

GOVERNMENT INFLUENCE ON THE CONSTRUCTION INDUSTRY DURING THE ECONOMIC RECESSION 2007 - 2013

Paul Tansey¹ and John P. Spillane²

¹*Department of Civil Engineering and Construction, Institute of Technology Sligo, Ballinode, Sligo, Ireland.*

²*School of Planning, Architecture and Civil Engineering, David Keir Building, Queens University Belfast, Belfast BT9 5AG, Northern Ireland, UK.*

Due to the high degree of international and economic integration across the globe, the 2007 global financial crisis quickly spread, causing recessions and widespread credit restrictions in advanced nations. During recessions, economic fluctuations cause dramatic changes to the market structure of industries, in particular, that of the construction sector. These structural changes can be further influenced by government strategies and policies; which if used incorrectly, can serve to fuel and exacerbate downturns. In contrasting form, during an economic recession, government strategies and policies can also be used to aid in exiting such economic turbulence. From an extensive review of literature it became apparent that very little research offered a comprehensive and systematic overview of Irish and UK construction related government policies and strategies adopted during recessions; hence the emergence of this topic. As part of an ongoing research PhD, the purpose of this paper is to collate and group Irish and UK Government strategies and policies adopted for the construction sector during the recession period 2007-2013; resulting in the establishment of a construction industry development framework and a taxonomic framework. The results reveal serious problems with the national strategic plan for the Irish construction industry, given that there is no overseeing body or target dates for implementation of the proposed actions. Furthermore, both countries failed to prioritize the proposed key actions within their strategic plans. The findings of this paper can be applied in the context of the construction sector to address shortcomings in the respective subsectors, while also aiding policy makers and company executives in mapping out future strategic milestones.

Keywords: economic development, government policies, recession, taxonomy.

INTRODUCTION

The 2007 global financial crisis which began in the United States was caused by an interest rate increase in July that triggered bankruptcies in the subprime market along with the start of tumbling house prices as demand dried up (Knopp 2010). The collapse of Lehman Brothers in September 2008 signalled the acute stage of the crisis, with the severe economic recession quickly spreading across the global financial system; causing recessions and credit crunches in advanced nations such as Ireland and the United Kingdom (UK). Subsequently, the challenging economic environment which unfolded sent unconceivable shockwaves across the construction sector as

¹ ptansey@itsligo.ie

confidence weakened across the property sector. In response, governments used monetary and fiscal policy measures in order to stimulate growth and to maintain economic stability.

From a thorough review of previous studies it became apparent that very little research offered a comprehensive and systematic overview of Irish and UK construction related government policies and strategies adopted during the recent recession. To address this gap in knowledge, the purpose of this paper is therefore to collate and group Irish and UK Government strategies and policies adopted for the construction sector during the recession period 2007-2013. It aims to establish a construction industry development framework and a taxonomic framework, which will aid policy makers and company executives in mapping out future strategic milestones, while also providing a basis on which to benchmark the industry.

GOVERNMENT RESPONSE DURING RECESSION

Through its administrative power of intervention, government can play a major role in the construction industry, thereby influencing the market structure of the sector (Kang 2006). During recession, governments will generally change monetary policy by lowering the interest rate while it raises interest rates when there is inflationary pressure. With regard to fiscal policy in recessions, actions are generally taken by governments in order to stimulate the performance of the economy. During the recent recession, interest rates declined and inflation fell rapidly, leaving governments in both Ireland and the UK with little room to use monetary policy to stabilise the economy.

