. This may suggest that a proportion of the 51,724 units connected for electricity in 2008 - the basis for recording completed units - were actually built in previous years.

There is limited data available for 2009 so far but the trends suggest that activity level continued to decline in the opening months, with the number of registrations down 73% in the first quarter and total completions down by 47% in the first two months. Again the latter figure relates to units connected for electricity and we suspect the total number includes some houses which were waiting to be sold at the end of 2008. These rates of decline should moderate throughout the year as the second half performance in respect of most indicators was weaker in 2008 than the first half.

The conditions in the market reflect very weak consumer sentiment as potential house buyers have been holding back due to concerns about their jobs and the general economic situation. Consumers perceive that it is not a good time to make major purchases despite the very favourable reductions in house prices and mortgage rates to date. Thus although housing affordability has improved substantially since the house price peak in early 2007, many potential purchasers expect further house price falls over the coming months. Average house prices, according to the permanent-tsb/ESRI index, were down by 18.5% in March 2009 from the peak or by 21.5% in real terms.

The excess housing supply situation is being further compounded by the increase in vacant properties for rent as job losses increase further. The latter is already leading to a significant reduction in rents, reported by Daft.ie to be down by almost 15% in the first four months of 2009 on the same period last year.

20,000 completed units projected for 2009

Projections for new housing supply are thus fraught with uncertainty. If one uses the available data to inform the projection there are two leading indicators of future supply: commencements and registrations. The commencements data report the number of units for which preliminary and other site works have been commenced by the builder in advance of proceeding to construction of the units. Registrations are made after commencements as dwellings must be registered before construction can proceed. However, the registrations series is not comprehensive and excludes housebuilders and developers who are not affiliated to the national insurance schemes¹², as well as some one-off housing units that are built directly by the owner and units completed by the public sector. In the past we have estimated total registrations by applying a grossing up factor for the

¹² Homebond and Premier Guarantee.

number of one-off units, which totalled around 10,000 in 2008. The figure in 2009 could be closer to 6,000 units.

In this preliminary assessment for 2009, the basis for the housing supply projection is the commencements series at the end of 2008. Thus the total number of completions (i.e. units actually built) this year is projected at 20,000, although this figure could well be lower. Much will depend on the social housing contribution, which is likely to be well below the 6,671 units constructed in 2007¹³. However, the number of ESB connections will be much higher than 20,000, as the unsold stock accumulated at the end of 2008 is sold. Thus the figure reported for completions as measured by 'ESB connections' is likely to be closer to 35,000 units this year.

3.3.2: Private Non-Residential Construction

Non-residential building - supply in the pipeline

Looking initially at the potential supply of non-residential buildings in the pipeline, the next chart provides data on the total floor area planned for new construction of non-residential buildings over the period 2002 to 2008. While planning permissions have a five year life and there is no way of knowing when the development will take place, the figures do provide an indication of the potential future supply.

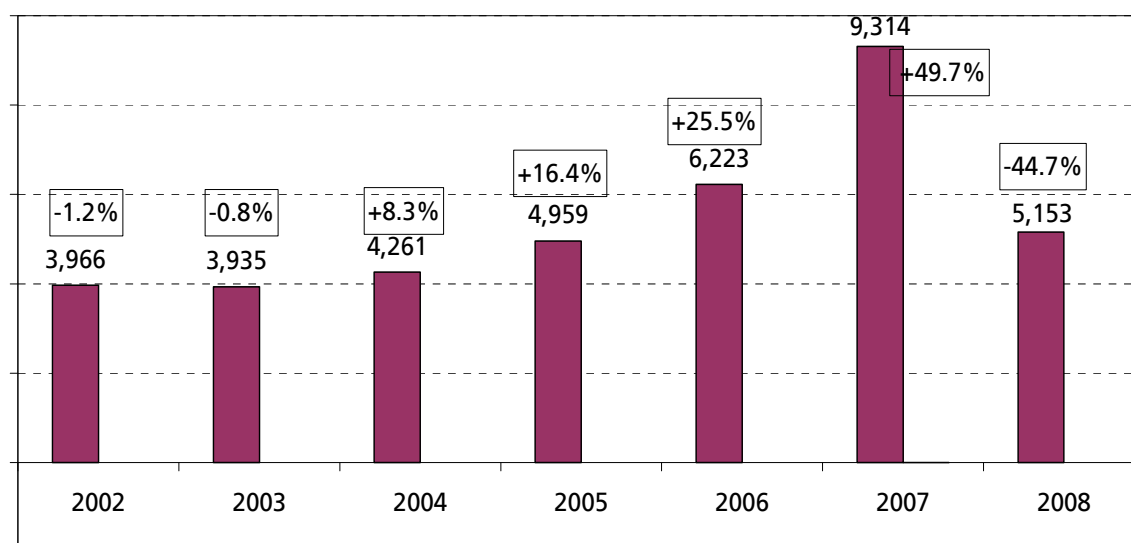
The figures suggest that the total floor area planned for non-residential buildings recorded a significant decline in 2008 (-45%) following two strong years in 2006 and 2007.

