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NZ$3 billion for construction: is it enough to keep everyone working?

MAY 2020

Paul Buetow
Partner

Katrina Van Houtte
Special Counsel

Brendan Cash
Partner

There were some significant announcements for the construction sector in Budget 2020: $3 billion in additional infrastructure spending; 8000 more homes to be built by Kāinga Ora range of training initiatives. All of that will be welcome and much-needed support for the sector.

However it also leaves some large questions unanswered. Where will the 3 billion be spent? What sort of work will it entail? How much value will there be in the project? Those considerations will have a large bearing in determining the value of the spending to the sector. It's not yet possible to say just how substantially this spending may assist the sector as a whole. Those contemplating the prospect of large high value projects may have felt some misgiving at talk that the Auckland light rail project remains only a possibility at some future date, but nothing more than that for now.

Commercial building sector

One area of construction at particular risk is commercial (vertical) building. This is a sector that relies heavily on private investment, in building large scale housing developments, apartments, commercial office buildings, private industrial complexes, hotels, tourist facilities and similar. It's also the area with the lowest margins and therefore, is at the most risk in an economic downtown. Many of the players in this part of the sector will have a book of work that will carry them through the next 6 to 12 months but the question is: what projects will there be for them to work on when those reach completion?

Auckland Airport's decision to cease some of its development work is a good example of private sector investment in this space beginning to fall away. Uncertainty will see projects put on hold, as developers and the funders lack certainty of demand sufficient to support investment. A message we are hearing from parts of the market is that some future projects that make up the pipeline of work in 6 to 12 months' time are at least stalling.

Banks are also more cautious in these times, meaning funding is harder to come by even if the project is viable. Again, we are certainly hearing that it is more difficult to secure funding in the current circumstances.

The big questions are:

- to what extent will the Government direct funding into this sector? (as opposed to large scale civil infrastructure projects)
- can Government spending in this space make up for any reduction in private investment? Commentary to date suggests that it may very well not.
- Will Government be prepared to provide support in any other way to encourage and enable private developers to continue with projects? Some commentators are certainly indicating that such support may be necessary to avoid a hole in 6 to 12 months time as current jobs come to an end.

The answers to these questions are important. For example, the lack of work during the recession in the early 1990's resulted in this part of the industry being stripped to its bare bones. The sector is still paying for that today in terms of, for example, a shortage of senior skilled people able to support the work now required.

Resources

Resourcing constraints will limit the sector's capacity to deliver the shovel-ready projects expected to be announced this month. It's all very well saying we need to stimulate the economy by increasing spending on infrastructure. But it needs to be done carefully. If not there is a risk of an already stretched sector being overwhelmed to breaking point. The money needs to be spent carefully: targeted at the areas of highest need, but also at those with the resources to deliver it.

As part of the process by the Infrastructure Reference Group to identify shovel ready projects, consideration should be given to more creative solutions. One such example identified by the Group's Chair, Mark Binns, is the Government taking shared ownership of a private apartment development, such as for university accommodation, funding the project and then selling the asset at a late date when market conditions are favourable. We would encourage this approach. It steers valuable support toward spheres of high need such as the commercial building sector, and makes the most of an area with an available workforce.

So far in the shovel-ready programme, the sort of projects the Government has appeared to favour is the 'horizontal' infrastructure project, such as rail and water infrastructure. While thje country's infrastructure deficit extends to these projects too, unfortunately, this work tends towards a greater use of heavy machinery rather than labour and so employs the fewest workers. If keeping people employed is the aim of the government stimulus funding in the sector, they may need to look past traditional infrastructure projects towards for example the vertical sector which employs workers in largest numbers.

A further key issue faced by the industry in recent years is a lack of available resourcing during a 'construction boom' which has contributed to the delays and cost overruns suffered on many projects. That help has ordinarily come in the form of professionals and workers from overseas being drafted in to help, particularly on large projects such as Transmission Gully. That will not be possible in the near term, while COVID-19 lockdown border restrictions remain in effect.

To address this, the Government has announced $1.6m in funding to support workers who may have lost their jobs as a result of COVID-19 with free tertiary courses for apprenticeships or vocational training in building and construction, agriculture and manufacturing. While this initiative will help, it does not address the immediate resourcing needs and skills shortages on existing projects.

Local Government

Local Government is also a major player in the sector. Local Government faces a large shortfall in revenue as a result of the crisis, estimated in Auckland to be approximately $500 million. A large proportion of Council revenue comes from sources such as visitor attractions, pools, leisure centres, public transport fares and the like, all of which are significantly down. The reduction in revenue impacts significantly on Councils' ability to deliver essential services and much needed infrastructure. Whilst some Councils can borrow, many are already carrying large debt and have borrowing limits. Because of the shortfall Councils are likely to reduce both their capital and operational expenditure.

Conclusion

In all, the budget shows a large and welcome intention to help the sector to keep moving. Whether it will create sufficient opportunity to keep all the wheels turning remains to be seen.

Key contacts

Paul Buetow
Partner
D +64 9 375 1114
M +64 21 668 214
E paul.buetow@dentons.com

Katrina Van Houtte
Special Counsel
D +64 9 375 1142
M +64 21 660 741
E katrina.vanhoutte@dentons.com

Brendan Cash
Partner
D +64 4 915 0780
M +64 21 665 050
E brendan.cash@dentons.com

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