The scope of this study will be broadly based on fiscal policies, which according to the Federal Reserve (2012), refer to the tax and spending policies of government. Throughout the economic literature ongoing debates concerning two distinct theoretical approaches on fiscal policy come to the fore, namely; neoclassical and keynesian. Keynesian models purport that fiscal policy should be countercyclical, while neoclassical models imply fiscal policy should remain neutral (Cuadra *et al.* 2010). In the aftermath of the 2007 global economic recession, Krugman (2009) polemically argued that keynesian economics, in the form of expansionary fiscal policy (e.g increasing public expenditure), are required to foster economic growth. Furthermore, Claessens *et al.* (2009) in their study of 21 OECD countries during the period 1960-2007, found that expansionary policies are associated with less severe recessions. Conversely, Blinder (2006), after evaluating empirical evidence on the matter, argues against the use of discretionary fiscal policy.

In the construction industry, a lot of the research concerning government strategies and policies are profiled under the domain 'construction industry development'. Some of the more prominent works on the role construction plays in national economics and the influence of government on the industry include; Turin (1973), Ofori (1993a), Hillebrandt (1984), and Fox and Skitmore (2007). However, there are only a limited number of studies which examine construction industry development and government influence during times of recession (e.g Ofori 1988; Hillebrandt *et al.* 1995; Chiang *et al.* 2004; Ng *et al.* 2009), with little on theoretical developments. Ofori (1988), for instance, critically reviewed the construction industry in Singapore between 1960 and 1986. In 1985 Singapore suffered a national economic recession where GDP fell by 1.9%, mainly attributable to an oversupply of property. Despite attempts by government to stimulate demand in the private sector, and increasing expenditure by 5% on public sector works (Ofori 1993a), construction output fell by almost 12%. In

the UK, Hillebrandt *et al.* (1995) investigated the behaviour and strategies of 18 large UK construction contractors during the early 1990s recession, while also examining the construction environment. They concluded that the recession was caused by a tightening of monetary policy, where government increased interest rates from 7.5% to 15% to combat an overheated economy. Conversely, it caused the property market to collapse. Chiang *et al.* (2004) reported on a collaborative research project involving 11 Asian countries relating to the years 1995-2001. The study entailed a detailed review of each construction industry, specifically highlighting the industry behaviour and government policies adopted in response to the 1997 Asian crisis. In Australia, for example, they found that the implementation of fiscal policies, such as the goods and service tax in 2000, led to a contraction in construction activity of over 24%, however the sector steadily emerged out of this in 2001 (CII and Sharma 2004). Utilizing an extensive literature review and a series of interviews, Ng *et al.* (2009) investigated the construction industry development of advanced economies (Australia, Japan, Singapore, South Korea, UK) that encountered financial recessions. They summarised the strategies and policies adopted by the studied nations using a long-term framework which included five key attributes: government policies and strategies supporting construction business; industry led better practice and culture; financial resources and skill training; research and development for construction; and exploring alternative markets. In relation to government initiatives, they concluded that if a recession lasts for a long period of time, then it would be difficult for government to increase expenditure on public projects.

TAXONOMY OF GOVERNMENT STRATEGIES AND POLICIES

Given that most of the studies above analyse construction related government policies and strategies under a broad spectrum, the framework proposed by Ng *et al.* (2009), was further developed, resulting in a new construction industry development framework (Figure 1). Using the framework shown in Figure 1 as a guiding template, Irish and UK construction related government strategies and policies adopted during the recession period 2007 – 2013, were collated and grouped under a taxonomic framework (Table 1). While a full review of all government strategies and policies adopted during the recession are outside the scope of the study, those most applicable to the construction industry are outlined as follows;

- Strategic planning and reform - In response to industry pressure, the Irish Government published a national strategy for the construction sector in 2013, which set out a vision for the industry to 2015 and beyond (Forfas 2013). In contrast, the UK construction industry has gone through several years of reform after the Latham and Egan reports (Latham 1994; Egan 1998). Furthermore, a Housing Strategy was published in 2011 followed by the launch of Construction 2025 in 2013, documenting the vision and long-term strategic direction for the industry (UK Government 2013).
- Laws and regulations - To combat issues regarding poor quality standards the Irish Government announced publication of the Building Control (Amendment) Regulations 2013. Registered employment agreements were ceased in 2013; thus allowing employers to hire new employees on lower pay. The Construction Contracts Act 2013 was also enacted to combat the severe problem of delayed payments encountered by main contractors and subcontractors during the recession. In the UK, the Planning Act 2008 was introduced in order to fast-track the planning process for major infrastructure projects, while under the Localism Act 2011, a new major infrastructure

planning unit was established (Department for Communities and Local Government 2011).