Within the total the strongest declines were recorded for agricultural (-77%) and industrial (-36%) buildings.

The level of agricultural buildings with planning permission has been growing at an exceptional pace since 2006. The prospects for agricultural building are expected to weaken considerably from 2009 onwards as the deadline for the close to completion date of farm buildings in receipt of grants under the Farm Waste Management Scheme expired in December 2008.

¹³ The contribution in terms of units built by local authorities and the voluntary sector in 2008 is not yet available.

Figure 3.4: Planning permissions granted for non-residential buildings
Total floor area (000s square metres)



Source: CSO

Percentages indicate annual growth rates.

Table 3.5: Key building types granted planning permission
Total floor area (000s square metres)

	Commercial	Industrial	Agriculture	Health & Education	Other social buildings	Total
2005	2,978	737	596	314	314	4,959
2006	2,573	1,105	1,945	209	209	6,223
2007	2,673	1,229	4,536	230	230	9,314
2008	2,488	792	1,041	229	229	5,153
Annual growth rates %						
2006	-13.6%	49.9%	226.3%	17.1%	-33.4%	25.5%
2007	3.9%	11.2%	133.2%	65.2%	10.0%	49.7%
2008	-6.9%	-35.6%	-77.1%	-6.7%	-0.4%	-44.7%

Source: Central Statistics Office Planning Permissions granted for non-residential buildings.

The private non-residential sector is not immune from the current recession. This is evident from a recent survey carried out earlier this year by the Construction Industry Council (CIC) to establish the volume of private sector construction work over the next three years¹⁴. Over 200 organisations - representing 34% of the private new building market - including developers, contractors and private clients, were contacted to ascertain their views regarding the state of the construction industry over

¹⁴ Available at: http://www.scs.ie/press_submissions/submissions_files/29-04-09-CIC-Submission-to-Government.pdf

the period 2009-2011. That survey concluded that there was a significant reduction in demand for office accommodation, which was exacerbated by a lack of tenants and purchasers. The inability to secure finance from lending institutions was a key factor contributing to the delay/postponement of projects. The general economic uncertainty, the collapse in the residential property market and the economic recession were all damaging confidence amongst potential clients.

Substantial fall off in private sector work this year

The response to the question regarding the prospects for private non-residential work over the period 2009-2011 suggested that the volume of work looks set to fall sharply over the next three years. Companies were extremely pessimistic about the outlook as employment losses continued to accelerate. It was evident from the survey that confidence in the sector is at an all time low.

For the purpose of this preliminary assessment we have used the survey to ascertain the volume of private non-residential construction output expected this year. According to the survey the decline envisaged by the respondents in the volume of work this year was around 44% on the previous year's level. This assessment projects a 40% decline in the volume of new private industrial, commercial and tourism building output this year.

Problems exacerbated by the oversupply in the boom period

A key difficulty faced by the private non-residential building market is the extent of the oversupply situation, following the boom over the period 2004-2007. The value of commercial building put in place over this period increased from €1.6bn in 2004 to €4.1bn in 2007 which corresponded to an average annual volume increase of almost 30% over the three year period¹⁵. As with the residential market, the problem is further compounded by the increased stock of vacant space. According to CB Richard Ellis Research¹⁶ the office vacancy rate in Dublin currently stands at over 16% and will continue to edge upwards over the coming months, particularly as the level of second-hand and surplus office stock coming to the market increases as existing occupiers consolidate their businesses. That same report referred to the pressures facing the retail sector with an increasing number of retailers going into administration and defaulting on their tenancies in reaction to weakening economic conditions and deteriorating employment prospects. These factors combined with the substantial oversupply of retail space over the past decade, suggest that the retail sector faces a difficult period for some time to come.

