Watts Bulletin

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No upturn in tender prices for two years, says BCIS

Contractors are being forced to keep tenders low in an attempt to remain competitive and ride out the recession, according to the latest Tender Price Index compiled by RICS' Building Cost Information Service (BCIS).

The price of new construction work fell by 0.8% in the third quarter of 2008 compared with the previous quarter, and by 1.2% compared with a year earlier. BCIS expects tender prices to fall by a further 10% throughout 2009 and 2010.

Overall, new orders for construction fell 10% in the third quarter when compared with the previous quarter. And they fell by 18% compared with the same quarter in 2007. Over the same period, costs continued their upward trajectory with materials rising 7.2%, and wage rates rising by 4.6% in the year to the third quarter, putting a tighter squeeze on potential profits.

BCIS expects new work output to fall by 7% in 2009 and by 3% in 2010, with the private housing, private industrial and private commercial sectors set to suffer the most significant downturn during the next two years. The public sector has a more positive outlook, with the Government planning to bring forward projects in an attempt to stave off the impact of the recession. However, many of these projects are still struggling to attract private finance and, as a result, doubts about the effectiveness of these measures are already being voiced. BCIS analysts are not expecting new work output to grow until 2011.

Peter Rumble, BCIS Information Services Manager confirms that the next two years are going to be tough on the construction industry, "Contractors are going to have to be competitive in order to stay in business. As a result it is expected that the current trend of falling tender prices is going to continue for some time to come. Contractors who traditionally carry out a significant proportion of public sector work are likely to fair better than those carrying out mainly private sector work. However this is assuming that a prompt release of public funds is delivered, as promised in the Pre-Budget Report, which is already looking unlikely."

For more information go to www.bcis.co.uk

Editorial

Welcome to the March issue of Watts Bulletin. More bad news. Building magazine reported in February that construction liquidations are up by 57% and an estimated eight building firms are closing their doors every day. The result of this is bad debt and failed projects. Inevitably, competition for the work that is out there means falling tender prices.

On page three of this issue, we consider a report on the prospects for regeneration projects. The verdict: hard times ahead but there are still opportunities for those who can put together innovative deals and have access to the right resources. And finally, on page four we look at the options that may be open to those who find themselves with a stalled or failing project to deal with.

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Flood risk developments given go-ahead

In a month when, once again, hundreds of people were forced out of their homes due to serious flooding, a new report reveals that developments in high flood risk areas are still being given the green light.

Local planning authorities in England granted planning permission for 16 major developments, including some 240 homes and a primary school, in areas at risk from flooding despite Environment Agency objections, says the report. The Agency's annual 'Development and Flood Risk' survey, shows the performance of local planning authorities in England between April 2007 and March 2008 on planning applications where the Environment Agency provided advice on flood risk.

Virtually all planning decisions (96%) where the Environment Agency objected, were in line with its advice – the highest ever level of compliance. However, 16 developments were approved against Environment Agency advice, up from 13 in 2006/2007, including some 240 homes, a primary school, offices, apartments, a business park and a ferry terminal.

The Environment Agency lodged objections to 6,200 planning applications on the grounds of flood risk in 2007/2008 up from 4,750 in 2006/2007. A high proportion of these objections were removed after negotiation with developers and local authorities resulted in modified plans.

The insurance industry has already said that it may not provide insurance to certain new developments in the flood plain if properties are granted planning approval against Environment Agency advice.

For more information go to www.environment-agency.gov.uk

Energy Performance of Buildings Directive is recast

The EU Commission has launched its proposal for a revised Energy Performance of Buildings Directive (EPBD) as part of the Energy Security and Efficiency Package and Second Strategic Energy Review.

The existing EPBD, adopted in 2002, aims via legislation, to improve buildings' energy performance. Some EU Member States are meeting the requirements of the Directive. However, many countries have major gaps in their implementation and the EU Commission believes there is potential for improvement. The Commission is keen to enhance and clarify the EPBD and launched a public consultation on a recast Directive during 2008. The main changes of the new proposal (COM 2008/780) compared with the EPBD from 2002 are:

- National promotion and national plans to be established, with clear targets for increasing the number of low or zero-carbon buildings. Public Authorities are to take the lead with their own buildings.
- Minimum energy performance levels will be set for new and renovated buildings. The aim here is for national minimum energy performance requirements of buildings to gradually approach cost-optimal levels in four steps. First, countries will set cost-optimal requirements using their own methodology. Then the Commission will develop a comparative methodology and countries will take part in a comparison. From 30 June 2014, countries that provide incentives for the construction or renovation of buildings will only be able to give them for projects that comply with minimum energy performance requirements based on harmonised calculation methods. Finally, from 30 June 2017, reviews of minimum energy performance requirements will include that these requirements are cost-optimal, using the results of the harmonised calculation methodology.
- The obligation to consider renewable energy systems and district heating for new buildings is extended to all new buildings not only those above 1,000 m², as is the case at present.
- The 1,000 m² threshold for meeting national or regional energy performance requirements when buildings undergo major renovations, is to be scrapped. A 'major renovation' will be designated as works valued at more than 25% of the building value or where structural renovation of more than 25% of the building envelope is undertaken.
- Minimum energy performance requirements to be introduced for the installation of new or the replacement/major retrofit of technical installations such as boilers, heat distribution and ventilation systems.
- Energy Performance Certificates to be strengthened and clarified. Certificates must be provided every time there is a property transaction and the prospective buyer or tenant must be informed of the energy performance of the building/flat at the earliest possible stage of the marketing process.
- Clarification of the required frequency and reporting of inspections of heating systems and air conditioning.
- Clarification of the requirements for both skills and independent status of accredited experts undertaking production of building certificates and inspections of technical installations.

