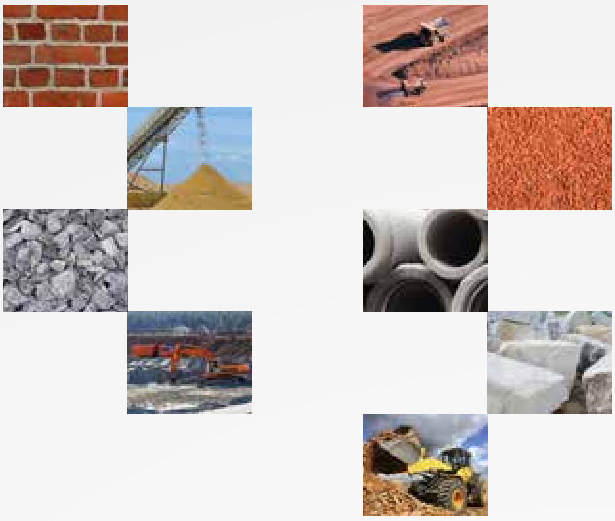
Competitive Analysis of the Construction Materials Sector on the Island of Ireland - an Update

November 2015



Irish Concrete Federation — Set for life

QPA Northern Ireland — Providing Essential Materials

InterTradeIreland — Discover what's possible

Prepared by Irida Consulting Limited for the
Irish Concrete Federation and Quarry Products Association Northern Ireland

Contents

Foreword

In 2012 InterTradeIreland, the Irish Concrete Federation and the Quarry Products Association of Northern Ireland published a competitive analysis of the construction materials sector on the island of Ireland. The report articulated a vision for the sector based on a combination of strong management capability, efficient use of resources/capacity, product quality and innovation. This report updates that research.

The construction materials sector reviewed in this report comprises the stone, sand, aggregates, readymix concrete, concrete products and bitumen products that form a critical part of our built infrastructure. The construction materials sector is a strategically important one, as without its products, our built environment would simply not exist in its present form. Despite the need for its output; the sector is not a significant contributor to building costs. Concrete products and stone account for less than 5% of the costs of a new house.

Concrete and stone is delivered to building sites and so transport is a relatively high proportion of operating costs. Ready mix concrete has a very short usable life after mixing, so the distance from a plant to a building site must be relatively short. Consequently, the industry comprises many plants distributed across the island.

Given the distributed nature of the industry, two economic conditions are essential for its continuance. First, construction activity should be at a reasonably sustainable level and, second, this sustainable level should be evident in all parts of the island.

These two circumstances are not being met on the island today. Construction activity is just half of what it should be in a normal economy and, furthermore, the growth in activity in recent years has been focused on the two major urban centres of Dublin and Belfast. Outside of these centres many companies are under extreme pressures; have scaled back operations significantly, and are unable to retain experienced staff.

For a sustainable future, the Governments on the island need to appreciate the strategic importance of the construction materials sector; to support it by addressing the island's infrastructural needs and making sustainable levels of capital investment in new projects together with appropriate levels of maintenance on existing and newly built infrastructure. From local authorities and Government agencies, there is a need for much improved enforcement of the regulations affecting the sector, particularly in the areas of planning regulation; product specification in construction contracts and improved monitoring of construction materials provided.

We recognise the contribution of the industrial development and promotional agencies in Northern Ireland and Ireland who have supported many companies to develop sales in Great Britain and further afield; a critical contribution to their survival. The growth of exports to Great Britain is testament to the comparative price levels – Irish product prices are lower than their British counterparts.

The industry itself has contributed much through rationalisation; cost reduction; plant closures and reinvestment of financial reserves to keep businesses in existence. Critically, it needs a more normal business environment, supported by Government investment in infrastructure and housing; coupled with reasonable levels of regulatory enforcement, to underpin a competitive recovery.

1 Introduction

In 2012, InterTradeIreland, in cooperation with Invest Northern Ireland, Enterprise Ireland, and the key industry representative bodies (Quarry Products Association NI, the Irish Concrete Federation and the Irish Asphalt Pavement Producers' Association) published a research report[1] analysing the capacity and capability of the construction materials sector within the island of Ireland and identifying options and opportunities open to the sector.

The objective of the study was to assist recovery in the construction materials sector through a series of practical recommendations and options for tackling capacity issues and improving competitiveness within the construction materials sector.

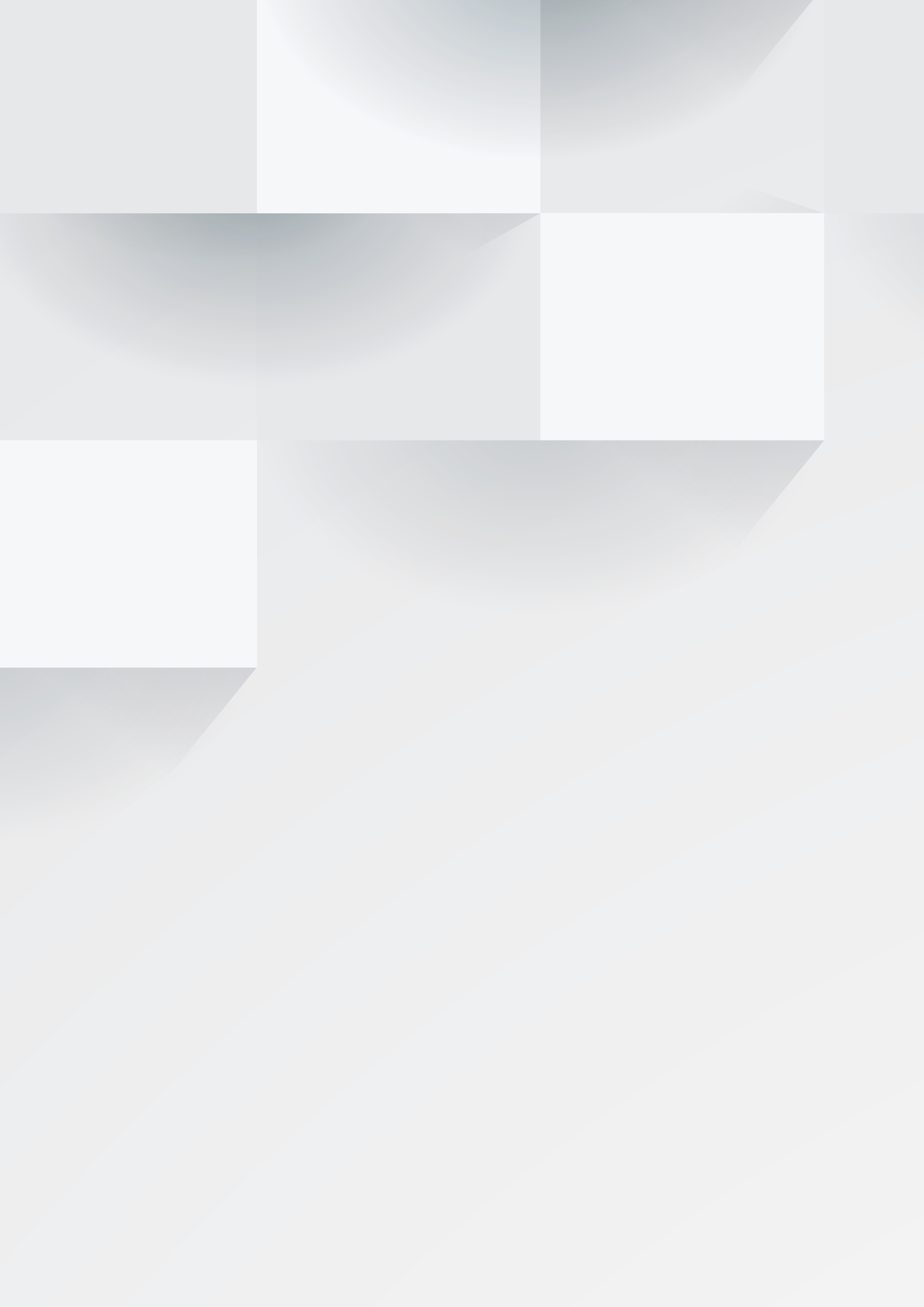
The outputs included:

- An analysis of the options and possible solutions facing the sector which drew on consultation with industry players and other representatives and stakeholders.
- A baseline analysis of the sector, in terms of its output, capacity and capabilities; and
- An outline of the changing nature of the markets (on and off the island) for construction materials and the opportunities and threats that this will entail for the sector.

The report contained a series of recommendations aimed at addressing these areas.

The key industry representative bodies (Quarry Products Association NI and the Irish Concrete Federation) have now commissioned Tony O'Brien of Irida Consulting Limited to provide an update on developments and the progress made since the publication of the previous InterTradeIreland report and to recommend where future action should be directed.

1 InterTradeIreland, *Competitive analysis of the Construction Materials sector on the island of Ireland* (May 2012).



2. Executive Summary

The construction materials sector is a strategically important element of the construction supply chain. It provides a range of basic materials such as stone and aggregates and a range of concrete products, including readymix concrete, blocks and precast concrete elements.

2.1 Overview

The Construction Materials Sector

The construction materials sector is a strategically important element of the construction supply chain. It provides a range of basic materials such as stone and aggregates and a range of concrete products, including readymix concrete, blocks and precast concrete elements.

Capacity utilisation

The 2012 InterTradeIreland report found that capacity utilisation in the sector was as follows;

Table 4.3: Estimated All-Ireland Capacity - 2012

Product	RoI Capacity	NI Capacity	Total	Current Output	Capacity Utilisation %
Readymix Concrete - 000s m^3	8,960	3,000	11,960	3,200	27%
Aggregates - millions tonnes	123	32	155	41	26%
Precast concrete - €millions	289	145	434	175	40%
Asphalt - millions tonnes	7.0	4.0	11.0	4.8	44%

Source: InterTradeIreland

From our consultations we conclude that the current level of sector capacity utilisation remains broadly similar in 2015. There has been some reduction in the number of operating facilities across the island; however, as these could be re-opened relatively easily and the capacity still remains, though operational efficiency has improved.

Market demand

There has been some growth in construction output and market demand across the island in the recent past but this has been in specific geographic areas. Official data show that construction industry output in volume terms has fallen in Northern Ireland but has grown by small amounts in the Republic. However, industry sources say that the increases in activity are concentrated in and around the two major cities – Dublin and Belfast – and are not evident in many parts of the island. Total market demand remains substantially below what is regarded as a normal level of activity.

Employment

Employment in the construction materials sector had fallen from some 20,000 people within the island of Ireland in 2007 to some 7,700 people in 2012 – a reduction of 62% from the peak. It is judged by the industry that employment levels have not changed to any significant extent and many in the industry are providing employment on a "short week" – i.e. 3 days per week – or temporary basis.

Financial Performance

The 2012 report included a survey of twenty companies across the island that showed 65% of the companies incurring losses. It has not been possible to replicate that survey as a number of the companies have either closed or undergone substantial change. These companies were amongst the weaker or most at risk in the original sample. A review of the original sample companies whose financial statements were available suggest that these closures and corporate changes have led to some improvement in the sector's financial performance – however, it must be stressed that this improvement is due more to rationalisation and corporate action than any market uplift.

2.2 Future Prospects for the Industry

Construction industry activity in the island is currently about half the size it should be in a normal economy. While economic indicators generally suggest that economic growth should be reasonably strong in the near future, housing output is far below what is needed across the island; infrastructure spending is very low and the EU supported Rural Development Programme is getting under way slowly.