3.3.3: Public Sector Construction

Public capital programme provisions down 5% in 2009

Public sector construction activity relies on the capital allocations provided each year in the public capital programme which are made up of voted expenditure provisions, mostly funded by the Exchequer, and non-voted expenditure provisions. The latter relate to non-Exchequer funded capital provisions which are funded out of the resources of the semi-state agencies and local authorities and from external borrowing. It is the funds which are allocated to construction projects only that are of interest. While the proportion of funds allocated to building and construction

¹⁵ According to estimates from the Annual Construction Industry Review and Outlook, September 2008.

¹⁶ Bi Monthly Research Report, CB Richard Ellis Research, May 2009.

projects varies across each government department, approximately 70% of the total voted expenditure is allocated to construction projects. The remainder represents investment in machinery and equipment.

The most recent capital provisions for 2009 were published with the April Budget and in the Revised Estimates for Public Service 2009. The overall public capital programme (PCP) provision for 2009 is €11.8bn, which is 5% below the provisional outturn for 2008. Within the overall total, the voted expenditure provision is down by 16% while the non-voted provision is up by 20%¹⁷.

Table 3.6: Projected Public Capital Expenditure for 2009

	2008p	2009E	Annual	
	€m.	est	%	
		€m.	change	
Total Voted Expenditure	8,998	7,603	-16%	
Total non-voted expenditure	<u>3,497</u>	<u>4,206</u>	<u>20%</u>	
Total PCP	12,496	11,809	-5%	
<i>made up of:</i>				
1. Productive infrastructure				
Transport	3,992	4,003	3,555	-11%
Energy	1,281	1,435	1,925	+34%
Environmental Services	713	711	718	+1%
Telecommunications, Postal Services, Broadcasting	68	147	126	-14%
Sub-total	6,054	6,296	6,324	0%
2. Social infrastructure				
Housing	2,181	2,206	1,937	-12%
Government Construction	1,031	1,033	889	-14%
Education and Science	828	809	879	+9%
Health and Children	659	673	495	-26%
Sub-total	4,699	4,721	4,200	-11%
3. Sectoral economic investment	1,053	1,478	1,285	-13%
Total PCP	11,806	12,495	11,809	-5%

Source: April 2009 Budget and Revised Estimates for Public Service.

The Exchequer provision alone, which represents the vast bulk of voted expenditure, has been reduced by €1.6bn in 2009 compared with the 2008 provisional outturn¹⁸.

¹⁷ The detailed breakdown of the 2009 provisions by area of expenditure in the PCP is provided in Appendix.

¹⁸ The total exchequer element of non-voted expenditure was €8.9bn in 2008 and is projected at €7.3bn in 2009. The differences compared with the voted expenditure figures in Table 3.6 are accounted for by external borrowings/EU receipts.

Looking at the composition of the 2009 PCP:

- The largest provision is for **Transport** (€3.6bn), which is down 11% on the provisional outturn for 2008. The vast bulk of this expenditure is for the construction and improvement of roads (€2.2bn), which is down 17% on the 2008 outturn. Expenditure is projected to continue at the State Airports (+54% to €531m), notably at Dublin, while the third largest area within transport, namely investment by CIE, is down by 36% (to €427m). Other investment in public transport projects is also projected to fall and is down by 9% to €201m.
- The second largest provision is for **Housing** (€1.9bn) which is down by 12%. Within the total, the provision for local authority and social housing is down 27% (to €1.4bn).
- **Energy** (€1.9bn) is allocated the same amount as Housing, the largest proportions of which are for the ESB (€1.1bn) and BGE (€528m). By far the largest increase is projected for Energy (+34%) where investment by the ESB, Eirgrid, Bord Gáis and in energy conservation measures are all projected to rise strongly.
- The category **Government Construction** covers a broad range of areas including investment by the Office of Public Works (OPW) which is responsible for managing major projects for government departments and State Agencies as well as investment in courthouses, prisons, libraries and urban renewal. The total allocation of €889m is down 14% on 2008. This category also includes non-construction related capital investment such as computerisation (€91m).
- The €879m provision for **Education** includes €814m toward educational buildings across primary, post-primary and third level which is 2% above the corresponding allocation for 2008.
- The 26% reduction in the capital provision for **Health** includes a 31% reduction in the provision for investment in hospital and health facilities to €388m.
- Apart from Energy, **Environmental Services** is the only other area where the capital provision is projected to increase, albeit by only 1%. Within this total investment in Water Services (€615m) is projected to rise by 3% this year.