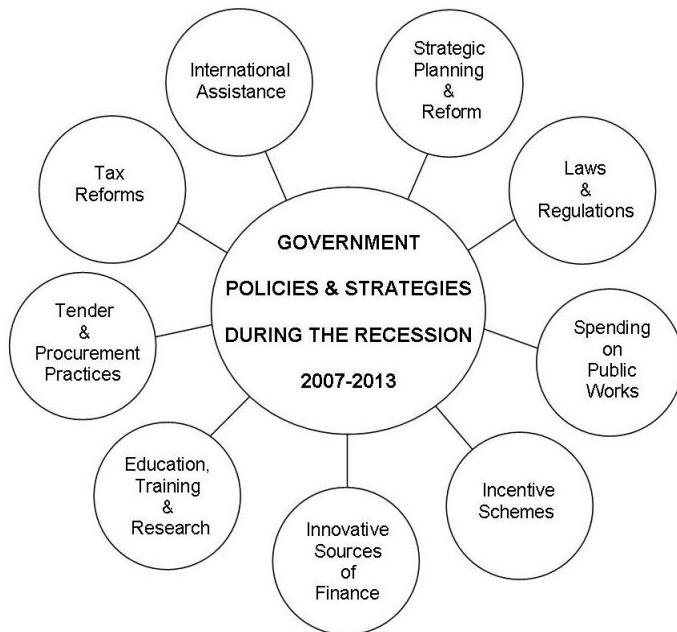


Figure 1 Construction industry development framework

- Spending on Public works - In Ireland, expenditure on public capital projects in the years leading up to the recession averaged at €9.1bn per year (Government of Ireland 2008) while during the recession spending averaged at only €3.4bn per year (Department of Public Expenditure and Reform 2011). During the recession in the UK, public and private infrastructure investment increased from £41 to £45 billion per year (HM Treasury 2013). However, there was a 15% drop in the value of public construction output from a peak of £32.2bn in 2010 to £27.3bn in 2013 (Office for National Statistics 2014).
- Incentive Schemes - In 2011, the Irish Government established a new National Internship scheme called 'JobBridge', which provides work experience placements for jobseekers. The Government also implemented energy efficiency incentive schemes while conversely providing work for smaller construction firms through the Better Energy Homes scheme, and the Home Renovation Incentive scheme. The UK Government launched the Renewable Heat Incentive scheme for the non-domestic sector, while the Green Deal scheme was designed to entice home owners and businesses to adopt more green energy technologies. As part of the housing strategy 2011, a number of incentive schemes were implemented, such as; the New Build Indemnity Scheme, Firstbuy, and New Homes Bonus scheme.
- Innovative Sources of Financing - The Irish Government developed very few innovative ways of raising finance for construction projects during the recession. It wasn't until April 2013, some six years into the recession that Real Estate Investment Trusts (REITs) were launched. Conversely, the UK Government responded better to the economic crisis by providing finance for infrastructure projects through direct measures, such as the UK Guarantees Scheme, while also creating a new Green Investment Bank to tackle any shortfall in the debt markets (HM Treasury 2010-2013).