Economic forecasts predict growth in future years – the Irish Central Bank's most recent Quarterly Bulletin projects construction volume growth in excess of 8% for 2015 and 2016. The Construction Skills Network forecasts average annual growth in Northern Ireland construction of 2.2% over the period 2015 to 2019. The consultees in the review see significant potential for growth, but the lack of impetus both North and South in increasing public sector investment throws doubt on when the promised uplift will actually materialise. It is felt that any short term growth in construction demand is dependent primarily on the private sector.

2.3 Challenges Facing the Industry

Capacity

This current assessment concludes that some 35% of existing production plant capacity can be defined as structural over-capacity; broadly similar, though marginally smaller than the 37% identified in the 2012 report. There have been improvements in operations efficiencies since that report; including for example, sharing of transport and some manufacturing capacity, and in overall terms, the financial performance of companies within the construction materials sector has shown some improvement, but this appears to be due more to rationalisation and closure than improved in market conditions. An industry over-capacity issue remains.

Opportunity in the sector

Construction materials suppliers are very largely dependent on local markets. However, a number of companies across the island have developed markets in Great Britain for stone and precast concrete products. The development of off-island markets has been important for a number of companies in the sector.

These companies' competitive advantage is attributed to the relatively low cost of basic materials in Ireland compared to Great Britain. High transport costs relative to the value of product being shipped preclude these companies from trading in markets further afield.

Regulation and Enforcement

A key challenge facing the sector is competition from unauthorised, non-compliant operators. This affects all parts of the island, though the issue seems more serious in the Republic. Product standards; planning compliance and quality assurance requirements exist in the industry and the cost of meeting the relevant standards – the cost of compliance – is estimated at being between 10% and 15% of the selling price of the various materials.

Our consultations within the industry suggest that non-compliant operators benefit from:

- A price advantage of at least 10% to 15%;
- Failure on the part of some specifiers to refer to the relevant standards in contract documentation;
- Failure on the part of some public bodies and developers to audit the materials used by contractors; and
- Failure on the part of some local authorities to take enforcement proceedings against non-compliant operators.

This issue appears to have been addressed to a far greater extent in Northern Ireland than in the Republic. In the absence of enforcement, there is little the industry itself can do in addressing this issue.

Profitability and Scope for Future Investment

Prices within the island are widely regarded as unsustainable in the long run. Low prices are attributed to the current low level of demand coupled with the impact of non-compliant operators. Relative to Great Britain, prices in Ireland are extremely low; this is partly attributable to the high cost of aggregates in Britain. Concerns have been expressed within the industry and by customers that at current price levels, insufficient profits are being made to give reasonable assurance that future investment - such as opening new quarries or expanding distribution fleets - will be possible. A high cost construction materials environment, comparable to that in Britain, could develop in Ireland unless the issues of low market demand and non-compliant operators are addressed.

Skills

Employment in the sector has fallen substantially from its peak; many young qualified people have left both the sector and the island and concern is expressed regarding an emerging skills shortage; especially at craft, technical and professional staff levels. The age profile of the sector is a concern; attracting and retaining good new staff is difficult and while training in some areas such as management and safety is on-going, technical skill shortages may hamper future development in the event of a market upturn.

Roles of the State and its Agencies

A conclusion of the 2012 report was that Governments could address national infrastructure needs and at the same time assist the construction materials sector by ensuring appropriate levels of investment in new projects, along with appropriate levels of maintenance on existing infrastructure. The expressed view that this would help to support a strategically important sector; to maintain jobs; retain existing skills and ensure that a competitive construction materials sector remains in existence when the economies of the island recover to more normal operating conditions remains valid today.

Local authorities can also assist the sector through improved planning for use of materials and also thorough improving planning enforcement. It is hoped that the restructuring of local authorities in Northern Ireland will provide an opportunity for the industry to get more support from local government in the area of planning enforcement.

In general the experience of those in the industry that have worked with the State development agencies has been positive, especially in the development of export markets. This view was expressed across the island. Some companies dependent on indigenous markets found that some aid programmes such as ones providing assistance with working capital were overly bureaucratic.

2.4 Recommendations

Government

1. The Governments should appreciate the strategic importance of the construction materials sector and seek to support it through addressing the island's infrastructural needs and thereby making sustainable levels of capital investment in new projects together with appropriate levels of maintenance on existing and newly built infrastructure. The fiscal and economic benefits of spending on construction can be significant, and projects where the identified fiscal and economic benefits are substantial and/or substantial private sector investment is available, should be prioritised. This recommendation was also made in the 2012 report, which suggests that little has been achieved in this regard since then.

2. We recommend that both Governments should seek a more rapid implementation of programmes such as the Rural Development Programme and sub-programmes.

3. There is scope for much improved regulation of the sector, particularly in the areas of planning enforcement; product specification in construction contracts and improved monitoring of materials provided. We recommended that Governments should encourage the relevant agencies to develop processes to enable them to act on unauthorised non-compliant operators much faster than at present. At present, by the time action is taken against such operators, projects can have completed its acquisition of basic materials and enforcement is ineffective at that stage. This issue appears to have been addressed more effectively in Northern Ireland than in the Republic.

4. Governments should implement procurement policies in all public bodies under which contracts should include conditions that all construction materials suppliers are compliant with relevant product standards and have the requisite planning approvals. Public contracts should be contested by compliant operators.

5. The Governments should institute improved contracts governing public works to reduce the risk for suppliers. For example, the use of Project Bank Accounts is being trialled in Northern Ireland, while it does not appear to be even a consideration in the Republic.

Local Authorities

6. We recommend that local authorities that have responsibility for planning enforcement and compliance with CE marking should work with the construction materials industry to seek the means to bring about improvements in enforcement where such improvements are needed. This recommendation was also made in the 2012 report. Its inclusion suggests that little, if any, progress has been made in this regard since then.

7. We recommend that local authorities should seek to manage their demand patterns to enable the materials sector to respond to demand in the most efficient manner possible. This is as made in the 2012 report and we note that in the Republic roads grant programmes incorporate a requirement to spend specific amounts of the annual road maintenance and improvement grants by the end of the summer.

Other State and Development Agencies

8. We recommend continuing liaison between the development agencies and the representative bodies to see what scope exists for supporting the sector. At present, there is a high level of satisfaction with aid provided for exporting activities. Consultation might therefore consider other forms of aid that could be provided, say for management development, in companies reliant on indigenous markets.

9. We recommend that consideration be given to an industry skills audit to see the extent and scale of prospective skills shortages in the sector and the subsequent drafting of a skills development programme.

10. We recommend that the State agencies should ensure that the interests of the construction materials sector are considered in any future strategic planning exercises carries out by them. While there are no issues that this is not being done; it should be a consideration in future planning.

The Industry

11. Four recommendations were made to companies in the sector in the 2012 report which essentially were that:

    - Companies should give consideration to upgrading management skills or systems to support the ongoing development of their business;

    - Individual companies consider the pros and cons of exiting the sector; and the costs of staying in business versus the long term payback that may accrue when the economy improves.

- If the use of financial reserves to keep a business in operation does not provide an acceptable return or payback; the owners/directors should consider the potential for bringing about a reduction in costs through operating or specialisation agreements with other companies in the sector.

- Finally, if some form of corporate action such as examinership or liquidation is inevitable, companies should take a proactive approach and seek to maintain as much control as possible over their own destinies.

These recommendations remain valid for the sector, even though some improvement has taken place in terms of operations rationalisation and co-operation in the use of transport and production facilities. Given the uncertainty regarding the emergence or – more specifically – the timing of the emergence of substantive demand of the industry, further opportunities for co-operation should be pursued.

Financial pressures appear to have abated somewhat, though this is possibly due more to some company closures and action on the part of some companies in the sector to rationalise and restructure. For some individual companies, the recommendations remain valid.

12. The industry should make stronger representation to customers and specifiers to ensure that construction materials used on building works should comply with all relevant regulatory requirements and that an audit trail should be a requirement of all construction works to ensure that only compliant materials are used.

3. Methodology

This report contains the findings of the desk research carried out; industry consultations and consideration of the factors affecting the construction materials sector as whole within the island of Ireland. One constraint on this is that as Northern Ireland is a region within the United Kingdom; data relevant to the region alone is not available in some cases.

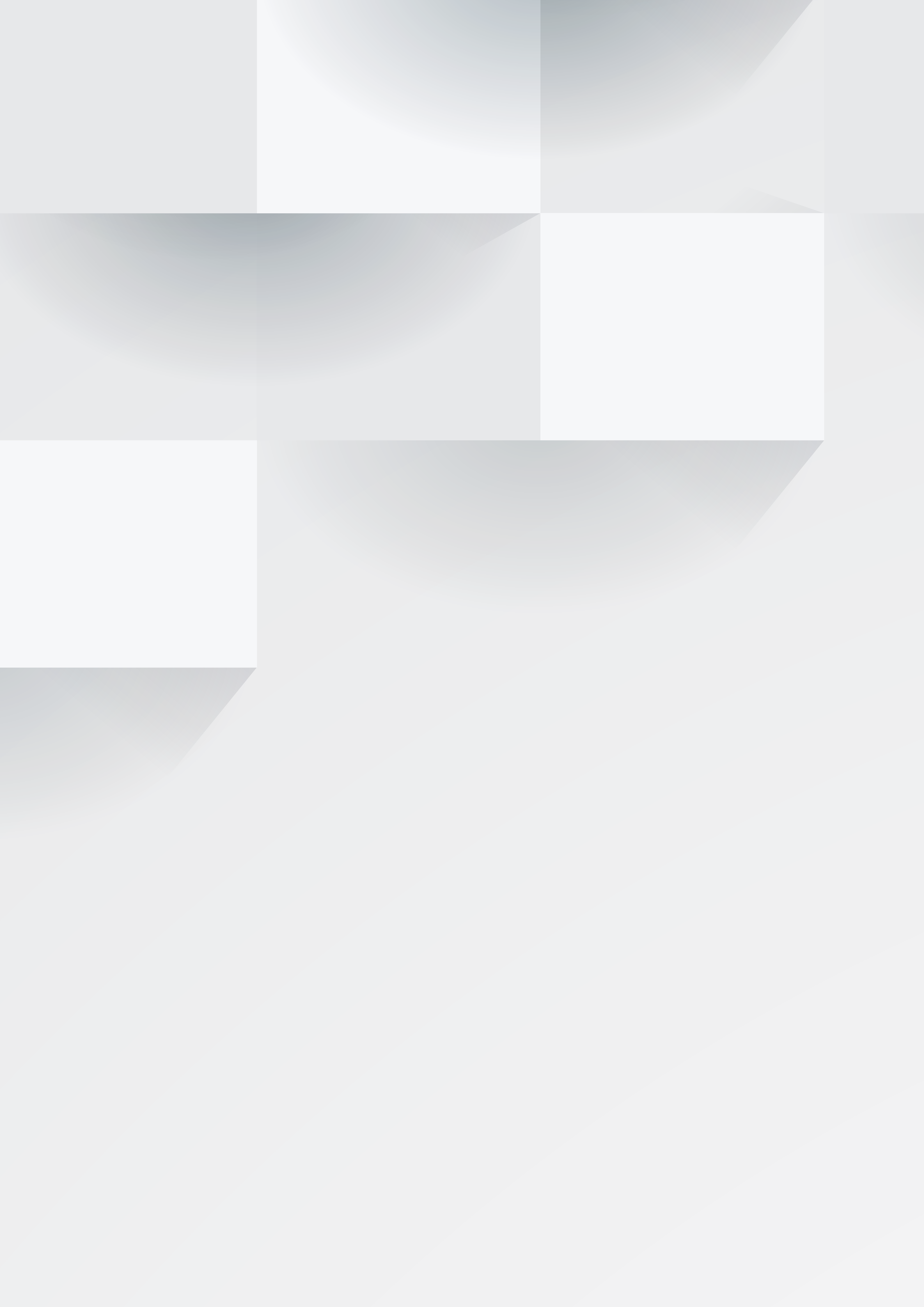
In the Republic of Ireland, the key data sources were the Central Statistics Office; the Department of the Environment, Community and Local Government; the Housing Agency; the Central Bank and individual providers of research and opinion.