Capital spending down 14% in first four months

In terms of public capital spending to date this year, the April Exchequer Statement showed capital expenditure at €1.86bn in the first four months, down 14% on the same period in 2008. This amount corresponds to 27% of the (net) voted capital provision for the year compared with the cumulative spending profile projected for the first four months of 33.6%. The delay in spending possibly reflects a timing issue. However a certain amount of the capital allocations in each Government Department would already be contractually committed to ongoing projects at the beginning of 2009, implying less capital available for new start-ups. In the case of the National Roads Authority, for example, there was only one national road project planned to start this year.¹⁹

¹⁹ Available at: <http://www.nra.ie/News/DownloadableDocumentation/file,15953,en.pdf>

Similarly, in regard to hospital building projects, we understand that around 60% of the 2009 capital provision was already contractually committed at the beginning of 2009.

For the purposes of ascertaining the impact of the projected allocations on the volume of construction output we estimate the construction related element of each provision for each category of work (i.e. roads, education, public transport, hospitals etc.) based on our knowledge of the composition of the PCP and the returns obtained once a year on construction expenditure from Government Departments and State Agencies for the *Construction Industry Review and Outlook (CIRO)* publication. Our preliminary forecast for 2009 presented in Table 3.5, relates to construction related public capital investment only.

Combining the prospects for new work in the two public sector areas of civil engineering (+0.2%) and general contracting building work (-17.3%), the volume of public sector construction in new/major projects is forecast to decline by almost 7% this year.

3.3.4: Repair, Maintenance and Improvement Expenditure

The economic recession is putting some companies and businesses under pressure to reduce their cost base. Investment in repair and maintenance works is likely to be reduced or postponed unless deemed to be necessary. Thus the total volume of repair, maintenance and improvement (RM&I) expenditure on building and construction is projected to decline by 15% this year, made up of a 10% reduction in housing RM&I, a 13% reduction in general contracting RM&I and just over an 18% reduction in civil engineering RM&I.

3.4: Overall Prospects for 2009

The most severe contraction in thirty years

Our preliminary forecast for construction output this year is summarised in Table 3.7. The severity of the economic recession is such that the industry will experience the most severe contraction in almost thirty years. Following an estimated contraction in construction output of close to 18% in 2008, the volume of output in the industry is expected to contract by a further 35% this year. Thus the construction industry by the end of 2009 is projected to have lost 46% of its value at the peak in 2007. Moreover, the 2009 projection is unique in that all sub-sectors of the industry experience a decline in output. **By end 2009, the construction industry will already have shrunk to 13% of GNP compared with almost 25% at the peak.**

The one sector which was expected to support construction activity through the economic slowdown was the public sector and that has now not materialised due to the deterioration in the public finances. We will explore the prospects for public sector work over the medium-term more fully in the next *Construction Industry Review and Outlook (CIRO)* publication expected over the summer.

This assessment acknowledges that the construction sector is currently in a very difficult period, which is being exacerbated by the economic recession. The likelihood is that confidence will remain weak and job losses will continue to increase as the industry adjusts to a more sustainable and lower output level over the next three years. Nonetheless there is a real opportunity to invest in building and infrastructure projects now as the industry has spare capacity and unemployed resources. Moreover there is excellent value for money with tender prices back to where they were at a decade ago. The hope is that the Government moves quickly on its plans to harness alternative funding mechanisms (e.g. pension funds) for projects which would have been previously funded by the Exchequer. In the absence of such funding initiatives, the prospects for construction activity are exceptionally weak over the next few years.

Table 3.7: Short Term Prospects for Building and Construction (B&C) Output in 2009