- Education, Training and Research - In Ireland, the Department of Jobs, Enterprise and Innovation increased expenditure by 17% during the period (Department of Public Expenditure and Reform 2011). As part of its jobs initiative programme, the Irish Government announced 'Springboard' which offers higher education places for the unemployed. In order to stimulate research and development, Enterprise Ireland launched innovation vouchers and innovation partnership grant programmes. The UK Government established the Tunnelling and Underground Construction Academy (TUCA), with the objective of training workers for major infrastructure projects, while the Employer Ownership Pilot (EOP) scheme was launched with the aim of allowing employers to design and develop their own training (HM Treasury 2013).
- Tender and Procurement Practices - In response to significant cost overruns on major public projects, the Irish Government introduced the Capital Works Management Framework (CWMF) in 2007. The UK Government set up 'Infrastructure UK' in 2010 in order to investigate methods of reducing costs on major infrastructure projects and to coordinate and simplify planning and prioritisation of investment in infrastructure (HM Treasury 2014). Similarly, the UK's Government Construction Strategy was launched with the main objective of delivering a 15-20% reduction in construction costs. The governments requirement of fully collaborative 3D BIM by 2016 is also stimulating change across the supply chain in the UK construction sector.
- Tax Reforms - In order to help the declining property market in Ireland, a new incentive relief from Capital Gains Tax was announced. The government also made changes to Value Added Tax (VAT) rates with a reduction in 2010 and an increase in 2012 (Revenue 2014). The UK Government also implemented tax reforms and as part of the fiscal stimulus package in 2009; VAT was reduced, along with the spreading of tax payments for SME's. Furthermore, in 2010 and 2013 the UK Government reduced Corporation Tax for large and small businesses (UK Government 2009 - 2013).
- International Assistance - During the recession Enterprise Ireland announced a €100m Enterprise Stabilisation Fund in order to help exporting small and medium enterprises (SME's) who were in financial difficulty (Enterprise Ireland 2009). They also launched a tailored training initiative called 'Leadership 4 Growth: Construction'. The UK Government through its Construction Strategy 2025, proposed the 'GREAT' brand, which identifies global trade opportunities for firms (HM Government 2013). The High Value Opportunities (HVO) programme was also launched, and aims to help UK firms bid and win work for large overseas projects (UK Trade and Investment 2014).

DISCUSSION

The taxonomy shown in Table 1 outlines the various construction related strategies and policies which were adopted by the Irish and UK Governments during the economic recession 2007-2013. Although a full discussion of all the themes portrayed in Figure 1 is outside the scope of the paper, the extent of the discussion will be focused on four themes, namely; strategic direction and reform; laws and regulations; international assistance; and spending on public works.

During the crisis the Irish construction sector lacked any form of strategic direction from government, taking some six years after the recession started, to announce a

national strategy for the sector. Meanwhile in the UK, strategic direction was accomplished a lot earlier, through the Housing Strategy in 2011 and the Construction Strategy in 2013. There were some significant problems identified with the Irish strategic plan, such as, the non-existence of an overseeing body to deliver the plan, and a lack of target dates for monitoring each of the proposed 36 key actions. In comparison, the UK's strategy adopts a more practical and realistic approach, in that, the plan is overseen and delivered by a new Construction Leadership Council, while the key actions encompass target dates on which to monitor their progress. Nevertheless, both strategic plans lack prioritization of the stated key actions. In his research on construction industry development, Ofori (1993b) reported similar observations with regard to construction sector strategic plans.

During the recession the Irish Government introduced the Building Control (Amendment) Regulations 2013 in order to deal with poor quality standards and to help combat the black (cash) economy. Yet again, the government delayed in adopting such an important regulation, but on a positive note, the new regulations bode well for the industry. All contractors and subcontractors involved must be registered and tax compliant, thereby reducing shadow economy operators, and the loss of revenue to the state. According to a survey conducted by the Construction Industry Federation (CIF) (2012), the number of black economy operations have increased by 90% since the downturn began. Also gone are the days of building off planning permission drawings, with all build stages now requiring proper supervision and compliance, thus bringing Ireland in line with UK standards. In the UK, the government responded swiftly by introducing the Planning Act 2008 in order to boost construction activity by fast-tracking major infrastructure projects. However, in five years only a mere 14 developments have been decided on, with government acknowledging that there is still room for improvement (Department for Communities and Local Government 2013). Moreover, with regard to both countries, there is cause for concern with the lack of appreciation by government of the importance of timely decisions during recession. Similar sentiments were acknowledged by Hillebrandt *et al.* (1995) relating to the 1990s recession in the UK.