In Northern Ireland, statistical data are also provided by a range of Government sources, including the Department of Enterprise, Trade and Investment; the Office for National Statistics and the Department for Social Development and the Department of Agriculture and Rural Development.

We carried out a summary financial analysis based on financial statements of a sample of companies as lodged with the relevant companies' office.

We have relied on industry consultations to assist us in reaching reasonable conclusions, however, again, there is little available in terms of up-to-date survey data on the product sectors. Our consultations included over twenty individuals in companies in the sector; customers of the sector; government agencies and financial institutions.

We wish to thank all those in the industry; in the State agencies; suppliers and financial institutions who met with us.



4. Construction Sector Review and Outlook

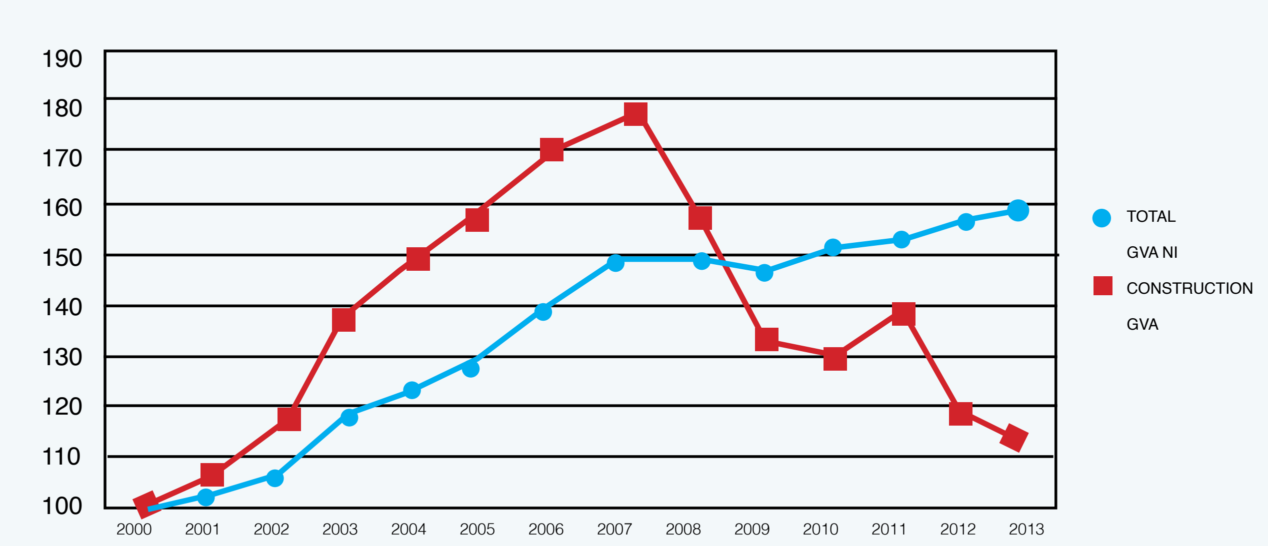
This chapter summarises the performance of the construction industry in the island of Ireland over the past three years, and aims to put that performance in the context of the broader macroeconomic environment.

4.1 Northern Ireland - Macroeconomic Context

Chart 4.1 shows that GVA[2] in Northern Ireland rose steadily from 2000 to 2008, before falling by some 2% in 2009. It recovered marginally in 2010 and has continued to grow modestly since then. (2013 is the latest year for which data are available.) While construction GVA rose faster than the overall regional GVA from 2000 to 2007; since then it has lagged substantially and by 2013 output in the sector had fallen to 2002 levels.

NISRA data show that in volume terms, construction output in 2014 is down marginally on 2013; the fall being just under 1%. In value terms, construction output in 2014 was up by some 2% on 2013. The data show that output was particularly strong in quarter 4 of 2014; the highest since Q1 of 2013.

Chart 4.1: NORTHERN IRELAND - OVERALL AND CONSTRUCTION GVA, 2000-2013



Source: Derived from Northern Ireland Construction Bulletin; shown at constant 2011 prices

2 Gross Value Added (GVA) is used to measure the value of goods and services produced in a region of an economy. Northern Ireland is a region within the United Kingdom; therefore GVA is used as a measure of its output. The Republic of Ireland, being a State, uses Gross Domestic Product (GDP) as the measure of national output. 2013 is the latest annual data available at the time of drafting of this report.

The volume trends in Northern Ireland construction are examined in Table 4.1 which shows the rates of growth and decline on a sectoral output basis. The table shows construction output at constant 2011 prices and therefore represents the volume of activity taking place.

Table 4.1: Northern Ireland - Construction Output by Sector at Constant Prices

Housing	Infrastructure	Other Public	Industrial/ Commercial	R & M	Total
1,444	428	421	575	660	3,528
875	422	355	328	640	2,620
527	406	254	218	617	2,022
477	348	323	246	616	2,010

Source: Derived from Northern Ireland Construction Bulletin; shown at constant 2011 prices

Since 2010, the key sectors have been housing, which has seen a reduction in output of 45%; Industrial/Commercial, which has seen a reduction of 25% and infrastructure, which has fallen by 18% in volume terms. However, Industrial/ Commercial has been increasing in 2014 after a serious fall in 2013 and there has been a similar pattern with public building, i.e. non-infrastructure, works. Repair and maintenance works have remained at a fairly constant level.

The relative importance of the different market segments has changed significantly. Housing accounted for 39% of construction activity in 2000, but this has fallen to 24% in 2014. On the other hand, Repair & Maintenance has grown from 17% of the market to 31%; while infrastructure has doubled in relative importance, from 8% of output in 2000 to 16%/17% in recent years. This Repair & Maintenance segment is not as construction materials intensive as housing or infrastructure and so the construction materials suppliers tend to lose volume disproportionally as the share of different market segments shift as they have done.

A key development has been the extent of growth in reliance on public sector expenditure in Northern Ireland. From 2000 to 2007, the public sector accounted for some 40% of total construction activity. Since 2007, reliance on the public grew to 59% in 2013 and this has slipped back to 56% in 2014. Clearly, Government budget decisions are a major factor for the industry at present.

Construction industry data published by NISRA shows that the scale of the decline in activity in recent years has been moderated to some extent by higher values in the work done as shown in Table 4.2.

Table 4.2: Northern Ireland Construction Output

Northern Ireland Construction Output	Value stg£million	Volume stg£million
2011	2,295	2,295
2012	2,264	2,205
2013	2,138	2,022
2014	2,182	2,010

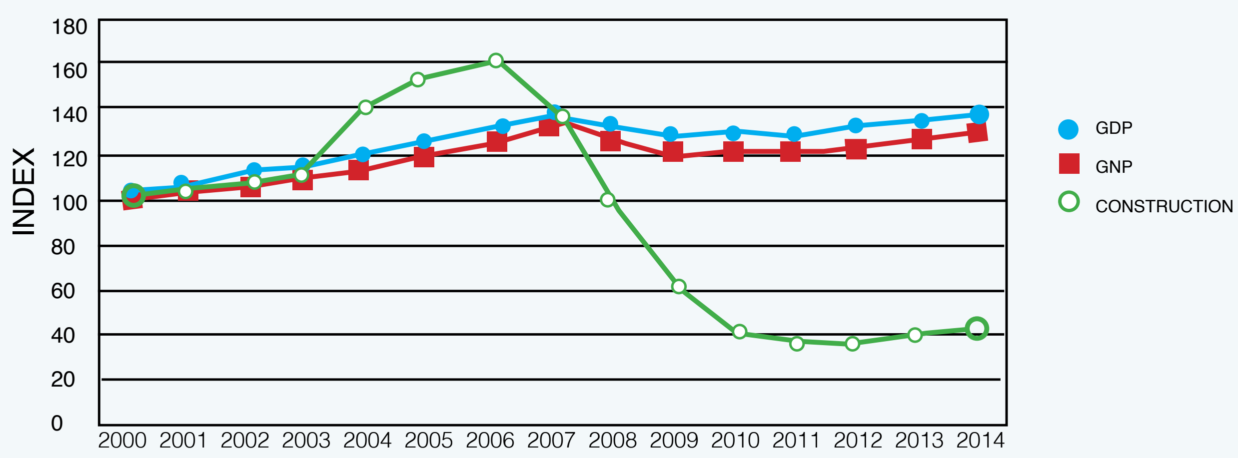
Source: NISRA. Volume is measured at 2011 prices

The decline in value terms from 2011 to 2014 is 5%; however, the volume decline – a more accurate measure of activity – was 12%. The Northern Ireland Construction Bulletin measures indices of output on a quarterly basis and in its most recent commentary it suggests that the decline in industry output may be levelling off.

4.2 Republic of Ireland - Macroeconomic Context

While Northern Ireland suffered a "construction bubble"; industry output in 2013 was still 14% ahead of 2000, though it was down some 35% from the peak output, which was in 2007. However, for the Republic, the collapse, both in comparison to 2000 and the peak output, has been much greater as can be seen in Chart 4.2.

Chart 4.2: Republic of Ireland - GNP, GDP, Construction Output, 2000 - 2014



Source: Central Statistics Office

Construction output far outstripped the economy as a whole from 2003 onwards, only to collapse in 2007. The decline was moderated to some extent by ongoing public sector works, such as motorway construction. But the rate of decline deepened as public capital expenditure was cut in 2008/2009 and the fall in industry output did not level off until 2012. There has been marginal growth since then.

In value terms, total construction output was measured at €35.489 billion in 2006[3]. Based on CSO Building Construction indices, and using 2006 as the base year, we estimate that industry output in 2014 was valued at €10.213 billion at current prices and at €9.443 billion at a constant price or volume basis.

CSO data show that the volume of output in building and construction fell by 2.6% in the first quarter of 2015 when compared with the preceding quarter. A fall of 5.6% in the volume of residential work offset increases in the civil engineering and non-residential building.

Construction employment peaked at 273,900 people in Q2 2007 and fell to 99,600 people in Q2 2012 – the quarter in which the InterTradeIreland report was published. Employment had increased by a modest 4,000 persons by Q4 2013; but during 2014 it has risen by 13,100 to 116,700 people .

To seek to understand the regional trends in construction, we examined the regional changes in employment levels and we note that of the employment created in the period 2012 to 2014, 72% was created in the regions of Dublin and the South-East. Performance was mixed elsewhere; and there was a reduction in employment in the Border region.

The recovery in construction has been led mainly by the non-residential building sector with volume output by this sector being nearly 12% higher in 2014 than in 2010. By way of contrast, residential building in 2014 was 17% lower than in 2010, but the CSO statistical data suggest a strong pickup in activity in 2014 – up 17.5% over 2013. In 2014, civil engineering output was quite similar to 2010 levels.

