Developments in the Construction Sector of Maldives

*by: Mariyam Rashfa**

Introduction

The construction sector of the Maldives has witnessed unprecedented growth in recent years. In particular, its contribution to GDP has increased from just 6% in 2002 to an average of 9% between 2003 and 2007, peaking at 12% in 2007. During this period, the average growth of the sector also increased significantly from an average of 11% (between 1996 and 2000) to 27% driven by a number of factors. This includes the launching of large scale public infrastructure projects such as the development of Hulhumale', rapid urbanisation, changes to land laws, introduction of housing finance schemes and the massive repair and reconstruction efforts following the 2004 tsunami. In addition, the commencement of large scale construction projects following the leasing of several new islands for resort development since 2004 also contributed to the growth of the sector. However, with the end of the tsunami reconstruction boom and the onset of the global financial crisis, the construction sector registered a marked turnaround in 2009. Since then the growth of the sector has remained rather volatile, declining twice between 2009 and 2012 owing to various problems and challenges faced by the sector.

Against the backdrop of these developments, this article will provide an overview of the construction sector of Maldives highlighting some of its key features and factors behind the rapid growth of the sector during the boom years. It will also identify the main challenges facing the sector and provide some concluding remarks on the outlook for the sector.

Key Features of the Industry

The construction sector is a vital sector of the Maldivian economy. It contributes significantly to GDP and plays an important role in delivering the basic infrastructure needed for socio-economic development. In this regard, it covers the construction of roads, highways, harbours, ports, bridges, tunnels and other civil works and also the building of factories, houses, offices, schools and apartments. In addition to the direct contribution of construction industry to the economy the sector also contributes indirectly through its linkages to other sectors of the economy ranging from the suppliers of construction materials, architectural and real estate services. Apart from the positive contributions of construction sector to the Maldivian economy, it is also important to note the sector's excessive reliance on imports and its negative impact on the country's balance of payments.

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Output

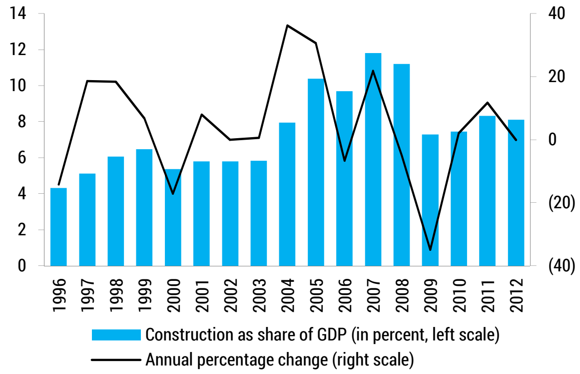
An important characteristic of the construction sector is the cyclical nature of construction activities as it depends to a large extent on government programmes; business and consumer confidence; and financing conditions or availability of credit. As a result, this often makes the output of the sector subject to large fluctuations in the business cycle (Figures 1 and 2) and other external developments. For example, in the case of Maldives, the developments in the construction sector are closely linked to developments and capacity expansions in the tourism sector while it is also highly influenced by government spending on infrastructure development. Another important feature of the construction sector of the Maldives is the dependence of the sector on imports since almost all building materials such as cement and aggregates, base metals and wood have to be imported. This also makes the industry highly vulnerable to fluctuations in global commodity prices and changes in the exchange rate.

Employment

The activities in the construction sector are very labour intensive making it a significant contributor to industrial employment in many countries[1]. According to the Household Income and Expenditure Survey 2009/2010, the construction sector employed about 5% of the total local labour force in 2010. Of the total workforce of the construction industry, expatriate employment accounted for 88% in 2010 compared to 75% in 2006. While there has been a slight decline in the number of locals employed in the construction sector between 2006 and 2010, the number of expatriate employment in the sector nearly doubled during this period highlighting the excessive dependence of the sector on expatriate workers (Figure 3). With the large increase in expatriate labour force, the construction sector has also has now become the single largest

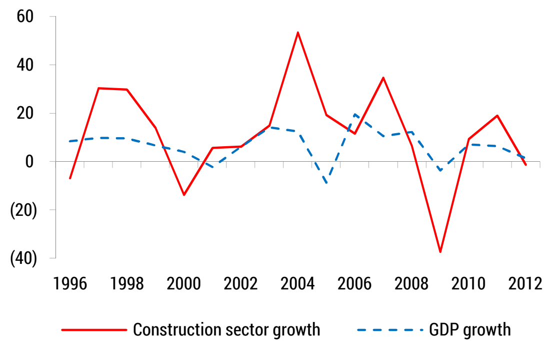
1 The construction industry is Europe's largest industrial employer, accounting for about 7% of total employment. In the European Union, the US and Japan combined employs more than 40 million people. Among all OECD countries, the construction industry accounts for an average of 6.47% of GDP (OECD).

