# Escalating cost - a major headache

## To overcome the pain, developers, contractors, building material makers and Government ought to work together


THESE are challenging times. The construction sector in Malaysia will attest to this, as will property developers.

With prices of building materials in an upward spiral, all those connected to the building industry are finding themselves caught in a bind.

Contractors who agreed to building projects when the cost of raw materials were much lower are now finding it next to impossible to complete those jobs without losing money.

Industry bodies like the Real Estate and Housing Developers' Association (Rehda) are afraid that as construction costs keep creeping up, many projects may be postponed or stopped altogether.

If contractors become insolvent as a result of their inability to finance the higher costs of raw materials, and building projects get abandoned, the ramifications for the industry, and for the economy as a whole, will be far-reaching and severe.

The construction industry has vital linkages to many industry and professional services, such as banks which have loaned huge sums to contractors, developers and home buyers; all of which will have to bear some measure of the knock-on effect, should work come to a standstill.

Currently, we are looking at cost escalations of about 30%. The biggest rise in prices have come from steel bars and cement.

In early July, steel bars cost RM4,100 per tonne compared with RM3,500 just a month before. Cement was RM13.45 a bag up from RM10.95 the previous month.

There is currently a shortage of steel and cement; prices of building materials are being pushed up by strong demand.

Worldwide, rising demand for essential building materials continue unabated, driven in part by the continued property boom in the Gulf states and our neighbouring countries.

However, it is not just building materials that have been responsible for rising construction costs.

Last month's removal of the fuel subsidy, which caused petrol and diesel prices to go up by about 40% has also hit the construction industry hard.

Contractors routinely depend on heavy machinery such as mobile and tower cranes, bulldozers, off-highway trucks, all of which require fuel to run.

Subsequently, electricity tariffs went up by 18%, which adds to the burden that developers and contractors already face.

Higher prices will surely erode the profit margins of both contractors and property developers and, in many cases, those companies that are unable to bear the higher costs will go out of business. Only the strongest will survive.

Some contractors who are unable to complete their projects due to escalating prices may decide to abandon the job rather than suffer losses.

For developers to ensure that those properties which have already been sold, are completed and delivered to the respective buyers on time so that they are not liable for liquidated damages, developers have little choice but to bear the price increases and work closely with their contractors to ensure smooth progress of the developments.

One way that developers can assist contractors is by providing for cost variations in contracts for the prices of raw materials like cement and steel, so that current fluctuations in costs are matched.

Developers should also pay their contractors promptly to facilitate their purchases of building materials.

On the other hand, one needs to be aware that there may be contractors who may take advantage of rising costs as an excuse to ask for an upward revision of their contracts.

Eventually, of course, the cost of houses will need to be adjusted upwards and homebuyers will have to pay more for new homes.

Still, some analysts doubt that there is sufficient room for passing on this increase because inflationary pressures are already eating into household disposable incomes.

However, it is likely that house prices will be adjusted before the year is out.

It is likely that growth in the construction sector will be revised down from Bank Negara's March forecast of between 5% and 65 to about 4.5%.

To overcome this crisis, it is imperative that all developers, contractors, building material manufacturers and the government work together as a team.

The government is considering cutting the tax on building materials and reducing stamp duty charges for sales and purchase agreements.

The Master Builders Association of Malaysia (MBAM) has petitioned the government to stockpile steel and cement to help supply and stabilise prices.

Contractors have also asked for the 10% import tax on cement to be abolished and, instead, for an export duty to be imposed on essential building materials.

Material manufacturers, in particular, should try to fulfil local requirements for their materials first before looking at overseas markets.

By giving priority to the local market, they may forfeit short-term profits but will contribute towards the long-term economic well-being of the country as a whole.

Industry bodies should also take the lead in working with the government to determine the best way forward for all.

Property prices in Malaysia are a steal compared with other countries in the region. While the government has been promoting Malaysia as a favoured destination to live in with the Malaysia My Second Home scheme, it needs to focus on boosting confidence levels so that we continue to enjoy more foreign investments.

In order to achieve the kind of environment conducive to investments, we need a politically stable environment with long-term policies that are transparent and favourable to business.

Policies, once implemented, should not be changed too quickly. Investors need this commitment to accurately analyse risks and probable returns.

We are faced with a crisis. We must all step up, work together and find the best solutions to ease the burden, all around.

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