Construction: how Volcker brought the house down

by Lydia Schulman

When Federal Reserve Chairman Paul Volcker inaugurated phase one of his credit restraint program last Oct. 6, the National Association of Home Builders (NAHB) responded with disbelief and braced for the worst. The association stated that the entirely predictable results of the credit measures would be a precipitous drop in new housing starts down to 1 million units per year—50 percent drop from 1978 levels—and mass unemployment in the construction industry.

Those predictions have come true with a vengeance. Those types of construction immediately related to maintaining and enhancing the standard of living of the U.S. population—the single-family home, middle and low income apartment dwellings, hospital and schools, and nuclear power plants—are in a nose dive.

In March, starts of new private homes fell to a seasonally adjusted annual rate of 1.04 million, down 42 percent from March 1979. The number of construction workers employed in residential construction has plummeted by over 163,000 since a peak last August—a 28 percent drop. No one is pretending that this is a merely "seasonal" phenomenon. Record high interest rates and the collapse of the bond market have been the *coup de grace* for the U.S. nuclear industry. Besieged alternately by unwashed greenie demonstrators and spiraling interest rates, the Public Service Co. of New Hampshire was forced to begin laying off half of the 4,700 construction workers at Seabrook in March. Plans for at least 13 nuclear facilities were cancelled or shelved for the same reasons this past winter.

Industrial and commercial construction have not been significantly affected—yet. In these areas of the construction industry, where projects have long lead times and construction spans several years, builders report that they are still working off contracts that were signed in early 1979 before the Volcker tight money regime began. If interest rates do not come down significantly below 17 percent by this coming October, these builders report, there will be a sharp ratchet in both commercial and industrial contract construction.

Cutbacks in federal spending since 1975 have leveled public spending on hospitals, schools, and other essential infrastructure. The bulk of the cuts proposed in the Fiscal 1981 budget are to come out of federally funded construction projects: Army Corps of Engineer projects, water resource projects, airport construction grants and road building. But even before these budget cuts hit, the Federal Highway Administration is expected to run clear out of money by this summer, leaving states in the lurch for $1.4 billion in let contracts.

Housing: a calculated collapse

One of the first calculated consequences of the Volcker credit squeeze was to dry up mortgage money, or, what amounts to the same thing, to price it out of the reach of most prospective home buyers. In the state of California, one of the 24 states without usury laws, mortgage rates were holding firm at 17.5 percent at last count, even though certain other interest rates have come down a bit.

The dizzying rise in mortgage rates this past winter has resulted in an even more dizzying rise in monthly mortgage payments. In January 1979, the median price of a single family home in California was $79,599, the prime mortgage rate was 10⅜ percent, and the monthly mortgage payment was $577. In January 1980 the price of the same house was $97,957, the mortgage rate was 13 percent, and the monthly mortgage payment was $1,170. (These figures are from an in-house report in preparation by Crocker National Bank in San Francisco.) Over the 30 year life of the mortgage, the homeowner will have paid $414,000 in interest and principal payments for the $97,957 house!

In many states mortgage money has simply been nonexistent. Unpublished figures compiled by the Federal Home Loan Bank Board indicate that the federally insured savings and loan institutions made fewer mortgage commitments to prospective homebuyers this past March than at any time since such statistics started being kept in 1976. In the first quarter of the year the S&Ls had the lowest net inflow of deposits in a decade, a situation which is not likely to improve, because, even if interest rates ebb and flow over the months ahead, high interest rates are here to stay.

The "growth" areas

The Carter administration does have a construction program of sorts—one which is guaranteed to feed the nation's double-digit inflation since it adds nothing to the production of tangible wealth.

In Houston, Texas, in a pattern typical of the oil producing and refining regions of the country, a new "growth" area has opened up for construction in the maintenance and refitting of old oil refineries. At the present time, approximately one-third of the industrial construction workforce in the area—around 10,000 workers—is engaged in the maintenance and revamping of refineries to outfit them to process domestic crude oil with its high sulphur content.

The state of Utah—an open shop state like Texas, has been promised billions upon billions of dollars in future construction contracts related to the production of synthetic fuels and the MX missile system. At the present time about $1 billion in synthetic fuel-related construction contracts are in progress or have been let out in what is known as the "overthrust belt," the mountainous region encompassing parts of Montana, Idaho, Wyoming, Utah, and Colorado. This figure could easily triple by the end of 1981, according to area contractors.

Also on the agenda in Utah: construction of the Intermountain Tower Project is expected to start up next year. When completed, the ITP will be the largest coal processing plant in the country. Projected time of the project is seven to eight years and the cost $4 billion.

The possibility of the $50 billion MX missile system also holds out the promise of billions of dollars in future construction projects for Utah, according to some. The cost analysis study done by the General Accounting Office on the system indicates that 60 percent of the $50-to-52 billion in projected costs will be in construction.

The basing of the missile system in Utah has been opposed by forces in the state who do not like the war-preparation implications of the system and who do not want to see their state torn up to house it. The "race-track" design for the system advanced by the Airforce involves the construction of a vast underground railway system in the Utah desert over which the missiles would be constantly moving—ostensibly out of reach of Soviet bombers. Currently making the rounds in Utah is the joke that there is really no need for this elaborate subway system; the Airforce should just give the missiles to Amtrak and then the Russians will never be able to find them.

Construction by sector