Figure 1: Construction Industry's Contribution to GDP, 1996 - 2012



Source: Department of National Planning

Figure 2: GDP and Construction Sector Growth, 1996 - 2012
(annual percentage change)



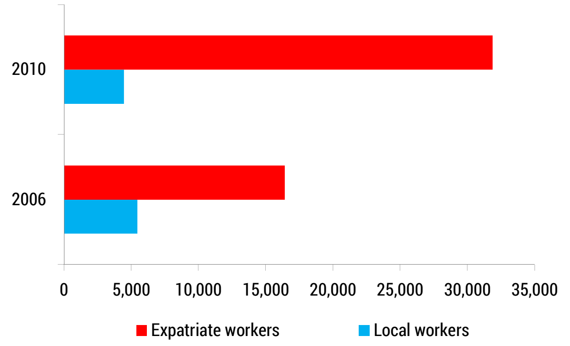
Source: Department of National Planning

employer of the country's expatriate labour force (accounting for 43%). Although most expatriate workers in the construction industry are employed as labourers, a significant portion is also employed under the skilled crafts category, partly reflecting shortages in local craftsman. As for the nationality of expatriate workers, majority of them are from neighbouring countries of Bangladesh, India and Sri Lanka at a cheaper cost, since the cost of living in these countries is much lower than the Maldives (Figure 4). However, in recent years there has also been an increase in the number of skilled crafts level workers from South East Asian countries, namely Indonesia. This mainly reflects difficulties in obtaining such labour from India, which used to be the traditional source of such labour to Maldives.

Enterprises

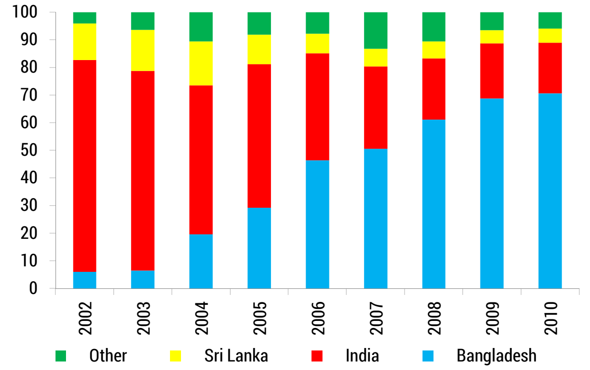
The construction industry is generally characterised by the existence of a number of small and medium enterprises (SMEs). According to the Economic Survey conducted by the Department of National Planning in 2007, there were a total of 1,638 establishments in the construction industry of Maldives in 2007. 12% of these establishments were classified as small (employing less than 10 workers), around 50% as medium (employing 10-99 workers) and the remaining 38% as large firms (employing over 100 workers). Although most of the firms were classified as SMEs, over 70% of industry workforce was employed by the larger firms which generated about 90% of the industry turnover and value added. While most major construction projects are undertaken by the larger firms or a general contractor, a considerable portion of the work are sub-contracted to smaller and more specialised companies or groups. This is because of the dynamic nature of different construction projects and the specialised skills required in performing the jobs. For example, resort construction projects require a high level of craftsmanship and are often managed by a general contractor or a project coordinator (usually the owner of the resort) who sub-contracts certain aspects of the project to smaller more specialised groups.

Figure 3: Local and Expatriate Employees in the Construction Industry, 2006 - 2010



Source: Department of National Planning

Figure 4: Expatriate Employment in the Construction Industry by Nationality, 2002 - 2010
(in percent)



Source: Department of National Planning, 2003 - 2012

The Construction Boom of 2004-2008

Starting from the early 2000s until 2008, the construction sector of the Maldives witnessed a boom driven by both private and public sector activity. During this period activity across all major types of construction projects witnessed expansions. For example, residential construction grew markedly, particularly in Male' and Hulhumale' reflecting the natural growth of the population, rapid urbanisation due to in migration from outer islands, improvements in direct supply of social housing by the government and the facilitation of affordable housing through provision of land and introduction of housing finance schemes. During this period growth of construction sector was also fueled by the launching of post tsunami reconstruction efforts and the commencement of large scale resort construction projects, following the leasing of several new islands for resort development by the government since 2004.