During our consultations, many of the views expressed questioned the accuracy of the picture described by published data. The key criticisms expressed are that the current growth in construction industry output is focused in the Dublin region and that outside the fringes of the M50 orbital route, there is little evidence of a pickup in business volumes. Indeed, outside Dublin, many firms are reliant on the agriculture sector for concrete; concrete block and aggregate sales. Many quarries have a substantial dependence on agricultural lime. Residential construction activity is very limited and mostly dependent on one-off houses; while commercial construction is generally described as inactive. The pre-cast companies are heavily dependent on export markets.

There is a unanimous view within the industry that the Irish construction market can currently be regarded as two separate regions; Dublin and the rest of the country; and that the published data, including data from non-Government sources, do not express the regional differences sufficiently and this may be having deleterious effects on public policy. Current expectations are that construction will grow by the order of 20% in the Dublin region in 2015; while activity outside Dublin is expected to remain static at best.

In broad terms, since the publication of the InterTradeIreland report in Q2 2012, official data

3 Review of the Construction Industry 2006 and Outlook 2007-2009; DKM Economic Consultants Ltd. for the Department of the Environment, Heritage and Local Government; published September 2007

show that the Northern Ireland construction sector has continued its decline, though this has been moderated to some extent by higher value/prices. The most recent edition of the Northern Ireland Construction Bulletin suggests that construction demand may have levelled off in 2014. Construction output in the Republic has shown some moderate growth, led by the non-residential building sector. Indeed, the most recent statistical data suggest that the pace of recovery in civil engineering and non-residential might be accelerating; but it is from a low base and is somewhat concentrated in the Dublin area.

4.3 The Construction Materials Sector

The report published by InterTradeIreland in 2012 provided the following estimate of construction materials output and capacity utilisation in the island as a whole:

Table 4.3: Estimated All-Ireland Capacity - 2012

Product	RoI Capacity	NI Capacity	Total	Current Output	Capacity Utilisation %
Readymix Concrete - 000s m3	8,960	3,000	11,960	3,200	27%
Aggregates - millions tonnes	123	32	155	41	26%
Precast concrete - €millions	289	145	434	175	40%
Asphalt - millions tonnes	7.0	4.0	11.0	4.8	44%

Source: InterTradeIreland

There are limited up-to-date statistics on industry output in recent years and our assessment of the current state on the industry relies to some extent on industry consultation and the use of what data are available.

Northern Ireland

Developments in Northern Ireland may be described as follows:

- While overall industry activity has been in decline, demand for construction materials has remained reasonably steady;
- Construction materials output has been supported by the strong export performance of the precast concrete products sector and shipments of stone to the Great Britain market and by reasonably strong domestic demand from the agricultural and renewable energy sectors;
- Table 4.4 following shows the growth in High PSV aggregate shipments from Northern Ireland to Great Britain since 2009. The growth since 2012 – the date the InterTradeIreland report was published – is impressive.

Table 4.4: Shipments of Stone from Northern Ireland to Great Britain

000 tonnes	2009	2010	2011	2012	2013	2014
High PSV Aggr.	507	803	901	867	1,103	1,315

- Public sector road maintenance expenditure has held up well in recent years;

- The private sector has been steady and is showing some signs of a recovery in some areas;

- However, the overall level of activity is not spread evenly across the region. Activity in the Eastern part of the region is reportedly stronger than in the Western part; though it is not possible to quantify this.

In general, the level of output of construction materials in Northern Ireland is described as being comparable to what it was at the time of publication of the InterTradeIreland report. While this may seem inconsistent with the overall trends in the construction industry as outlined previously; it should be noted that exports to Great Britain have increased and also that not all industry segments are equally materials-intensive.

Republic of Ireland

In the Republic, consultations with industry sources and PRODCOM 2013 data indicate that output of aggregates dropped slightly after the publication of the report, but has since recovered to some 21 million tonnes. Readymix concrete production also slipped marginally to about 2.0 million cubic metres but is estimated to have recovered to 2.3 million cubic metres in 2014. Bitumen product output has declined by small amounts in volume terms.

Broadly speaking, output from the construction materials industry in 2014 across the island as a whole has been close to the volumes reported in the InterTradeIreland report.

In general, prices of construction materials, such as readymix concrete and concrete blocks are virtually unchanged since 2013. Stone, sand and gravel prices have increased, but this might be due, in part, to product mix changes. Stone is a very low cost product, and has relatively high transport costs that have been affected by fuel price increases. In addition, the period since 2010 has seen the introduction of much higher standards of quality assurance and traceability, which have added costs to quarry operations.

The most significant increase in materials prices has been in bituminous products, driven by increases in international oil prices. From 2010 to 2014, asphalt prices rose by some 43% in total. Prices dipped by some 12% from their mid-2014 peaks during Q1 of 2015, but have now returned to 2014 price levels.

Consultation with the industry indicates that there has been some change in industry capacity in the Republic; while no significant change is evident in Northern Ireland. In the Republic, some significant closures have been seen in the South-East; the Mid-West; Galway and the Midlands. However, not all of these have ceased operations; some are reported as having re-opened, though on a smaller scale than heretofore.

In summary, industry consultation and the available statistical data suggest that the industry capacity analysis provided in 2012 remains reasonably representative of the sector in Northern Ireland; whereas there has been some reduction in competition in parts of the Republic. It is not certain that the capacity in the closed firms has been disposed of; and therefore the capacity may be temporally “mothballed” rather than eliminated.

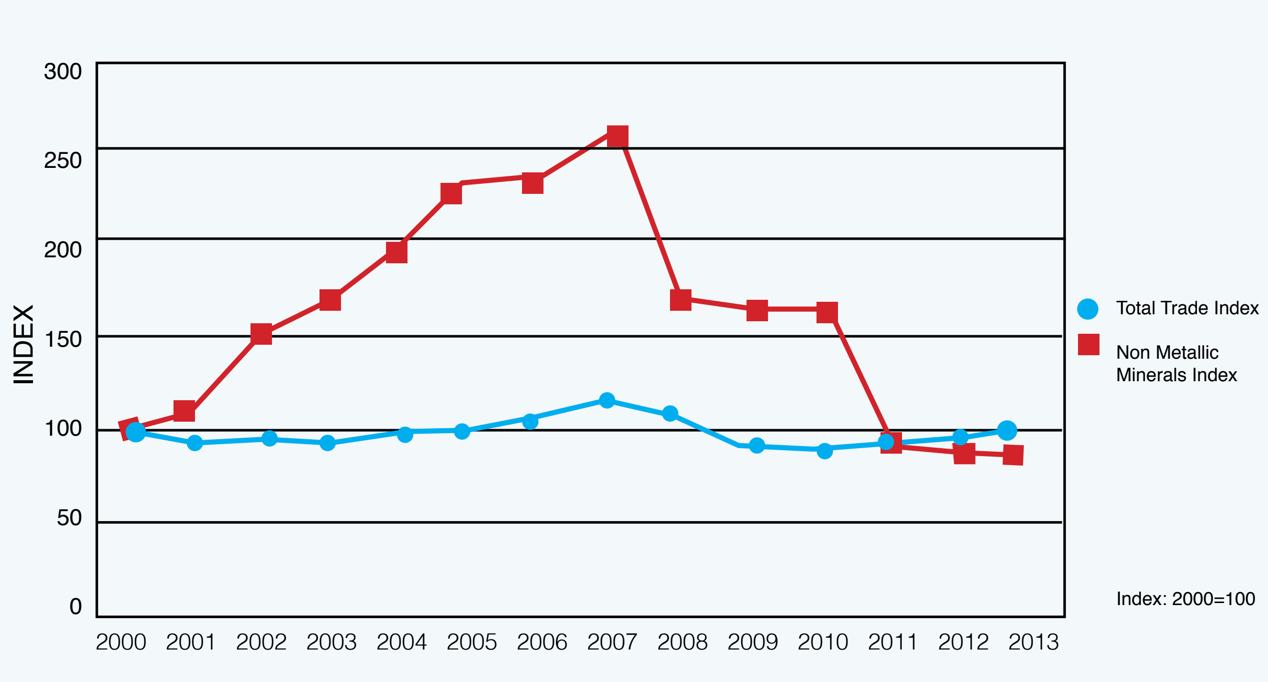
4.4 Cross-border trade

As noted in the previous report there is no exact match for construction materials in the figures for cross-border trade from the Central Statistics Office or the Department of Enterprise, Trade and Investment. For the purposes of the reports we use the SIC (07) code 23 which covers 'manufacture of other non-metallic mineral products'.[6]

The following charts show how the non-metallic minerals sector became a significant one in cross-border trade in the 2000s. In 2000 it accounted for €162.5m or 5% of the total manufactured goods crossing the border and this increased by 160% to €421m (or 11% of the total) in 2007. Since then there have been six consecutive years of declining cross-border demand to €131.8m in 2013 (or 4% of the total).

Chart 4.3 shows how both the growth and the subsequent decline in the trade in non-metallic minerals have far outstripped that of total cross-border trade.

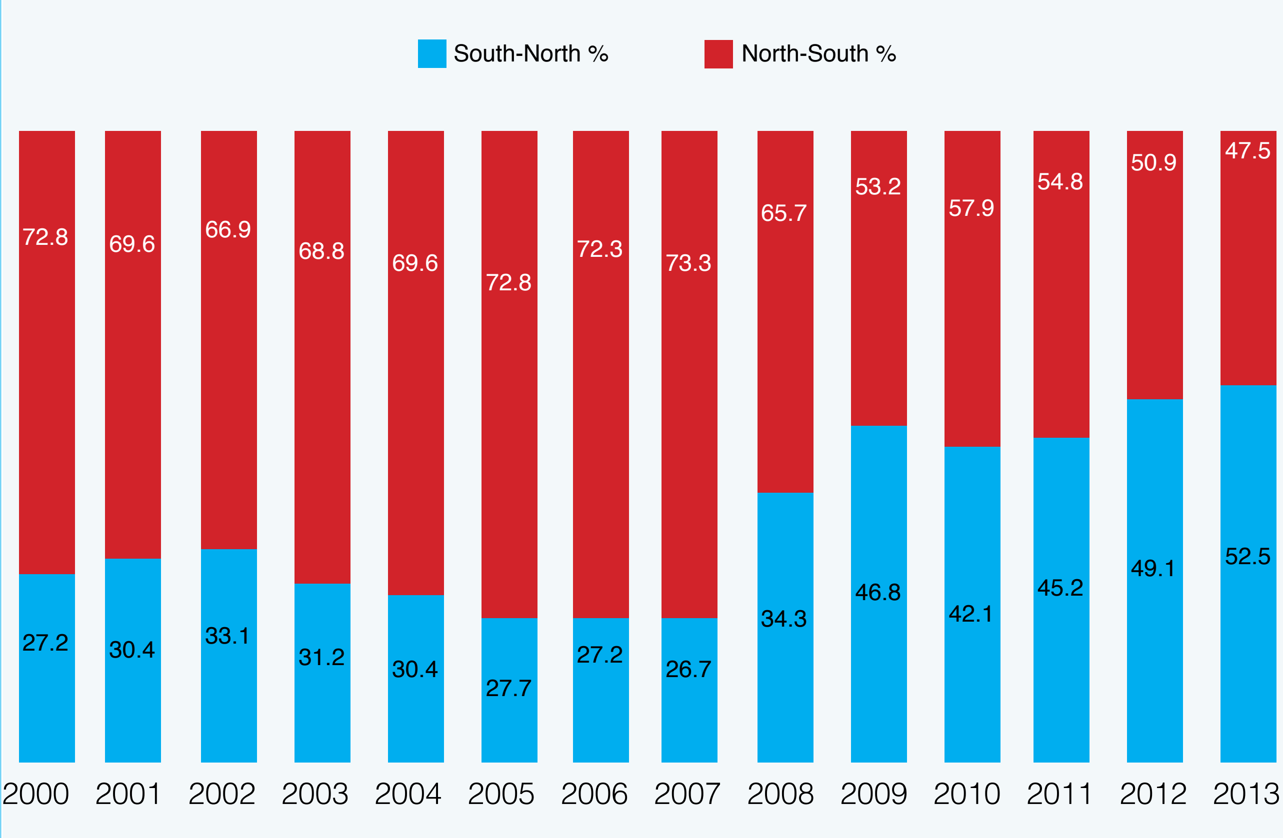
Chart 4.3: Comparative Trade Indices – Total Trade and Non-metallic Minerals



6 The sector includes cement, concrete, stones but also glass and ceramic goods.

Chart 4.4 shows that the share of the cross-border trade in these goods has, until 2009, been predominantly in a North-to-South direction but now the shares are much more equal, showing the fall in demand particularly in Ireland.