In relation to international assistance, Enterprise Ireland has been proactive in assisting Irish construction firms export their services abroad. According to a Forfas (2013) report, a number of Irish construction companies involved in professional services have become well established in international markets during the recession period, with some companies reporting a 15% increase in export intensity between 2010 and 2011. Nevertheless, despite launching a tailored training initiative called 'Leadership 4 Growth: Construction', which was designed to develop the capabilities of Irish CEOs in attaining international growth (Enterprise Ireland 2014), several large Irish construction contractors failed miserably on their international expansion. For example, Sisk and Roadbridge ceased construction works in Poland in 2012 following major disagreements with the Polish roads authority, reporting losses in the region of €50 - €60m (Independent 2012). Evidently there is a serious need for more appropriate government action in helping Irish contractors to succeed internationally. A lack of government assistance was also evident in Hong Kong, with Chiang *et al.* (2001) concluding that the government has never helped local contractors in securing

Table 1: Taxonomy of construction related government strategies and policies adopted during the economic recession 2007-2013.

Strategies & Policies	Ireland	United Kingdom
Strategic Planning & Reform	Forfas report	Housing Strategy
	Establishment of new department	Construction 2025
Laws and Regulations	Building control regulations 2013	Localism Act 2011
	Cease of employment agreements	Planning Act 2008
	Construction Contracts Act 2013	
Spending on Public Works	63% reduction in spending	15% reduction in spending £14bn CrossRail project
Incentive Schemes	National internship scheme	Renewable heat incentive
	Better energy homes scheme	Green deal scheme
	Home renovation scheme	New build indemnity scheme Firstbuy New homes bonus
Innovative Sources of Finance	Real estate investment trusts	UK guarantee scheme
		Green investment bank
		Enterprise zones
		Insurance growth action plan
		Pension infrastructure platform
Education, Training & Research	17% increase in dept. spending	Set up TUCA
	Springboard	EOP scheme
	Innovation vouchers & partnerships	Patent box initiative
Tender & Procurement Practices	Capital works management framework	Infrastructure UK
		Construction strategy
		BIM mobilisation group
Tax Reforms	Capital gains tax relief	Reductions in VAT rates
	Introduction of property taxes	Spreading tax payments
	Changes in VAT rates	Reduction in Corporation tax
International Assistance	Enterprise stabilisation fund	'GREAT' brand
	Leadership 4 growth: Construction	HVO programme

contracts abroad through fiscal means. In contrast, the UK already have a well established base of international contractors with experience of overseas contracting spanning back many decades. However, only recently has the UK Government put significant emphasis on international growth for its construction firms; mainly through its Construction Strategy 2025. Through the High Value Opportunities (HVO) programme which was established in April 2011, UK firms have already won £8 billion worth of contracts at all levels of the supply chain (UK Trade and Investment, 2014), thus demonstrating the success of key government assistance. Similarly in Turkey during the late 1980s, a contraction in the construction industry resulted in a response from Government in the form of a signed agreement with the Russian Federation (Oz 2001).