If the new Directive is adopted by the EU Commission during 2009, it must be included in national legislation by 31 December 2010 and fully implemented by 31 January 2012. National information campaigns will be devised on the use of building certificates and inspection reports and penalties will be enforced if Member States do not implement the new provisions.

The new Directive is expected to reduce EU energy consumption and carbon dioxide emissions by an estimated 6-8% by 2020.

For more information go to www.europa.eu

Parkinson report reveals regeneration at risk

An independent report 'The Credit Crunch and Regeneration: Impact and Implications' commissioned by the Government from Professor Michael Parkinson of Liverpool John Moores University, published its findings at the end of January.

During the past six months Professor Parkinson's team from the Investment Property Databank (IPD), Oxford Economics, the University of Reading and City University has collected a wide range of evidence based upon interviews with many key players in the regeneration community, a major national survey, and analysis of work with many regeneration agencies.

The report found that the impact of the credit crunch on regeneration is serious but with the right sort of long-term leadership and resources it can come through the downturn. The financial crisis is impacting on a business model that has underpinned regeneration in recent years and pressure on the sector is likely to get more intense.

Professor Parkinson is clear the system will not recover quickly and everyone from the private sector, councils, regional agencies and central Government has a part to play in getting through the downturn and preparing for better times.

Key points in the report are:

- The financial crisis is severe and not over yet. The pressures will get more intense.
- Long-term regeneration activity is continuing and must be sustained. There is a need to retain capacity to keep skills in this sector.
- Regeneration has and will continue to move from risky to quality investments. Deprived areas will need most support.
- Real long-term leadership and commitment is needed to keep the wheels moving and prepare for the upturn.
- The sector needs more financial innovation, more genuine partnerships and more quality schemes.
- Public resources and programmes are keeping regeneration going as much as the private sector. This contribution will be even more crucial in the coming months.

Professor Parkinson concludes that the impact of the credit crunch on regeneration is mixed. Many of those projects that are already underway are continuing, especially where the public sector is involved. Projects yet to begin are at risk. Economically marginal projects are increasingly less attractive and the north of England and the midlands have been affected more than the south-east.

Looking ahead, Professor Parkinson identifies opportunities for partners to review current commitments; make strategic land acquisitions rather than begin new schemes; focus on long-term place making as well as house building and create longer term relationships between developers and the public sector.

To download the full report 'The Credit Crunch and Regeneration: impact and implications' go to www.communities.gov.uk

WRAP report goes out to tender

The Waste & Resources Action Programme (WRAP) has put the production of its successful Materials Pricing Report out to competitive tender. The Government-backed organisation is looking for a company capable of producing a credible and independent guide to prices for recyclable materials on a regular basis, as well as maintaining subscriber and pricing databases.

Distributed electronically, the Materials Pricing Report is a free weekly subscription service aimed specifically at buyers and sellers of recovered materials. It contains pricing information based on live transaction data, as well as a commentary section which includes market intelligence on the key factors driving the market.

The publication is an important element in WRAP's work to encourage and enable businesses and consumers to be more efficient in their use of materials and recycle more items more often, with the aim of helping to minimise landfill, reduce carbon emissions and improve our environment.

Liz Dixon Smith, Economist with WRAP, explains: "The Materials Pricing Report was introduced by WRAP in mid-2004 to improve the transparency of the markets for recyclable materials. It offers an independent authoritative source of pricing information on recyclable materials and helps subscribers achieve market prices for their material."

For more information go to www.wrap.org.uk

Government announces 'Great British Refurb'

In future, British households will be able to receive expert, targeted help to reduce their fuel bills and access low-carbon heat and power in their homes. This is the objective of an ambitious long-term heat and energy-saving strategy set out by the Department of Energy and Climate Change in February.

The draft plan, published for consultation on 9 February, establishes the need to reduce household carbon emissions to almost zero, in order for the UK to achieve its ambitious target of an 80% cut in emissions by 2050. By 2030, the aim is for whole-house improvements to be available to all householders in England and Wales.