Chart 4.4: Shares of Cross-Border Trade of North-South and South-North Directions



4.5 Prospects for the Industry – Republic of Ireland

In the Republic, Budget 2015 contained several measures which should have the effect of increasing construction output. The abolition of the 80% windfall tax on land disposals; the target of providing 7,500 new social housing units in 2015 and the extension of the Home Renovation Incentive Scheme should all increase construction activity.

The Housing Agency estimates that an annual average of 16,000 new dwellings will be required in Irish urban centres in the period up to 2018, suggesting that scope for the construction sector to increase output to meet demand exists. Housing completions in 2014 were 11,106; 33% higher than 2013, but even at that, output remains far below the Housing Agency estimates.

However, future growth in housing output will depend on a range of factors including the ability of prospective purchasers to acquire dwellings. Shortages in housing stock were driving prices upwards and mortgage approvals, while increasing, have yet to show that they are sufficient to meet demand. However, new requirements for a minimum 20% deposit for purchases of dwellings are being implemented; though it is yet somewhat early to identify all the possible impacts of these requirements. It appears that the initial impact has been to reduce immediate demand and reduce price levels. A combination of funding issues; concerns about the future prospects for investors in the buy-to-let market and questions over the supply of houses make it difficult to project with any confidence when the housing market will return to some degree of normality.

New dwelling planning permission data shown in Table 4.5 show that the increase in permissions granted from 2013 to 2014 was quite modest, especially in the context of the well-publicised need for new dwelling construction. The number of new dwelling permissions in Q1 2015 was 18% above the 2014 levels, but whether this is a once-off increase or an indicator of increased activity remains to be seen.

Table 4.5: New Dwelling Planning Permissions – Republic of Ireland 2008 - 2014

	2008	2009	2010	2011	2012	2013	2014
Planning Permissions Granted	17,491	10,380	6,347	4,767	3,643	3,316	3,606
Total Floor Area (000 Sq Metres)	9,837	5,928	2,861	1,981	1,199	1,305	1,366

Source: Central Statistics Office

The total floor area for the permissions granted has also been quite low. In fact, the total floor area for which permission was granted over the five year period from 2010 to 2014 is lower than what was approved in 2008 alone. Normally, permissions granted in or before 2009 would no longer be valid in 2015; though some may have had their validity extended. Even if their validity were extended, many of the permissions granted may not be appropriate, given the changes in demand for housing seen in the recent past.

In overall terms, the planning permission data do not give any assurance that the house building industry has or will have sufficient reserves of valid permissions to meet current demand. If all the permissions granted in 2014 were for apartments of 75 square metres floor area; the floor area cited in the CSO data would equate to permission being granted for 18,200 such apartments. If all of the permissions were for houses of 140 square metres; the total floor area would equate to 9,757 houses. It is not possible to say how many dwellings are actually provided for in the permissions granted; but one can say with some confidence that it is less than the 16,000 units needed annually as prescribed by the Housing Agency.

Recently released housing commencement notice data show that the number of residential dwellings commenced in 2014 was 7,717. While this is a substantial improvement on the 4,708 see in 2013, it is still not sufficient to meet current needs.

Total expenditure under the PCP (Public Capital Programme) for 2015 is provided at €6.53 billion; a 6% increase over 2014. The PCP includes the Multi-Annual Capital Investment Framework (€3.89 billion) which is almost entirely funded by the Exchequer and other public capital investment, such as by State agencies, which amounts to €2.64 billion. Not all of this is construction related; for example, the proposed expenditure on social housing includes provisions for the purchase of existing dwellings.

On April 1 2015, the Minister for the Environment, Community and Local Government announced a funding package of some €1.5 billion which aims to provide 22,882 new social housing units. However, these will be provided through a combination of construction; acquisition and leasing, so the extent of construction activity is not known.

The average cost of building a social housing unit is €185,000; hence if all the funding were used for construction, it would provide just over 8,000 houses. It is reasonable to assume that leasing will be used widely.

Nonetheless, the proposed programme should absorb some vacant houses overhanging the market and should therefore increase construction activity in the medium term.

The commercial market saw a shift around mid-2014 to development of new office space, particularly in Dublin. Rents have been increasing; driven by a shortage of good quality space and the business case for further construction is now much stronger than in recent years. Commercial activity is expected to grow in Dublin, but the market outside Dublin may be confined to the other cities.

Industrial, retail and tourism related investment should increase, but at a reasonably modest rate.

In summary, the general improvements in the economy suggest that strong construction industry growth should be seen in the Republic in 2015; however, a combination of continued public sector budget restraints and housing market factors, both on the demand and supply sides, make it difficult to assess the level to which potential output will actually be achieved.

4.6 Prospects for the Industry – Northern Ireland

For Northern Ireland, it is equally difficult to project likely events in 2015 with any degree of confidence.

Housing completions have been at some 8,000 units from 2012 to early 2014, which is about half the level of completions seen in the mid-2000s. Housing starts have also been running at between 5,000 and 6,000 units over the past three years; again significantly lower than in the mid-2000s. However, price increases have occurred in 2014 – these been seen for the first time in some seven years – and these are expected to continue. A recent reform of the stamp duty should increase activity around the Stg£250,000 threshold. A modest pick-up in housing starts is expected, though this will be from a low base.

The Department for Social Development has previously concluded that on the basis of regional population projections, the long term average need for new housing in Northern Ireland is of the order of 12,000 units per annum. Current output levels are substantially lower than this. It must therefore be expected that in a stable long-term economy, the likely housing output will be of the order of 50% greater than current volumes. However, it is not anticipated that this level of output will be seen in the short to medium term.

The Construction Skills Network[7] forecasts that over the period 2015 to 2019 forecasts an average decline of -1.6% in public housing and an average annual increase of 3.7% in private housing investment will be seen.

The Department for Social Development's budget for 2015/16 will be Stg£715 million, down from Stg£790.3 million, the government announced in January. This is in line with the reduction suggested in November's draft budget and means the delivery target for new social homes will be cut from 2,000 to 1,500. The Construction Skills Network forecasts little growth in infrastructure spend over the period 2015 to 2019.

Reductions in public expenditure have a disproportionate impact on the Northern Ireland economy compared to other countries or regions within the UK, because about 1/3rd of all Northern Ireland employment is in the public sector and 2/3rds of its economic output is dependent on it.

The planned cuts in public expenditure have two impacts; one is on actual demand for construction work, including housing, and the other is on the ability of people to fund house purchases or other works.

In a report issued in November 2014, the Department for Regional Development said that the draft budget for 2015-16 showed a reduction of

- Stg£22.5 million, i.e. from Stg£344.6 million in 2014-15 to Stg£322.1 million in current expenditure; and
- for the capital budget, the reduction would be Stg£65.6, i.e. from Stg£391.4 million to Stg£325.8 million.

7 Industry Insights; Northern Ireland 2015 – 2019; published 2015

Priority will be given to specific projects, such as the A8; A2; A26; A44 and A31 schemes; while for schemes such as the Belfast Rapid Transit "it may be necessary to manage delivery over a longer timeframe."

However, the Department admits that its proposed expenditure will not support the level of investment necessary across essential water, waste water, roads and public transport services. It says that a well maintained road network is essential for the social and economic well-being of Northern Ireland, and it has been independently established that Stg£133 million (Stg£115 million in capital and Stg£18 million is current expenditure) is needed annually to maintain the structural integrity of the road network adequately. An initial estimate is that the capital funding will fall Stg£70 million short of the level of capital required. The Department will therefore be reliant on the Executive's in-year monitoring process to secure additional funding for essential structural maintenance.

Detailed information on other sectors such as commercial or retail is difficult to source. The Construction Skills Network forecasts that the Commercial and Industrial segments will grow at annual averages of 4.4% and 2.3% respectively over the period 2015 to 2019. However, these two market segments account for just some 17% of New Work and so while welcome, these increases will not have an impact comparable to housing or infrastructure spend.

While the UK Budget 2015-2016 proposes a reduction in the rate of corporation tax, it also provides for further social welfare reductions. Northern Ireland is more dependent on social welfare than other regions and these proposals are likely to increase the level of disagreement between the Local Assembly members and the UK government. The outcome could be reductions in the capital programme to minimise cuts in the current expenditure programme. This would have a negative impact on the construction materials sector.

4.7 Overall Conclusion

The performance of the construction materials sector across the island of Ireland has traditionally been dependent to a large extent on the performance of the housing and public infrastructure sectors. It is difficult to be optimistic about the prospects for these two market segments at present.

In the Republic, there is strong demand for housing in the Dublin region. However, this demand is not yet evident in other areas. In 2012, Dublin recorded 1,266 dwelling completions while there were 7,222 in the rest of the country. In 2014, Dublin had 3,268 completions, an increase of 158%; while the rest of the country saw 7,748 dwellings completed, an increase of just 7%. In fact, half of the increase in the "rest of the country" was in the three counties bordering the Dublin region. It is difficult to see how the growth being seen in Dublin can be replicated in other regions unless and until indigenous industrial development and the attraction of overseas companies to regional locations can be achieved. Without this form of regional economic development, there are limited prospects for growth in the housing sector in the near term, and possibly in the medium term.

In a similar vein, prospects for significant public sector investment elsewhere other than Dublin are limited. Firstly, there are continuing public finance constraints and Government policy appears to be directed more towards personal tax reductions and restoration of public services than to increasing the level of investment. Consequently, in the near and medium term, infrastructure projects will be more modest than in previous years and will tend to provide local activity, such as the construction of town bypasses rather than road development between major centres. Indeed, concern has been expressed that Dublin is coming close to its infrastructure capacity at present and that investment may be required in this region if growth is to be maintained.

In summary, in the Republic, there is little scope for optimism in respect of housing activity outside of Dublin and public investment nationally. Regional areas will continue to depend to a significant extent on the agricultural sector. However, with the meat and dairy sectors currently under significant price pressures, the prospects for the agri-sector are not strong.

In a similar manner, an imbalance in Northern Ireland was noted by many in the industry in our consultations; with the Eastern parts doing relatively better than elsewhere in the region. The key issue in respect of future demand for the industry is that there an evident requirement for new house construction, but it is not developing into construction activity. As noted previously, new dwelling completions are running far below the level that is required to meet normal demographic demand. While there is some optimism regarding private sector housing, the same cannot be said in respect of public housing.

