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Getting on with the unfinished work

For the past five years or so, banks around the world have effectively been passing around envelopes with $1 million written on the front. Sadly, when opened, these have proved to contain nothing more than a grubby, well-fingered fiver and the world's economies have spun into a nosedive as a result.

Here in New Zealand we have been sheltered from the worst of the blows, but the new economic realities mean that there are inevitable savings that have to be made. So where does this leave infrastructure investment? Is it something to be deferred? Or is infrastructure spending – specifically by local councils – a way to prime the pumps and get the national economy motoring again?

Contractors' Federation CEO Richard Michaels believes that, while the coming year will be tough, there are positives.

"It looks like the infrastructure industry will fare a bit better than some other sectors," he said.

"The government wants to up the infrastructure spend on top of what has already been signalled, so that will go some way towards keeping the wolf from the door."

However, he predicts the local government sector will be tight and deferral of maintenance and construction should not be the first option.

"Councils have tightened up. Many of them are elected on low rate-rise tickets, but if you want to keep rates low, you can't keep up with infrastructure maintenance in a zero rate-rise environment.

"Some councils are keeping money earmarked for depreciation and using it to service debt and that is having a marked effect on the industry. I believe it's a short-sighted view and I think it's unfortunate that some councillors are more worried about ▷ re-election than about taking the long-term view."

He said that the underlying drivers of our economy were still strong and while commodity prices have fallen, they have fallen from historic highs.

"As a small exporting nation, we rely on the strength of other economies. Their bailouts will benefit us and there are a lot of positives over the coming year. By the middle of the year, I think people should be a bit more confident."

The immediate pain is a result of missed opportunities and failing to capitalise on the chances that the past five years of booming economic times brought.

"We have been through a quite profligate period of credit creation and that will take time to work through. However, there is still money out there and the people with that money will be looking for good places to invest it down the track. If a fraction of the money

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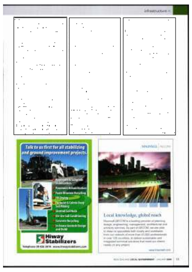

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Page 9 ▷ made in the last five years had been invested in productive companies rather than in financial markets, we'd be in a much better situation. That said, a lot of people are a lot better off than five years ago."

The government will have to take a leadership role in the coming months to stave off a deeper recession and to kick-start economic activity and confidence.

"I'd like to see the government keep its promise to invest in infrastructure.

"A review of the RMA would also have a benefit for all of us and some review of local government is also overdue. If the Royal Commission on Auckland brings change then I think that should be looked at on a national level so we can have standardised planning rules around the country."

Opus CEO Kevin Thompson says the situation is not all doom and gloom, but that there needs to be effective partnership between central and local government.

"If you're going to use infrastructure as an economic catalyst then that money has to come from central government. But it needs to be locally based and local government is an ideal partner. No other set of agencies is as equipped to manage and facilitate that," he said.

"It's well-known that pretty much all of the utilities are under capacity – there is not enough infrastructure to have an effective economy. There is a lot of physical work to be done."

Mr Thompson said that deferring capital works projects was not the answer and would merely result in higher end costs. Councils wishing to keep rates down by putting off infrastructure projects were creating false economies.

"Cost increases for infrastructure have climbed higher than the CPI on the back of very, very big demand. China was lifting the world prices for cement and steel on its own and that has been reflected here. Labour costs also rose. So the local government sector was paying higher costs and consequently rates were going higher than the CPI and people started to get worried about that.

"Central government will need to look at where the funding sources are and what is now available. There was a view that the public purse couldn't afford it, so do we look at increasing public debt? Or do we bring in the private sector?"

MWH's strategy leader for New Zealand Alan Hulley believes that central government has accepted that infrastructure spending is essential and he says that the beneficiaries of that should be local government.

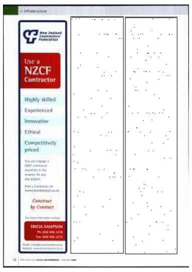
"I think the government has recognised that our infrastructure is not what it should be and wants to rectify that," he says.