During economic recessions the rhetorical question facing governments is; whether to spend your way out of recession or to implement acute austerity measures? Increased spending in the form of expansionary fiscal policy entails a Keynesian approach, while implementing acute austerity measures and shifting towards a balanced budget, encompasses a more neoclassical type approach. Between 2010 and 2013, military style austerity was the choice in Ireland, with spending on public works decreasing by 63%, while in the UK, less rigid budget cuts resulted in a spending decrease of 15%. This corresponds with economic theory, whereby contractionary budgets lead to economic and employment contraction. During the recession period 2007 - 2013, construction output in Ireland contracted by a staggering 79%; from €38.6bn to €8.25bn. In contrast, construction output in the UK contracted by just 5%; from £127bn to £121.1bn over the same period. Evidently, the severe reduction in spending on public works in Ireland has had a detrimental effect on the industry as a whole, however the effect on the UK construction industry was less prominent. As reported earlier, there is also an inherent risk in using the construction industry as a vehicle for economic growth. During the mid 1980s recession in Singapore the government increased expenditure by 5% on public sector works which conversely caused construction output to fall by almost 12% (Ofori 1993a). Economists will always generally disagree on whether government should use spending on public works to regulate the economy, or not. Furthermore, a consequence of low level spending during the six year recession period, particularly in the case of Ireland, is that there will be clear shortages and needs for public construction work, e.g social housing, viable transportation networks, and renewable energy schemes.

CONCLUSIONS

It is recognised that the government and its bodies play a major role in the behaviour and structure of the construction industry; particularly in times of recession. This paper has reviewed various construction related strategies and policies employed by the Irish and UK Governments during the recession period 2007-2013 under a construction industry development framework. Furthermore, this results in the development of a taxonomy of government strategies and policies, contrasting both Ireland and the UK. The results reveal serious problems with the national strategic plan for the Irish construction industry, given that there is no overseeing body or target dates for implementation of the proposed actions. Furthermore, both countries failed to prioritize the proposed key actions within their strategic plans. There is cause for concern for both countries regarding the lack of appreciation by government of the importance of timely decisions during recession. Also of particular concern are the ramifications of low level spending during the recession period, particularly relating to Ireland, given that there will be clear shortages and needs for public construction work.

The proposed taxonomy developed will aid policy makers and company executives in mapping out future strategic milestones, while also providing a valuable source of reference, especially during times of economic turbulence. It also provides a platform for academic researchers where the study could be used to investigate the effect of exogenous factors on the strategies adopted by construction firms during the recession.

REFERENCES

- Blinder, S A (2006) The case against the case against discretionary fiscal policy. In: Kopcke, R W, Tootell, G M B and Triest, R K (eds.) *"The Macroeconomics of Fiscal Policy"*. Cambridge: MIT Press.
- Chiang, Y H, Tang, B S and Leung, W Y (2001) Market structure of the construction industry in Hong Kong. *"Construction Management and Economics"*, 19(7), 675-687.
- Chiang, Y H, Anson, M and Raftery, J (2004) *"The Construction Sector in Asian Economies"*. London: Spon Press.
- CIF (2012) *"CIF black economy survey 2012"*. available at: <http://bit.ly/1ohMW3j> (accessed 2 July 2014).
- CII and Sharma, S (2004) Australia. In: Y. H. Chiang, M. Anson & J. Raftery, (eds.) *"The Construction Sector in Asian Economies"*. London: Spon Press.
- Claessens, S, Kose, M A and Terrones, M E (2009) What happens during recessions, crunches and busts? *"Economic Policy"*, 24(60), 653-700.
- Cuadra, G, Sanchez, J M and Sapriza H (2010) Fiscal policy and default risk in emerging markets. *"Review of Economic Dynamics"*, 13(2), 452-469.
- Department for Communities and Local Government (2011) *"A plain English guide to the Localism Act"*. London: Crown.
- Department for Communities and Local Government (2013) *"Reviewing the nationally significant infrastructure planning regime"*. London: Crown.
- Department of Public Expenditure and Reform (2011) *"Infrastructure and Capital Investment 2012-16: Medium term Exchequer Framework"*. Dublin: DPER.
- Egan, J (1998) *"Rethinking Construction, Construction task force report for department of the environment, transport and the regions"*. London: HMSO.
- Enterprise Ireland (2009) *"2009 Press Releases"*. available at: <http://bit.ly/1qODpmT> (accessed 2 April 2014).
- Enterprise Ireland (2014) *"Funding: support and programmes"*. available at: <http://bit.ly/1m6MN3Y> (accessed 2 April 2014).
- Federal Reserve (2012) *"What is the difference between monetary policy and fiscal policy, and how are they related?"*. available at: <http://1.usa.gov/1mrtO6a> (accessed 22 January 2014).
- Forfas (2013) *"Ireland's Construction Sector: Outlook and Strategic Plan to 2015"*. Dublin: Forfas.
- Fox, P and Skitmore, R M (2007) Factors facilitating construction industry development. *"Building Research & Information"*, 35(2), 178-188.
- Government of Ireland (2008) *"Public Capital Programme 2008"*. Dublin: Stationery Office.
- Hillebrandt, P M (1984) *"Analysis of the British Construction Industry"*. London: Macmillan.
- Hillebrandt, P M, Cannon, J and Lansley, P (1995) *"The construction company in and out of recession"*. London: Macmillan.
- HM Government (2013) *"Construction 2025"*. London: Crown.
- HM Treasury (2010-2013) *"National Infrastructure Plan 2010, 2011, 2012, 2013"*. London: Crown.
- HM Treasury (2013) *"National Infrastructure Plan 2013"*. London: Crown.