On the public investment side, there is a wide range of projects "in the pipeline" that could start in the immediate future, but an absence of political agreement is holding up the release of the funds and there is some uncertainty as to when the projects will actually start. The recent UK budget proposals do not remove any of this uncertainty. A key difference between Northern Ireland and the Republic is that it is expected that the public sector funded projects, should they be started, will impact across Northern Ireland, whereas the expectations are that in the Republic, imminent projects are of such a scale that the impact will be local at best.

A view held across the island is that the advent of a corporation tax rate similar to that which exists in the Republic should make Northern Ireland more attractive to foreign direct investment and that any significant investment that may be attracted to the region will more than likely be close to Belfast. Careful management of the industrial development process will be needed to ensure a level of national/regional development.

In summary, in respect of Northern Ireland, one is left with a distinct impression that the industry sees a pipeline of future work that, in relative terms, is larger in scale than what is being seen in the Republic, but is no closer to being realised. With decisions being taken on public investment and with continued engagement with the Great Britain market, the prospects for a more sustainable future for the industry would be improved. In the interim, future prospects in all business sectors – housing, commercial and agri - are not strong.

5. Industry Financial Analysis

The InterTradeIreland report of 2012 contained an analysis of the accounts of twenty companies from across the island. The companies were chosen at random and the accounts were obtained from the relevant companies offices. We sought to replicate that analysis during this review to see if financial performance had changed; however, we find that there has been change – substantial in some cases - in many of the companies included in the original sample arising from closure; restructuring and/or change of ownership. In total about 25% of the original sample could not be replicated. We are therefore unable to show sufficient comparison between the 2012 and 2015 samples to provide a robust financial performance comparison. We therefore confine ourselves to a broad comparison of the industry financial performance in recent years.

Financial Performance

Our consultations within the industry in 2015 indicated to us that the financial performance of the sector is quite variable. Some companies are operating at a loss; others are making marginal profits and, particularly in the Republic, some cross-subsidisation is reported; i.e. construction materials are being sold at a loss, but are cross-subsidised by other activities or non-construction sales.

5.1.1 Profitability and Cash Generation

From the accounts available to us, we can say that in the most recent year filed, typically 2013, 60% of the companies were profitable; while a further 20% are best described as break-even, with 20% of the sample being loss making.

The 2102 report found that 65% of that year's sample were loss making. However, care must be taken in respect of the source of the apparent improvement. Some of the 2012 loss makers have either ceased operations or have restructured through some form of company action such as receivership. Some companies have turned around their performance; mainly in Northern Ireland, through a greater focus on the British market. One of the companies that was loss-making in its last filed accounts is now profitable following a detailed review of their business.

In summary, the apparent improvement in financial performance appears to be attributable more to corporate actions than to improvements in the construction materials market.

As was found in 2012, the profitable companies tend to be the larger companies, and ones that have a unique element; such as a unique product, a unique skill or some unique specialism. Many of the profitable companies have an involvement with the Great Britain market. It may also be assumed that good management has played a key role in maintaining profits.

The previous InterTradeIreland report and financial analysis showed that while many companies were not profitable, they still generated a positive cash flow. This arose from reasonably large depreciation charges that in turn arose from previous capital investment. However, depreciation charges are not as evident at this time. In their most recent accounts, loss making companies tend to show an increased dependence on their creditors. However, the sample is not sufficiently large to say that this is an industry-wide situation.

5.1.2 Balance Sheet Movements

As one might expect from an industry sector where the companies remaining in existence are showing an overall improvement in profitability; balance sheets have been strengthened. In many cases, debtor and creditor amounts have increased in line with overall performance. However, we note that in some companies, debtor and creditor levels both increased significantly, when compared to turnover figures. We appreciate that balance sheets are a snapshot of financial standing at one point in time, and these increases may not be typical of the situation throughout the full year. On the other hand, the increases could suggest an increased appetite for risk; and gaining business by offering extended credit terms; with the extended terms being funded by extending the time taken to pay creditors.

5.1.3 Indications

It is risky to seek to be definitive about the state of the industry from a limited sample of companies; but the analysis of the financial performance of companies remaining from the 2012 analysis suggests that overall industry financial performance has improved, but that may be due more to a combination of factors including corporate restructuring; changes in ownership; closures and changed strategy.

While it appears that more companies are now profitable, in many cases the profits are not substantial, but it does suggest that long term continuation in business may be less of a concern that it was three years ago – though this is not universal.

6. Review of 2012 Recommendations

Review of the Recommendations made in 2012

In the 2012 report, a series of short-term and medium-term recommendations were made. The following is a summary of relevant developments since then:

Table 6.1: Developments with Short-term Recommendations

Short term	Recommendation in 2012	Developments
1	InterTradeIreland to cooperate with industry bodies and agencies to disseminate the findings of this review.	Completed in 2012 with occasional checking up afterwards to see how things were progressing and therefore the 2014-15 report. This was done in Northern Ireland through a launch event at Stormont attended by the ETI Minister Arlene Foster. The document was also circulated to MLAs. Two information sessions were held in Northern Ireland to inform industry about the findings and get feedback from them regarding the practicalities and workability of the recommendations. In the Republic, a range of regional seminars took place for the industry.
2	The agencies and the representative bodies need to interact to explore how existing services and supports could be used more effectively by the sector in both jurisdictions and on a cross-border basis.	Invest NI continue to hold quarterly meetings with QPANI to assess the state of the industry and what supports might be applicable to member firms. Other sectoral initiatives are also continuing - e.g.; 25 February 2015 event on energy efficiency for the industry. There is regular and constant positive contact between the ICF/ Irish Precast Concrete Association with Enterprise Ireland that tends to focus on assisting exports.
3	Agencies and industry bodies should prioritise the provision of management skills training for the sector with a focus on operations management, financial aspects such product costing and profit management.	This area continues to be a focus of the work on the part of QPANI with the Invest NI offerings open to the industry. Issue here of skills shortages is particular areas mentioned by firms (design, QS, contract management). Similar skills issues are seen in the Republic; safety training is administered by Solas and a submission re apprenticeships has been made to the Apprenticeship Council by the ICF.

Table 6.1: Developments with Short-term Recommendations

Short term	Recommendation in 2012	Developments
4	Agencies to promote support available for both product innovation – such as glass reinforced concrete – and process innovation – such as improved methods for repairing potholes in roads – that would have spin off benefits for the construction materials sector.	Both InterTradeIreland and Invest NI have continued to support company R&D, product development and process innovation in the industry and their supports have been used - all based on a lack of displacement by the end product being cross-border or off the island exports. While Enterprise Ireland provides various forms of assistance, they benefit those in the sector who focus on export markets.
5	Agencies to continue the ongoing work in the promotion of sales off the island in the pre-cast concrete product segment, particularly the higher value added end of the product category.	Invest NI report that both sales and numbers of firms exporting outside NI have increased. In terms of cross-border trade this is less the focus than GB but is constantly being monitored. Recent exchange rate developments have assisted firms in the Republic substantially and competitiveness has improved significantly. Expectations are for further growth in export markets. Enterprise Ireland has been extremely supportive in developing the Great Britain market.
6	Agencies to explore opportunities for exporting the intellectual property associated with high bureau services from bases on the island, quality precast concrete design and potentially providing design	Invest NI has been doing some work with construction services firms to look at possible exporting opportunities - early stage of development.

Table 6.1: Developments with Short-term Recommendations

Short term	Recommendation in 2012	Developments
7	Industry actors should develop and adopt an improved product certification and standards.	Under the aegis of bodies such as the NSAI and with the support of Government departments, industry product standards are being continuously updated with the input of all stakeholders and in response to market demands. ICF and QPANI are heavily involved in this. However, there is a lack of both knowledge and understanding among stakeholders, including designers and specifiers on the standards which needs to be addressed so that standards are enforced in the wider construction sector. Public and private procurement policy must reflect these new and evolving standards. At the moment tendering focuses to a very considerable extent on one issue - price. There is a need for a greater focus on quality.
8	Industry actors and the relevant Departments and agencies to cooperate on exploring the potential for using 'project bank accounts' and for enforcing other regulations to fully protect the construction supply chain.	While this concept has been promoted, there has been no progress in the Republic. In Northern Ireland, Government Construction Clients under the leadership of the Central Procurement Directorate have adopted the use of project bank accounts in construction projects under Stg£1 million. Currently a number of pilot projects have been completed.
9	Individual companies in the sector should undertake a critical analysis of its current market, sales and financial performance and likely future prospects in order to allow owner/directors to consider the costs of staying in business versus the long term payback that may accrue when the economy improves.	There has been rationalisation of the operations of quarries and plants, which suggests that companies did review their performance. While capacity remains in existence, financial performance appears to have improved.

It is evident that there has been considerable activity on the part of the representative bodies and the development agencies across the island in two areas in particular; the development of sales to Great Britain and the continuing development of product standards.

Table 6.3 following shows the progress made in respect of the Medium Term Recommendations of the 2012 report. Some further work in respect of the medium term recommendations is needed. This is discussed in the following chapter.

Table 6.3: Developments with Medium-term Recommendations

Medium term	Recommendation	Developments
10	The two governments to address the issue of sustainable levels of capital investment in required infrastructure. Projects where the identified fiscal and economic benefits are substantial and/ or substantial private sector investment is available, should be prioritised.	While it is appreciated that Governments have been operating under stringent fiscal restraints, they are viewed generally by the industry as not maintaining a reasonable level of public investment.
11	At the same time maintenance of infrastructure and state buildings constructed during the past ten years should be considered.	Infrastructure maintenance had been regarded as having been quite good in Northern Ireland; but recent budget cuts will impact on this area of spending. In the Republic, spending on maintenance has fallen; but it appears now that the current levels will at least be maintained.
12	The relevant agencies and Departments to explore options for providing assistance for those made redundant from the sector through retraining to assist them to find employment in other industries and funding mechanisms such as the European Globalisation adjustment Fund (EGF).	This was not done to any significant extent. However, an emerging skills shortage suggests that training for construction work may be more appropriate in the future.
13	The relevant agencies to work with the industry to explore how regulation of the sector through product certification and improved planning enforcement.	Regulations, product certification; assurance systems and quality standards are evolving constantly. However there is a need for these to be communicated to the wider industry including designers and specifiers across the whole island, as pointed out above so that they become the norm in the industry. The product standards need to be supported by the provision of certification by suppliers showing that they have complied with the product standards. Planning legislation needs to be more protective of authorised operators and also rigorously enforced by local authorities. Public procurement should also encourage greater planning compliance.

Table 6.3: Developments with Medium-term Recommendations		
Medium term	Recommendation	Developments
14	Work with the construction materials industry to seek the means to bring about improvements in planning enforcement where such improvements are needed.	With the transfer of planning powers to the new 11 local councils in Northern Ireland in April 2015 QPANI is involved in delivering industry awareness training to assist in capacity building for new planning officers knowledge of the quarry products industry. In the Republic, the quality of planning enforcement remains a serious issue.
15	Local authorities should seek to plan their demand patterns insofar as possible, so as to enable the industry to respond to demand in the most efficient manner possible.	QPANI submission to single planning policy statement consultation in 2014 highlights importance of aggregate reserves and the need for collaboration between Councils to ensure a sustainable supply of construction aggregates across Northern Ireland. QPANI calling for introduction of "mineral safeguarding areas" to prevent sterilisation of important aggregate reserves. The ICF has also been liaising with Government Departments; local authorities and bodies such as the Geological Survey of Ireland in respect of aggregate mapping and long term supply.