The following discusses the main factors behind the construction boom.

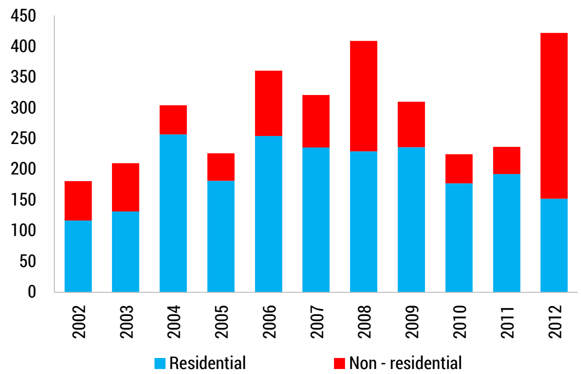
Urbanisation

With the capital Male' being the main commercial hub of the country, each year a large number of people from the outer islands continue to migrate to Male' looking for employment opportunities and better health and educational services. This has led to rapid urbanisation and a large increase in the demand for rental accommodation in Male', fueling the growth of residential construction (Figure 5). According to official estimates, the population of Male' has grown by 44% between 2002 and 2009 while the number of households living in rented accommodation more than doubled during this period.

Government Policies Influencing Housing

- *Development of Hulhumale'*: The Hulhumale' development project was initiated by the government to alleviate the acute housing congestion problem in the capital region Male' and to address the severe shortage of land for housing and industrial development. Hulhumale' is a reclaimed island located 3 kilometers from the capital Male'. The reclamation of Hulhumale' began in 1997 and was completed in 2002. With the completion of primary

Figure 5: Buildings Authorised for Construction by Floor Area in Male', 2002 - 2012
(in thousands of square meters)



Source: Department of National Planning

developments, which includes 280 residential units, 48 commercial units, major road network and main social and utility infrastructure, the first inhabitants settled in Hulhumale' in the middle of 2004 with a resident population of just over 1,000 people. Since then, several plots of land has been allocated to private sector as well as government agencies for private housing, condominium housing, social housing, institutional development and social infrastructure development (Table 1). The estimated population of Hulhumale' in 2010 was 12,000.

- *Land reforms:* The enactment of the first ever land law in 2002[2] and the introduction of individual registration of units in a building (condominium registration or strata titling) where individual units could be mortgaged, sold and or given with title has facilitated ownership housing in the country. Consequently, this has improved the availability of land and access to bank credit for housing development (Figure 6) boosting residential construction activities in the Male' region. Nonetheless, it should be noted that at the time of its implementation, the Land Act (2002) lacked regulations that promote the security of tenure and property rights which are important requirements for the creation of real estate and housing market.

- *Establishment of housing finance schemes:* Limited availability of housing finance and affordability has been a key impediment to the development and growth of residential construction in the country. To address this issue, the Housing Development Finance Corporation (HDFC) was established in March 2004 as a state-owned enterprise with the purpose of providing financing for housing with terms more favourable than commercial banks. During its initial years, the HDFC had limited capacity to cater for increasing need for financing due to limited financial resources available to them. However, following its privatisation in July 2008, with the government share reduced to 49% and with new lines of long terms credit, the HDFC re-entered the market for mortgage loans for individuals and families during February 2009. With these changes HDFC offers both developer and end user financing with efforts made to enable the poor and disadvantaged to have access to the facilities offered.

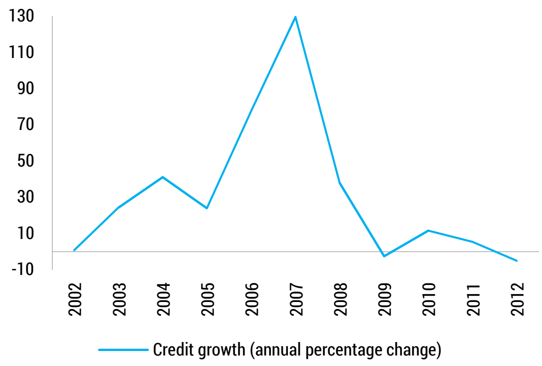
Table 1: Ongoing and Completed Residential, Commercial and Industrial Developments in Hulhumale', 2004 - 2012

	2004	2006	2008	2010	2012
Residential					
Apartment units	280	120	-	183	-
Apartment complex plots	-	-	6	-	-
Residential plots	222	254	-	-	150
Row houses	-	64	-	12	30
Social housing units	-	504	-		1000
Condominium units	-	232	-	-	-
Commercial					
Commercial units	48	-	58	-	10
Mini mall	-	-	-	-	1
Garage units	-	-	-	10	-
Industrial					
Industrial plots	54	-	62	-	-