The plan includes proposals for improving the quality and widening the availability of information and advice; the provision of new finance packages; and options for the delivery system of energy efficient and low carbon improvements. Key proposals are:

- Finance packages to install energy efficiency measures and low-carbon heat and power sources to be offered to householders. Repayment from part of the savings on energy bills would be linked to the property, rather than to residents.
- Combined with guaranteed cash payments by way of a Renewable Heat Incentive and a feed-in tariff for small scale electricity generation, payback for homeowners who switch to low-carbon technologies and save energy to start from day one.
- Options for improving the delivery of energy efficiency advice and measures, including establishing a central coordinating body funded by energy companies and working to Government-set targets.
- Rolling out low-cost home energy audits, developing a qualification for energy advisers, and establishing an accreditation scheme for installers.

The Heat and Energy Saving Strategy will be open for consultation for 12 weeks.

For copies of the consultation documents go to www.decc.gov.uk

Failed projects: what are the options?

In recent months we have become accustomed to business failure. All geographic locations and all sectors are now feeling the impact. But the opportunity exists for those caught up in the mess, particularly the banks, to take a more proactive approach this time around.

The amount of distressed and bad debt in UK property is unknown but without question we are talking billions of pounds. Watts is now working with a number of owners and administrators of both distressed debt and projects, finding ways to complete stalled projects and realise their value as quickly as possible. In our experience, the banks' favoured option to deal with the problem is often to take equity in these projects. But this is a medium-term play. The last thing banks originally intended was to end up owning the developments they agreed to fund. Furthermore, the equity will not release any value until markets improve and, depending who you talk to, this could be anything up to five years away.

So, what are the alternatives? Even in the current climate, there are still ways of completing and disposing of schemes. If they haven't already done so, banks should be carrying out scheme reviews of all developments now. In this way a coherent plan can be put in place to assist both banks and developers to nurture schemes to completion.

If the worst does happen, and a bank is forced to take possession of a development, it is vital to be able to view the situation with clarity. In order to clearly recognise the obligations, completion issues and disposal options that can be used to maximise return – or minimise loss, the first steps to take are to:

- take a deep breath;
- appoint a team;
- secure the site;
- procure a feasibility/options review (construction quality, cost, design/disposal options); and
- compile a recovery plan.

Each project presents its own set of circumstances and the recovery plan for each will be differently constructed. A range of options is on offer to failed schemes that includes:

- reconfiguring the deal and amending planning consents;
- injecting additional development expertise; and
- introducing third party equity.

A popular proverb is that the Chinese use two brush strokes to write the word 'crisis'. One brush stroke stands for danger, the other for opportunity. For the banks, rushing into a fire sale or simply doing nothing at all are both options, but neither is particularly attractive or financially beneficial. Instead, in this crisis as in all others, be aware of the danger – but recognise the opportunity.

For more information on Watts Project Recovery service, contact Chris Knott, Managing Director of Watts' London office on +44 (0)20 7280 8000.

The Watts Bulletin is the technical companion to the Watts Pocket Handbook, the essential guide to property and construction, as used by professionals since 1983.

Watts Bulletin editor: Trevor Rushton (Email: trevor.rushton@watts-int.com)
Watts Bulletin author: Lesley Davis

Comments, criticisms and contributions are always welcome.

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Watts network of offices:

BARCELONA
T: +34 93 255 31 25
E: barcelona@watts-int.com

BELFAST
T: +44 (0)28 9024 8222
E: belfast@watts-int.com

BERLIN
T: +49 30 345 0569 0
E: berlin@watts-int.com

BIRMINGHAM
T: +44 (0)121 265 2310
E: birmingham@watts-int.com

BRISTOL
T: +44 (0)117 927 5800
E: bristol@watts-int.com

DUBLIN
T: +353 (0)1 703 8750
E: dublin@watts-int.com

DÜSSELDORF
T: +49 211 159 434 12
E: dusseldorf@watts-int.com

EDINBURGH
T: +44 (0)131 226 9250
E: edinburgh@watts-int.com

FRANKFURT
T: +49 69 971 6816 0
E: frankfurt@watts-int.com

GLASGOW
T: +44 (0)141 353 2211
E: glasgow@watts-int.com

THE HAGUE
T: +31 (0)79 361 88 91
E: thehague@watts-int.com

LEEDS
T: +44 (0)113 245 3555
E: leeds@watts-int.com

LONDON
T: +44 (0)20 7280 8000
E: london@watts-int.com

MADRID
T: +34 91 435 54 59
E: madrid@watts-int.com

MANCHESTER
T: +44 (0)161 831 6180
E: manchester@watts-int.com

MUNICH
T: +49 89 678 0663 0
E: munchen@watts-int.com

PARIS
T: +33 (0)1 42 86 69 80
E: paris@watts-int.com

SOFIA
T: +359 2 827 2222
E: sofia@watts-int.com

STOCKHOLM
T: +46 (0)8 791 7300
E: stockholm@watts-int.com

VIENNA
T: +43 (0)1 533 6809
E: vienna@watts-int.com

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