"If the work needs doing – work that is decades long, rather than short-term projects – then local authorities are a good avenue to get money back into the economy."

However, he believes that excessive caution could be a stumbling block for the consultancy and contracting industries.

"Councils are being pressured on rates, despite there being a backlog of infrastructure spending and I suspect they are also feeling pressure from reduced development contribution projections, so there is pressure coming from two sides on the revenue stream.

"One concern I have is that when faced with that dilemma councils decide to batten down the hatches. The consultancy and contracting industries have put in a lot of work into building capacity, especially through recruitment. If the work dries up, perhaps we might not be able to get people Page 12 ▷



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Page 11 ▷ back when we need them in the future."

GHD's Barry Potter says that infrastructure investment is not simply a means of lessening the impact of the current recession, but it also represents a long-term commitment to the country.

"It does address short-term issues as well, but infrastructure investment is an investment in the future of the country. There is a link between infrastructure development and the long-term development of the country.

"New Zealand has a history of cutting back on investment in tough economic times and we've slid backwards as a result. It is going to be a tougher year ahead than we've seen for seven years or so, but it also a great opportunity to address issues that have held us back."

He believes there needs to be more innovative thinking around how infrastructure development is funded and implemented, saying that PPPs and alliancing offer good opportunities.

"It needs innovative and courageous thinking. When you look at the return on investment on infrastructure, it's a no-brainer really."

Beca's Robert Jamieson agrees that the private sector has to come in and that private-public partnerships are a useful option.

"It's a mechanism that hasn't been explored in New Zealand. Investors are looking for a safe haven for their money and what you need is almost a case where revenue streams to fund development in the private sector is guaranteed by the government," he said.

"With a National-led government, I think there is more acceptance of PPPs. While not all projects can be done that way one would hope the government would at least put them on the list of options."

Mr Jamieson is picking a tough first half of 2009, and he hopes the government works quickly.

"It will take six months to work out how much money is available for infrastructure and new projects in the pipeline will be delayed to some degree; to what extent will depend on the government's investment in infrastructure."

Extended investment is another option, spreading the cost of projects over several years instead of coming out of one annual budget.

"At the moment the current-year tax take funds infrastructure development and there is no attempt to roll the cost over 20 or 30 years. In Australia and the UK they use a 20-30 year time horizon to cashflow a project. That does provide a contingent liability over that time, but the governments bank on increasing the tax take over the time period," he said.

Tony McCartney, Duffill Watts' local government director, is a bit more pessimistic about government action to boost infrastructure spending.

"All the theories say that infrastructure projects are a good way to keep people employed; but while there has been a lot of rhetoric, there is little actually happening.

"Central government is talking a lot about spending, but the size and scale of that spend means there will be a nine- to 12-months' lead-in period before anything happens. That will only help those firms already involved in projects; there won't be an equitable share-out of the spend and some firms will drop off. On the contracting side, there are some big concerns there."

He says that the worrying thing about a downturn in infrastructure projects is the effect it will have on staff in an environment where there has been no let-up in the recruitment pressures facing many companies.

"We will start losing people to Australia, where there is a bigger buffer against recession. And then when the work does come in there won't be the people here to do that work.

"It's not all doom and gloom, but it is a potentially recessive time."

He shares the concerns about deferral of construction projects in order to reduce the rates burden on people at a time of economic uncertainty.

"I don't think councils should be deferring projects, it's the wrong call; in fact they should bring them forward to take advantage of better prices and lower costs now. There is more need for councils and industry to work together to get on with work and councils should be trying to fast-track investment.

"I think the government has been sitting on its hands. Since Christmas we haven't seen much action and if we don't spark up and get busy now it's going to be a lousy winter. I believe there are opportunities for local and central government to work together on projects such as regional water issues for example. Big infrastructure projects on a regional basis and tap the Cullen Fund to pay for it. I also think local government should undertake more partnering solutions. This would allow more inventive funding options whilst keeping people busy."