- HM Treasury (2014) *"Infrastructure UK"*. available at: <http://bit.ly/1mid1IQ> (accessed 31 March 2014).
- Independent (2012) *"Sisk partners €50m action over Polish motorway dispute"*. available at: <http://bit.ly/1jPLt1F> (accessed 2 July 2014).
- Kang, J (2006) *"Strategic analysis of large local construction companies in China"*, PhD thesis, Nanyang Technological University, Singapore.
- Knoop, T A (2010) *"Recessions and Depressions"*. 2 ed. California: ABC CLIO.
- Krugman, P (2009) *"How did economists get it so wrong?"*. available at: <http://nyti.ms/1h1HeQG> (accessed 30 June 2014).
- Latham, M (1994) *"Constructing the team, final report of the Government/Industry review of procurement and contractual arrangements in the UK construction industry"*. London: HMSO.
- Ng, S T, Fan, R C, Wong, J M W, Chan, A P C, Chiang, Y H, Lam, P T I and Kumaraswamy, M (2009) Coping with structural change in construction: experiences gained from advanced economies. *"Construction Management and Economics"*, **27**(2), 165-180.
- Office for National Statistics (2014) *"Output in the Construction Industry, February 2014"*, available at: <http://bit.ly/1ouwChb> (accessed 13 April 2014).
- Ofori, G (1988) Construction industry and economic growth in Singapore. *"Construction Management and Economics"*, **6**(1), 57-70.
- Ofori, G (1993a) *"Managing Construction Industry Development"*. Singapore: Singapore University Press.
- Ofori, G (1993b) Research on construction industry development at the crossroads. *"Construction Management and Economics"*, **11**(3), 175-185.
- Oz, O (2001) Sources of competitive advantage of Turkish construction companies in international markets. *"Construction Management and Economics"*, **19**(2), 135-144.
- Revenue (2014) *"VAT Rates"*, available at: <http://bit.ly/1kbBaor> (accessed 1 April 2014).
- Turin, D A (1973) *"The construction industry: Its economic significance and its role in development"*. 2ed. London: University College Environmental Research Group.
- UK Government (2013) *"GOV.UK"*. available at: <http://bit.ly/1gSTfoJ> (accessed 20 March 2014).
- UK Government (2009 - 2013) *"GOV.UK"*. available at: <http://bit.ly/V9x4rm> (accessed 19 March 2014).
- UK Trade and Investment (2014) *"High Value Opportunities (HVO) Programme"*. available at: <http://bit.ly/1sgKxH3> (accessed 2 April 2014).