2008p Current		2008 Share %	2007	2008p	2009e
€m.	Housing completions		78,027	51,724	20,000
	New housing				
	<i>of which</i>				
9,459	- Private sector	32%	-11.5%	-39.8%	-67.3%
1,318	- Public sector	<u>4%</u>	<u>-0.9%</u>	<u>31.1%</u>	<u>-14.4%</u>
10,777	Total new housing	36%	-11.0%	-35.5%	-60.8%
4,436	RM&I housing	<u>15%</u>	<u>8.8%</u>	<u>-8.0%</u>	<u>-10.0%</u>
15,213	Total housing	51%	-7.2%	-29.4%	-46.0%
	New General Contracting				
	<i>of which</i>				
5,063	- Private sector	17%	26.6%	-15.8%	-46.3%
2,121	- Public sector	<u>7%</u>	<u>27.1%</u>	<u>21.7%</u>	<u>-17.3%</u>
7,184	Total new General Contracting	17%	26.7%	-7.4%	-37.8%
1,195	RM&I General Contracting	<u>4%</u>	<u>11.1%</u>	<u>-12.9%</u>	<u>-30.2%</u>
8,379	Total General Contracting	21%	24.1%	-8.2%	-36.7%
17,961	Sub-total building new	60%	-1.7%	-26.6%	-51.6%
5,631	Sub-total building RM&I	<u>18%</u>	<u>9.3%</u>	<u>-9.1%</u>	<u>-14.3%</u>
23,592	Total building*	79%	0.3%	-23.1%	-42.7%
	Civil Engineering				
4,896	New civil engineering	16%	7.3%	12.7%	0.2%
1,232	RM&I civil engineering	<u>4%</u>	<u>-3.5%</u>	<u>3.7%</u>	<u>-18.2%</u>
6,127	Total civil engineering	21%	4.8%	10.8%	-3.5%
29,720	Total B&C construction output	100%	1.0%	-17.9%	-34.6%
	<i>of which</i>				
14,522	Private Sector (New)	49%	-3.5%	-33.1%	-60.0%
8,335	Public Sector (New)	<u>28%</u>	<u>10.2%</u>	<u>17.5%</u>	<u>-6.6%</u>
22,857	Total New Work	77%	-0.4%	-20.7%	-40.5%
15,213	Housing (New and RMI)	51%	-7.2%	-29.4%	-46.0%
14,506	Other B&C (New and RMI)	49%	16.0%	-1.0%	-22.7%

Source: 2007 and 2008 figures are based on the Department of the Environment's Annual Construction Industry Review and Outlook (CIRO) publication (September 2008) with some 2008 figures updated, based on more up to date information. The volume growth rates are based on output figures in constant 2008 prices. 2009 figures are DKM estimates.

* Housing and general contracting combined. The above classifications for the various segments of the industry are consistent with the classifications used in the CIRO.

Appendix 1: Detailed 2009 public capital provisions

Appendix 1A: April 2009 Voted capital ranked by expenditure				
Ranked by Exchequer capital allocation:	Department	2008	2009	
Area of expenditure		Provisional	est	%
		Outturn		change
		€m	€m	
Construction of national/non-national roads	Transport	2,069	1,723	-17%
Social housing provision and renewal	EH&LG	1,392	1,078	-23%
Public transport capital projects	Transport	890	628	-29%
Water Services Investment Programme	EH&LG	496	500	1%
National Schools - building, equipment & furnishings	E&S	489	423	-14%
Building, equipping, furnishing health and nursing facilities	HSE	544	371	-32%
Third level buildings	E&S	155	200	29%
Second level - building grants and capital costs	E&S	155	191	23%
Sustainable Energy Programmes	CM&NR	44	93	111%
Affordable housing and private housing supports	EH&LG	123	83	-33%
National childcare investment programme	H&C	80	60	-25%
Grants for sporting bodies for sport/recreational facilities	AS&T	58	56	-4%
Gaeltacht and Islands Development (mostly infrastructure)	CR&GA	75	55	-26%
Decentralisation	OPW	97	52	-46%
Rural development (e.g. Leader/rural Econ Sub-programme)	CR&GA	42	48	15%
Communications - ICT and other programmes	CM&NR	52	43	-17%
Flood relief projects	OPW	27	43	59%
Govt sites and buildings	OPW	68	41	-39%
Prison buildings and equipment	JE&LR	38	38	0%
Garda computerisation	JE&LR	43	35	-19%
IT systems /related services for Health Agencies	HSE	19	30	58%
Garda buildings	OPW	37	28	-25%
Courthouses - capital works	JE&LR	26	21	-19%
Fire and Emergency services	EH&LG	24	20	-17%
Cultural infrastructure	AS&T	35	19	-45%
Other	CR&GA	20	19	-3%
Cross border initiatives	Transport	5	18	245%
Irish Film Board (grant-in-aid)	AS&T	20	17	-13%
Grants for building/equipping of Agencies	H&C	19	15	-18%
Barracks - buildings investment	Defence	23	15	-36%
National Parks and Wildlife Service	EH&LG	23	14	-40%
Built Heritage and Irish Heritage Trust	EH&LG	26	13	-52%
Grants for swimming pools	AS&T	20	12	-39%
PPP costs	E&S	2	12	550%
Energy Research Programmes	CM&NR	13	12	-10%
Waste Management recycling/landfill:	EH&LG	56	12	-79%
North-South cooperation	CR&GA	12	11	-13%
Natural Resources	CM&NR	11	11	0%
Horse and Greyhound Racing Fund	AS&T	10	10	4%
Garda - communications and other equipment	JE&LR	19	10	-46%