7. Industry Overview and Issues

7.1 The strategic importance of the industry

Chart 4.1 showed the Gross Value Added (GVA) for construction and total GVA for Northern Ireland as a whole and from this, it is estimated that construction's share of regional GVA is of the order of 5.3% for 2013. The Republic of Ireland's construction industry – at €10.2 billion – equated to some 5.6% of GDP in 2014.

CEN (The European Committee for Standardisation) reports that the construction sector is one of Europe's biggest industries accounting for 10% of GDP in 2010. Other reports issued by economic commentators put average EU construction output as a percentage of GDP at higher levels in some years, ranging from 12% to 14% during the last decade.

Construction output across Ireland is far below what a normal economy should be producing. The IMF suggests that in 2011 the Republic of Ireland construction output was about 1/3rd of its long term norm[8]. A comparison with the sector in Europe suggests that construction in the Republic should have an output in the order of €21 billion to €25 billion per annum and in Northern Ireland, annual output should be of the order of Stg£3 billion; a level last seen around 2005. This equates to circa €4 billion at current exchange rates. This suggests that the island wide construction industry should have an output in the order of €25 billion to €30 billion or Stg£18 billion to Stg£22 billion. In other words, the island's construction output is about half of what it should be in a normal economy.

The construction materials sector is a vital element in the construction supply chain. In essence, our built infrastructure would not be what it is today without stone, sand, aggregate, readymix concrete, and other concrete and bitumen products. These materials are at the core of building works; yet their impact on costs is small when compared to their role. The range of construction materials covered in this report, along with concrete blocks, account for less than 5% of the cost of a typical new house sold today in Ireland. In Ireland, over the nine year period from 2000 to 2008, readymix concrete prices increased by 26%; concrete blocks by 32% while overall house building prices rose by 53%. Materials prices were mainly driven by fuel and energy increases; fuel prices alone rose by some 65% over this period and transport costs are relatively high in this sector; given that the basic materials have a low cost and must be delivered to site.

Because of the nature of the materials, the sector will be one where there are a substantial number of plants spread across the island. A readymix concrete batching plant is confined to supplying customers within a radius of the order of 50 to 60 kilometres. Transport economies confine aggregates to a broadly similar geographic area.

8 The Driving Force behind the Boom and Bust in Construction in Europe; IMF Working Paper; August 2013

Consequently, to justify the existence of a plant, a reasonable level of construction activity is required within that area.

With construction output across the island being half what it should reasonably be expected to be – and has been for a number of years – and with output is focussed around the two major urban centres and their immediate regions, there is substantial pressure on construction materials companies in rural areas.

On-going Government investment is essential to address the island's continuing infrastructure needs. However, as discussed previously, there is little confidence within the industry that reasonable levels of investment will be undertaken in the near future.

To address the current imbalance in construction output; Government expenditure needs a greater focus on the less developed regions in the island. Until this happens, the construction materials sector outside of the major centres will continue to weaken. The sector has in the past shown a capacity to respond to demand fluctuations; however, it must be a concern that the continuing low level of activity may weaken the industry and reduce that capacity to respond to increased demand for its products; whenever such an increase is needed.

Governments need to appreciate the strategic nature of the construction materials sector as without it, the construction industry in parts of the island will be constrained.

7.2 The Vision for the industry

In the 2012 report, the stated vision for the construction materials sector was that:

- It has sufficient capacity that allows it to serve the market efficiently; this implies that the industry sheds some of the current over-capacity and eliminates the related carrying costs;
- It is smaller than its current (i.e. 2012) scale, but yet is a well-managed, competitive industry;
- It is a well regulated industry; this covers all aspects from product certification to planning enforcement on the part of the local authorities;
- It maintains the highest health & safety and environmental standards;
- It values its role as custodian of finite resources; and
- It generates a fair level of profit that will sustain the industry for the future.

7.2.1 Sufficient Capacity

The issue with the construction materials sector is not one of insufficient capacity, but one of over-capacity. It would normally be expected that where business volumes have fallen to the extent that they have in this industry, capacity would be reduced through closures and disposal of plant. This is referred to as "shakeout" and usually it is the less competitive businesses that close early in the process.

There have been some closures and some "mothballing" of facilities, but some firms that were apparently closed have subsequently re-opened their operations and their capacity remains in the marketplace, and is capable of being reactivated very quickly, without any significant expenditure. Quarry and batching plant capacity has not really been removed or eliminated to any significant extent.

While there is over-capacity at present; views expressed by the industry itself and by its customers reveal extensive concerns about long term capacity. Reference will be made later in this chapter to price levels, but there is some concern – which is more evident in the Republic – that current prices and profitability are so low that some companies will find it difficult to fund the opening of new quarries when their existing sites are exhausted.

A related area where sufficient future capacity is now questioned is the distribution of product. In the past, product distribution has been carried out by a mix of company-owner vehicles and self-employed hauliers. In recent years, fleets have been reduced and it is reported that a number of self-employed hauliers have left the business, leaving questions as to whether there would be sufficient capacity in the event of an uplift in demand. This is not regarded as an insurmountable issue by the industry as currently companies share the independent hauliers – i.e. hauliers do not work for one supplier alone – and in the event of an upturn, vehicle capacity could be increased through leasing. The issue could be one of driver availability.

In summary, the vision of the industry having sufficient capacity is being maintained, but concerns about the provision of future capacity are emerging.

7.2.2 Industry Scale

While a small number of companies have ceased operations since the 2012 report, and there has been some rationalisation through acquisition and some closures of specific plant; in general, the industry is not yet as a long term sustainable, balanced scale. Reference is made above to potential distribution issues and previously it was noted that across the island, industry output is about half of what it would be in a normal economy.

Pending the achievement of a normal economy across the island, it is difficult to see how the industry can establish the appropriate scale of operations.

7.2.3 Regulation

There is a strong set of standards in force for the industry such as I.S. EN206-1 for readymix concrete; and CE marking has been introduced for the majority of construction products and materials. These are complemented by the requirements of planning legislation for registration; authorisation and planning approval for quarries and production facilities.

The representative bodies have been very active participants in the development and communication of the relevant standards across the island.

The key issue with standards and regulation is the absence of enforcement in some areas of the industry, particularly planning enforcement and ensuring product adherence to the required standards. There were many complaints from interviewees that public sector tender specifications do not always include a stated requirement that materials meet the relevant standards; though the situation in this regard appears to be improving at a better rate in Northern Ireland than in the Republic. Allied to this, there is a view that contract audit trails and assurance are monitored better in Northern Ireland. Some individual government bodies and agencies were identified as being quite strict in respect of assurance that standards are met by suppliers – and this is welcomed within the industry - but there appears to be a great deal of laxity in some quarters.

It should be a standard in itself that public sector tenders state that adherence to specific standards is a condition of the tender and also that materials must be sourced from authorised suppliers only. This should be accompanied by increased proactivity in respect of standards verification and contract audit.

7.2.4 Health, Safety and Environmental Standards

This is an area where both the ICF and QPANI have been very active and where adherence to the highest standards by the members of each of these organisations is an imperative.

7.2.5 Custodians of Finite Resources

This is recognised by the members of ICF and QPANI.

7.2.6 A Fair Level of Profit

Industry profitability has been subject to serious competitive factors since the downturn in the industry commenced some years ago. This is discussed in more detail later.

Summary

In summary, we conclude that some progress is being made towards the achievement of the vision for the industry. Operational capacity now more closely matches demand, though overcapacity still exists. The industry remains very competitive and it has developed higher standards. However, it will be impossible to achieve the industry vision in the current economic circumstances and there are a number of factors that are of concern to the industry. These are discussed in the next section.

7.3 Review of Industry Issues

7.3.1 Effect of Industry Over-capacity

Over-capacity has been referred to in other sections of this report and there is both structural and cyclical overcapacity in evidence. In the short term, the sector is confident that it can respond to increased demand; however, there is a concern that a continuation of the current low levels of construction activity could, in some areas, weaken the sector to the extent that a reasonable response to increases in demand might be difficult.

7.3.2 Price Levels and Profitability

Across the island, the current level of prices in extremely competitive. In the Republic, CSO data on construction material costs show that in January 2015 the price of ready-mix concrete was marginally lower than in January 2014 and 2.7% cheaper than in January 2009. Concrete bricks and blocks were 6.8% more expensive in January 2015 than in January 2009. Similar data is not available for Northern Ireland, though the industry there says that prices are very competitive, particularly in the border areas where suppliers from the Republic can compete with local operations and in areas such as Belfast, where demand is more buoyant and where competition is strong.

Media reports of comparisons with prices in Great Britain showed that in late 2014, 40N ready-mix concrete in Britain was priced at the order of Stg£90 (currently €124) per cubic meter and aggregate for under floor fill was Stg£15 (€21) per tonne. These prices are about twice the current prices in the island of Ireland. There are reports that in the South-east of England, aggregate can cost Stg£25 (€35) per tonne.

There is a view within the industry that the relatively low aggregate prices in Ireland are a key factor in the competitiveness of Irish pre-cast products and aggregates in Great Britain at present. Maintaining price competitiveness is seen as a critical factor in the industry's future and any Government policy that would impact negatively on price competitiveness should be avoided.

The recent *Report on the Review of the Performance of the Public Works Contract* [9] recommended that all public sector construction projects with a value in excess of €2 million should be awarded on the basis of Most Economically Advantageous Tender (MEAT) with a significant weighting for quality. This is to move away from the current high level of focus on price.

It is of note that recent increases in demand in some areas do not appear to have led to increased prices for materials. This is possibly a reflection of the level of overcapacity within the market and a desire on the part of suppliers to retain customers. However, it is also possible that it a reflection of the price advantage enjoyed by the non-compliant suppliers – see section 7.3.3 following.

7.3.3 Competition from Non-compliant operators

Across the island, a significant concern of the industry is competition from non-compliant operators.

Certain legal and regulatory standards for construction materials are in existence, but three factors combine to provide an attractive opportunity for non-compliant operators to enter and leave the market. These are:

1. Cost Advantage

Detailed discussions with producers lead us to conclude that the cost of compliance including securing planning authorisation through to quality assurance systems; product testing and product traceability ranges from 10% to 15% of the selling price, depending on the product. This is the scale of cost advantage a non-compliant operator has. It does not include any transport cost advantage – many non-compliant operations open when a major construction project is taking place in the vicinity, which can provide an additional cost benefit through lower transport costs. This is particularly the case for aggregates where transport costs are a substantial proportion of total costs.

2. Product Standards not Specified

It is reported that in many cases, specifiers, including public bodies, fail to include adherence to particular standards in the specifications issued to building contractors. Comments made by some consultees were to the effect that some specifiers take the view that adherence to regulatory requirements on the part of building contractors is a "given"; while other consultees expressed their view that some specifiers are simply not aware of the requirements. The situation appears to be better in Northern Ireland,

9 Report on the Review of the Public Works Contracts; Published by: Office of Government Procurement; December 2014

where it is viewed that local authorities are increasingly specifying standards as part of their project documentation.

3. Weak Enforcement of Regulations

The level and extent of enforcement is weak, particularly in the Republic. Specific incidents were cited where complaints of public sector works being supplied by a non-compliant operator were made to the relevant local authorities (the client authority and the authority in which the non-compliant quarry was located); however, by the time action was taken, the project was completed and the non-compliant operator had closed.

There is little that the industry can do to mitigate this issue, other than to remain vigilant and advise the relevant authorities of incidents of activity on the part of unauthorised and non-compliant operators.

