Construction Business Recovery

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Review of the news

There is a distinct lack of good news in the construction and property markets at the moment - sales values continue to drop in many sectors and businesses are forced to cut costs to ensure their survival. For those people working in the industry during the recession of the early 1990s, there is, no doubt, a certain feeling of déjà vu…

> "*History doesn't repeat itself, but it does rhyme"* Mark Twain

Suffice to say that there is no need to dwell on the negatives here. Most construction and financial journalists and commentators are doing a sterling job in this respect. Sticking to the themes, however, of dropping sales values on the one hand and the cutting of costs on the other, this edition of Recovery News briefly seeks to discuss two questions in headline detail:

1) What effect is the Credit Crunch having on construction costs? This is especially relevant where a contributing factor to project distress *may be* contractor insolvency, with the result that packages / contracts may need to be re-let or renegotiated.

2) What will happen if my client (the funder) decides to cut its losses by taking control of their secured assets and "fire selling" these to recover their exposure.

These are especially pertinent considerations from a CBR Project Audit perspective.

Construction Costs: The Market Signals

It's fair to say that market conditions are not uniform. Some contractors that have solid order books are too busy to tender, but others are seeking work.

Overheads and profits are being trimmed and two-stage tenders are attracting figures of 2-4%. There is also a clear move back in the direction of single-stage tendering. More contractors are pricing competitively, and some clients are opting for construction management.

Preliminaries costs are now also being examined closely, but there have been increases in the cost of insurance, bank bonds and warranties in the wake of new financial world in which we find ourselves.

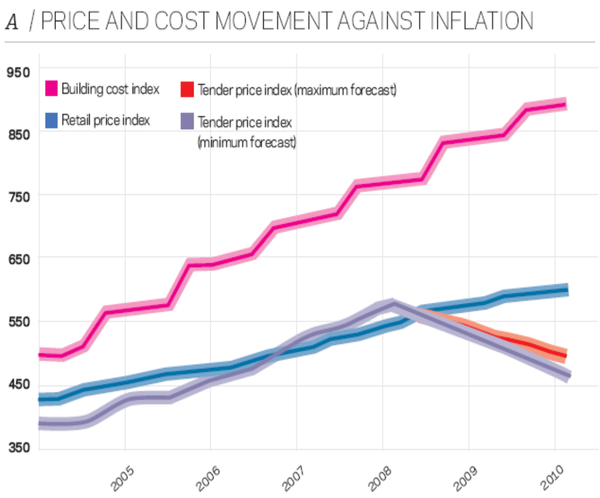
Subcontractors in trades such as concrete frames and curtain walling, who six months ago were dictating terms and conditions, are now more willing to negotiate sensibly. Staff and labour shortages have eased despite the reports of Eastern European workers returning home.

Tender price index

The third quarter of 2008 saw building prices in Greater London slip back by 1%. This looks like the start of a downward trend as work dries up, labour becomes abundant and materials costs drop. Prices are forecast to fall 5-7% next year and further the following year.

Building cost index

The building cost index rose to an inflation level of 6.8% in the third quarter 2008, reflecting record materials price rises in the first half of the year and a significant wage award at the end of June.



Funders and Secured Assets

The appeal in the case of Wilson v Dunbar Bank plc reminds lenders that they must observe the relevant statutory procedures to obtain the best price for properties which they have repossessed.

The salient facts:

Mr Wilson had carried out a development of 6 flats at Fernieside Avenue, Edinburgh with financial assistance from the Bank, but could not repay the debt and so the Bank called up its security and took possession of the development. The Bank employed marketing agents and ultimately agreed to sell the flats to an investor as one lot and retained the full proceeds from the sale.

Mr Wilson sued the Bank for damages claiming that if the flats had been sold individually, there would have been money left over from the proceeds for him. He claimed that the Bank had failed in its duty under the legislation to sell the flats at the best price that could reasonably have been obtained.

The decision:

The Court found in favour of Mr Wilson and noted that the efforts to market the properties "fell well below what would be expected of the reasonably competent surveyor." The Court however went on to say that "in the circumstances it was for the Bank to satisfy themselves that reasonable steps had been taken to ensure that the best price that could be reasonably obtained had been obtained. They failed to do so".

Conclusion:

The case law illustrates how each case will be decided on the facts and circumstances of the assets concerned as well as the type of security involved. It was held, for example, in a recent English case that the receiver had carried out his duty to obtain the best price that was reasonably obtainable in the open market by selling the properties secured as a portfolio instead of selling them individually. The case law also highlights that a lender cannot necessarily rely on agents having done their job. The lender must be satisfied that the job has not only been done but been done properly

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