Preliminary Forecast for Construction in 2009

Appendix 1A continued.....		2008	2009	
Area of expenditure	Department	Provisional	est	%
		Outturn		change
		€m	€m	
Carbon reduction measures	Transport	-	10	
Purchase of sites and buildings	OPW	39	10	-74%
Disability	OPW	1	10	568%
ICT in Schools	E&S	1	10	1003%
Disability services	EH&LG	11	9	-14%
Educational disadvantage	E&S	17	9	-48%
Irish Youth Justice Service	JE&LR	3	9	204%
LA library and archive services	EH&LG	15	9	-44%
Tourism product development	AS&T	16	8	-49%
Built Heritage	OPW	13	8	-39%
Economic and Social disadvantaged and disability	HSE	10	7	-29%
Irish Coast Guard	Transport	4	7	55%
State Pathology	JE&LR	1	7	383%
Miscellaneous services	EH&LG	7	6	-8%
Regional airports	Transport	9	6	-34%
Grants for Heritage Council	EH&LG	8	5	-36%
Culture	OPW	6	5	-27%
Probation service - services to offenders	JE&LR	2	5	153%
Other misc	OPW	5	4	-21%
Seaports and shipping	Transport	3	4	8%
Office machinery and supplies	E&S	3	4	16%
Inland Fisheries	CM&NR	2	3	72%
National Lottery funding	HSE	3	3	0%
Miscellaneous	CM&NR	2	3	11%
ICT	Defence	3	2	-20%
Community and social inclusion	EH&LG	5	2	-63%
National Sports Campus	AS&T	4	2	-50%
National Concert Hall and Crawford Gallery	AS&T	3	2	-47%
National Museum of Ireland	AS&T	5	2	-67%
Grant for certain refurbishment projects	OPW	5	2	-67%
National Qualifications Framework	E&S	2	2	0%
Lansdowne Road	AS&T	93	2	-98%
National Library	AS&T	2	2	-33%
Vehicle and driver licencing expenses	Transport	3	1	-45%
Arts Council	AS&T	5	1	-80%
Urban Regeneration	EH&LG	12	1	-92%
Broadcasting - grants	CM&NR	2	1	-63%
Road safety agencies and expenses	Transport	2	1	-59%
Grangegorman Development Agency	E&S	6	-	-100%
Grants for sport in disadvantage areas	AS&T	0	-	-100%
Remainder not separately identified here		1,308	1,345	3%
Total		8,998	7,603	-16%

Source: Revised Estimates for Public Service, 2009. Department of Finance.

Preliminary Forecast for Construction in 2009

<u>Appendix 1B: Composition of 2009</u> <u>Non-voted capital expenditure in PCP</u>	2008 Provisional Outturn €m	2009 est €m	Annual % change
ESB	960	1,064	11%
House Purchase/ Improvement Loans	466	654	40%
State Airports	344	531	54%
Bord Gáis	343	528	54%
Road improvement/maintenance	545	457	-16%
Eirgrid	36	188	422%
Local Authority and Social housing	220	120	-45%
Water and Sewerage Services Programme	98	115	17%
IDA Ireland Buildings	54	84	55%
Irish Aviation Authority	24	80	233%
CIE	78	57	-27%
Coillte Teoranta	59	47	-20%
An Post	44	46	4%
RTE	51	41	-19%
Bord Na Mona	28	30	7%
Sfadco	11	24	126%
Enterprise Ireland	45	24	-48%
Environmental Services	33	21	-36%
Teagasc	11	16	48%
Horse Racing Ireland	11	15	44%
Bord Na gCon	5	10	88%
Railway Procurement Agency	0	8	
IDA Ireland Grants	4	8	91%
Digital Hub Development Agency	0	5	
Udaras na Gaeltachta	8	4	-49%
Failte Ireland - tourism development works	13	2	-82%
SFADCO (Tourism)	1	2	123%
Port companies	1	2	192%
Ordnance Survey of Ireland	2	1	-26%
National Stud	1	1	0%
Irish Film Board	1	0	-50%
Broadcasting Commission of Ireland	0	0	-38%
Bord Iscaigh Mháire	0	0	
Urban Regeneration	1	0	-100%
Peace Programme	0	0	
Total non-voted expenditure	3,497	4,206	+20%

Source: Revised Estimates for Public Service, 2009. Department of Finance.