7.3.4 Material Reserves

During our consultations with both industry participants and stakeholders such as customers, the question of material reserves was raised on a number of occasions. The views expressed widely were that current price levels could be justified only if it is accepted that the materials being used currently – stone, sand – are being priced only at the marginal extraction costs and that the true cost, including all planning approval costs are not being provided for.

There is a substantial concern that the industry will not have sufficient reserves to meet a reasonable proportion of the initial costs needed to open new quarries when current quarries are exhausted. A situation could arise where materials will need substantially higher prices to justify new quarries being opened. It was noted above that aggregate prices in Great Britain are substantially higher than in Ireland and adequate reserves, with access to those reserves, is essential to maintain price competitiveness.

It must be concluded that the impacts of the current situation regarding industry over-capacity and the operations of non-compliant suppliers are threatening the long-term sustainability of the sector and the management of our natural resources.

7.3.5 Risk

An area of concern for the industry is the question of financial risk, particularly in respect of participation in public sector contracts. In the Republic of Ireland, under the current form of contract, there is a single main contractor and all other suppliers are sub-contracted to the main contractor. The concept of the “nominated sub-contractor” is not used for public sector contracts at present. From a financial perspective, this form of contract provides substantial difficulty for the construction materials sector in terms of getting payment for supplies. Essentially, the materials sector is at the end of the supply chain stretching from the customer through the main contractor to the materials supplier.

The recent *Report on the Review of the Performance of the Public Works Contract* made several observations about the operation of the Construction Procurement Reform Initiative launched in 2006. Under the previous forms of construction contracts used in the public sector, risk, including cost overruns, was largely held by the State with little incentive on the contractor to manage that risk. Substantial cost overruns occurred on certain projects. The current form of fixed price, lump-sum contracts were introduced in 2007, with a single main contractor accepting that risk. While a risk premium was expected, the construction downturn meant that tender prices dropped rather than increased. Many suppliers suffered slow, and sometimes withheld payment, culminating in offers from the main contractor to settle at a discount.

In the course of preparing the report, the authors received submissions from a range of stakeholders; many of which made reference to the issue of payments to sub-contractors. Proposals for addressing these issues were put forward, such as nominated sub-contractor status and “project bank accounts”. However, apart from recommending that “specialist” sub-contractors such as mechanical and electrical firms may contract directly with the public sector entity (a proposal that is being implemented); none of these other proposals were discussed in the report, even though, for example, the concept of project bank accounts is being trialled in Northern Ireland at present. There was no reference to dispute resolution procedures between the main and sub-contractors in the report. In essence, the issue of payment risk by suppliers other than mechanical and electrical contractors was not considered.

7.3.6 Procurement

There was much concern expressed with procurement procedures across the island and questions as to whether or not best value for money was being obtained by the State. The experience of the industry is that preference is generally given to the lowest price; which aids the non-compliant operator, rather than value for money. Even where the MEAT (Most Economic Advantageous Tender) approach is used, it appears that price is either the sole, or at best, a significantly dominant factor in the decision of award of contract.

Interviewees that have bid for public sector work have seen no evidence of abnormally low tenders being scrutinised to ensure that proper provision for quality assurance, traceability etc. has been included as part of the tender or in the evaluation process.

We are advised that public sector contracts do not always specify that materials must be purchased from registered and authorised, i.e. compliant, quarries; or that the legal requirement for the CE marking is adhered to or that standards such as EN206 for concrete be met. These open the market to exploitation by non-compliant operators.

In simple terms, a significant change of attitude in the procurement and enforcement process of more professional standards; consideration of the risk environment for sub-contractors by the purchasers of construction works; coupled with better enforcement would ensure that compliant producers are treated responsibly and that non-complaint producers cannot profit.

7.3.7 Skills

Concern was expressed within the industry with an emerging skills shortage; especially at craft, technical and professional staff levels. Some training in areas such as safety has been provided and/or supported by State agencies. However, technical skill shortages are becoming apparent as an issue that may hamper development in the event of a market upturn.

7.3.8 Age Profile of the Industry

The sustainability of the sector depends in part on its ability to attract qualified staff with the appropriate work ethic. A concern within the industry has been the age profile of those working in it. The economic downturn across the island, and the impact on construction activity led to

- Reductions in employment, with many younger staff emigrating from the island;
- A reduction in training and recruitment; and
- Limitations on the sector's capacity to offer competitive remuneration packages in comparison to other industry sectors.

A recent (2015) survey by QPANI shows an urgent need to address skills and succession issues within the sector, which, if not addressed, will worsen and endanger the long term viability and sustainability of the Industry. The survey results clearly show an over-representation of older age groups, i.e. over 36 years of age, in all sectors with quarrying having a particularly higher age profile in operational and transport activities. The survey results are currently being used by QPANI to inform members and relevant industry stakeholders of the critical succession, skills and recruitment issues facing the industry.

A partnership of QPANI, together with other construction materials representative bodies and the further education and post primary education sectors, is actively lobbying Government for support and pursuing the implementation of apprenticeship schemes and the development of training and competency frameworks that will map out a career path for prospective employees coming into the industry.

7.3.9 Quality of Market Information

There is a widely held view across the island that official data do not reasonably represent the construction market position.

Official data from the national statistical services are based on industry surveys and members of the construction materials industry find it impossible to reconcile the official data with, for example, national or local Government budget or expenditure reports, such as Public Capital Expenditure reports in Northern Ireland. There can be various reasons for this. For example, a road project costs can include land acquisition; road maintenance expenditure can include street cleaning. In its Production in Building and Construction Index, the CSO states that "Given the unprecedented low base this series is starting from, the CSO will continue to monitor the quality and comparability of this new data series"; implying a need for care to ensure the reliability of the published statistics.

Across the island, consultees are of the view that the two major cities, Dublin and Belfast, are both growing in terms of construction activity, but that very little activity is being experienced anywhere else. Indeed, it seems that as distance from either of these cities increases, activity reduces. An analysis shown earlier in this report (Section 4.6) clearly showed that increases in housing output were seen in Dublin and its neighbouring counties. The views expressed are that the official statistics do not allude to any extent to the regional disparities seen by the industry.

Projections for construction output increases for 2015 range from 4% to 8% in volume terms across the island; however, many consultees in rural locations are not confident of even the lower of these two figures being witnessed. Much depends on the spend by the agri-sector, which does not become apparent until the latter part of the year.

7.3.10 Rural Development Programmes

An on-farm capital investment scheme, TAMS II (Targeted Agricultural Modernisation Scheme II) with a budget of €395 million, is proposed under the new Rural Development Plan (RDP) was announced in January 2015. It has been agreed that the scheme will fund some key areas amongst which are milking equipment, slurry storage, animal housing and bioenergy schemes, which have some construction content.

The scheme is part of the Irish Government's €4 billion Rural Development Programme 2014 to 2020, which aims to enhance agricultural competitiveness, with a particular focus on benefitting from the abolition of EU milk quotas in April 2015.

The first scheme to be launched is the Young Farmer Capital Investment Scheme, which opened for submission of applications in June 2015. Opening dates for the other five schemes are being announced. The Programme is to run until 2020. Early implementation of the remaining schemes should provide some opportunities for rural providers of construction materials.

In Northern Ireland, a Rural Development Programme 2014 to 2020 is also being implemented, which includes some schemes such as a Business Investment Scheme, which provides, inter alia, for the building and refurbishment of farm buildings. The overall allocation for this scheme is proposed at Stg£200 million, which if implemented may provide opportunities for the construction materials sector.

Early implementation of these schemes across the island would provide support for the industry and would, in particular, provide a counter-balance to the increased demand for construction that is evident in major urban centres.

8. Recommendations

Government

1. The Governments should appreciate the strategic importance of the construction materials sector and seek to support it through addressing the island's infrastructural needs and thereby making sustainable levels of capital investment in new projects together with appropriate levels of maintenance on existing and newly built infrastructure. The fiscal and economic benefits of spending on construction can be significant, and projects where the identified fiscal and economic benefits are substantial and/or substantial private sector investment is available, should be prioritised.

2. We recommend that both Governments should seek a more rapid implementation of programmes such as the Rural Development Programme and sub-programmes.

3. There is scope for much improved regulation of the sector, particularly in the areas of planning enforcement; product specification in construction contracts and improved monitoring of materials provided. We recommended that Governments should encourage the relevant agencies to develop processes to enable them to act on unauthorised non-compliant operators much faster than at present. At present, by the time action is taken against such operators, projects can have completed its acquisition of basic materials and enforcement is ineffective at that stage. This issue appears to have been addressed more effectively in Northern Ireland than in the Republic.

4. Governments should implement procurement policies in all public bodies under which contracts should include conditions that all construction materials suppliers are compliant with relevant product standards and have the requisite planning approvals. Public contracts should be contested by compliant operators.

5. The Governments should institute improved contracts governing public works to reduce the risk for suppliers. For example, the use of Project Bank Accounts is being trialled in Northern Ireland, while it does not appear to be even a consideration in the Republic.

Local Authorities

6. We recommend that local authorities that have responsibility for planning enforcement and compliance with CE marking should work with the construction materials industry to seek the means to bring about improvements in enforcement where such improvements are needed. This recommendation was also made in the 2012 report. Its inclusion suggests that little, if any, progress has been made in this regard since then.

7. We recommend that local authorities should seek to manage their demand patterns to enable the materials sector to respond to demand in the most efficient manner possible. This point was made in the 2012 report and we note that in the Republic roads grant programmes incorporate a requirement to spend specific amounts of the annual road maintenance and improvement grants by the end of the summer.

Other State and Development Agencies

8. We recommend continuing liaison between the development agencies and the representative bodies to see what scope exists for supporting the sector. At present, there is a high level of satisfaction with aid provided for exporting activities. Consultation might therefore consider other forms of aid that could be provided, say for management development, in companies reliant on indigenous markets.

9. We recommend that consideration be given to an industry skills audit to see the extent and scale of prospective skills shortages in the sector and the subsequent drafting of a skills development programme.

10. We recommend that the State agencies should ensure that the interests of the construction materials sector are considered in any future strategic planning exercises carries out by them. While there are no issues that this is not being done; it should be a consideration in future planning.

The Industry

11. Four recommendations were made to companies in the sector in the 2012 report which essentially were that:

    - Companies should give consideration to upgrading management skills or systems to support the ongoing development of their business;

    - Individual companies consider the pros and cons of exiting the sector; and the costs of staying in business versus the long term payback that may accrue when the economy improves.

    - If the use of financial reserves to keep a business in operation does not provide an acceptable return or payback; the owners/ directors should consider the potential for bringing about a reduction in costs through operating or specialisation agreements with other companies in the sector.

    - Finally, if some form of corporate action such as examinership or liquidation is inevitable, companies should take a proactive approach and seek to maintain as much control as possible over their own destinies.

These recommendations remain valid for the sector, even though some improvement has taken place in terms of operations rationalisation and co-operation in the use of transport and production facilities. Given the uncertainty regarding the emergence or – more specifically – the timing of the emergence of substantive demand of the industry, further opportunities for co-operation should be pursued.

Financial pressures appear to have abated somewhat, though this is possibly due more to some company closures and action on the part of some companies in the sector to rationalise and restructure. For some individual companies, the recommendations remain valid.

12. The industry should make stronger representation to customers and specifiers to ensure that construction materials used on building works should comply with all relevant regulatory requirements and that an audit trail should be a requirement of all construction works to ensure that only compliant materials are used.

Inside Back Cover.

Back Cover

Irish Concrete Federation
Set for life

QPA Northern Ireland
Providing Essential Materials

InterTradeIreland
Discover what's possible