Source: Hulhumale' Development Corporation

2 Including its subsequent revisions in the years that followed.

Figure 6: Commercial Bank Credit to Construction and Real Estate Sectors, 2002 - 2012



Source: Maldives Monetary Authority

- *Direct delivery of social housing by the government:* Until the early 2000s, activity in the residential construction has been dominated by private housing projects (mostly individuals). However, with the aim of providing affordable housing to its citizens, the government has recently increased its involvement in the direct of supply of social housing. This is targeted to the most vulnerable and disadvantaged groups of the society and also to part of the low to lower middle income categories. Most of the government housing projects has been undertaken in Hulhumale' whereas some major projects have been initiated in Male' as well as in other urban centers in the atolls. These projects have been financed either by the HDFC, foreign loans, public private partnerships or directly from the government budget.

Launching of Post Tsunami Reconstruction Efforts

The tsunami which hit the Maldives in December 2004 caused considerable damage to housing and major infrastructure across the country including several resort islands. According to official figures, more than 8,500 housing units were damaged or completely destroyed by the tsunami. Of these, 5,700 houses required repairs and 2800 new houses needed to be reconstructed. Harbours and jetties in a total of 104 islands also required reconstruction. Meanwhile, health facilities on 40 islands and educational infrastructure totaling US$15.5 million were damaged or destroyed by the tsunami. Hence, the massive reconstruction and rebuilding efforts that followed in the immediate aftermath of the tsunami caused a boom in construction activity throughout the country between 2005 and 2008. Despite considerable delays, mainly owing to significant escalation in material prices (which more than doubled), most of the repair and reconstruction of houses and social infrastructure were complete by the end of 2008.

Leasing of Several New Islands for Resort Development

The construction, repair and refurbishment of resorts have been an important driver of construction sector growth since the inception of the tourism industry in 1972. The tourism sector is the single most important sector of the economy and directly accounting for around one third of the economy. The rapid growth of tourist arrivals over the years has resulted in a substantial expansion in the number of tourist accommodation facilities in the country. In particular, since 2004 there has been a steady increase in the number of resorts operating in the Maldives (Table 2) reflecting the leasing of several new islands for resort developments by the government. Overall, these new leases have allowed for an additional bed capacity of 7,712. However, the resort construction market, which relies extensively on external funding, registered a major setback in 2009 due to the global financial crisis and domestic downturn. Since then, activity in the resort construction segment has remained weak mainly reflecting the funding difficulties faced by resort developers after the global financial crisis.

Challenges and Outlook

The construction sector of Maldives is at present undergoing a weak phase in its business cycle. After witnessing a strong period of growth, the sector has registered a marked turnaround since 2009. The growth of the sector remains rather volatile and has declined twice between 2009 and 2012 due to various problems and challenges facing the sector. While most of these challenges reflect dynamic changes taking place in the business environment, particularly after the global financial crisis and the domestic downturn, some of these problems relate to various capacity constraints facing the sector. More specifically, the main problems facing the sector include the scaling back of government infrastructure projects on the back of budget constraints; increasing price of construction raw materials due to fluctuations in global prices; payment delays for contractors; challenges in obtaining finance by resort developers; difficulties in access to finance, constraints in obtaining foreign exchange from the formal banking sector and shortages in skilled labour. Apart from the industry specific issues, broader problems relating to the macroeconomic and regulatory environment also seem to have further lowered investor confidence, thereby hindering the ability to attract foreign finance for the construction projects.

Looking ahead, the long term prospects for the Maldivian construction sector will largely depend on the ability of resort developers and the government to secure finance for the ongoing projects and those in the pipeline, while also addressing the various challenges faced by the construction sector in a timely and cohesive manner.

Table 2: Number of Resorts and Bed Capacity, 2000 - 2012

Year	No.of resorts	Operational bed capacity	Bed capacity growth
2000	86	15,812	8%
2001	87	16,478	4%
2002	87	16,131	-2%
2003	87	16,692	3%
2004	87	16,621	0%
2005	88	13,946	-16%
2006	89	16,175	16%
2007	92	17,511	8%
2008	94	19,081	9%
2009	97	20,137	6%
2010	98	23,649	17%
2011	101	24,490	4%
2012	105	25,062	2%

Source: Ministry of Tourism, Arts and Culture

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