



Fall 2014 /  
Winter 2015



# BUILDING FOR THE FUTURE

CONSTRUCTION ECONOMICS  
Market Conditions in Construction

EXECUTIVE SUMMARY



# Summary

## CONSTRUCTION GROWTH LOOKING UP:

Construction spending for 2014 is expected to finish the year 5.4% higher than 2013. All sectors will contribute to the growth.

Cash flow of new starts for nonresidential buildings indicates a 15% increase in the monthly rate of spending over the next 10 months.

A correlation between the Architectural Billings Index (ABI), Dodge Momentum Index (DMI) and new starts cash flows has twice predicted the direction of nonresidential buildings spending over the last two years. Current forward look shows a flat period in Q4 2014 then a rapid rise in 2015.

The U.S. gained 290,000 construction jobs over the last 12 months. Construction jobs are up 13% from the low point. Jobs plus hours worked show that total labor effort is up 18% from its lowpoint. More than forty percent of the total increased labor effort in the last four years is due to added hours.



### ➔ FIGURE A:

#### All Construction Spending Rate of Growth 2013-2015

Total spending of ALL types of construction will grow 5.4% year over year from 2013 to 2014. We started 2014 at an annual rate of spending near \$950 billion and finished at a rate of \$990 billion.

As expected, non-residential buildings contributed to the dips in March and June in 2014, but helped lead the expansion for the second half of 2014.



## **SOME ECONOMIC FACTORS ARE STILL NEGATIVE:**

- Real inflation adjusted constant construction volume is still 22% below peak and has not yet returned to the level of volume in 1993. At the historical rate of volume growth, it will take seven to eight more years to regain previous peak volume levels.
- Currently there are 6.1 million jobs and the total workforce is near 6.7 million, still near a 15-year low, about 1.5 million (18%) lower than the 2006-2007 peak. Since January 2010, between 400,000 and 700,000 workers have left the workforce.
- As workload expands in the next few years, a shortage of available skilled workers will continue to drive up labor cost and have a detrimental effect on schedule.
- In a recent Associated General Contractors (AGC) survey of contractors, 80% indicated some difficulty in acquiring trained workers.

## **THE EFFECTS OF GROWTH:**

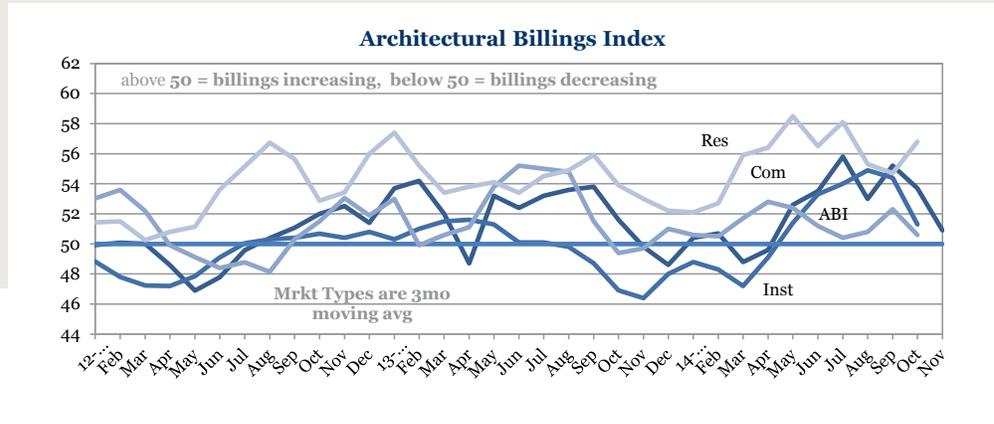
- Contractors gain more ability to pass along costs and increase margins as spending continues to increase. Selling price indices for 2013 and 2014 show contractors' as built price both years is above labor and material cost inflation. Margins are increasing.
- Since the low point in January 2011, spending has increased 25%. Construction labor effort has increased by 18%. However, spending corrected for inflation shows construction volume has increased by only 10%. Productivity is declining.
- Growth in nonresidential buildings and residential construction in 2014 and 2015 will lead to more significant labor demand. This may lead to labor shortages and productivity losses.
- Margins regained a positive footing in 2012 and extended those gains in 2013. Margins increased in 2014 and margins are expected to grow even stronger in 2015.
- When activity picks up in all sectors, escalation will begin to advance rapidly.

**“In 2014, the U.S. showed a productive increase of 290,000 construction jobs!”**



**FIGURE B:**

**Architectural Billings Index 2012-2014**



*The most favorable forward-looking conditions I've seen in years support my expectations for strong growth and profits in 2015. Very active markets will drive escalation to climb more rapidly than we have seen in six years.*

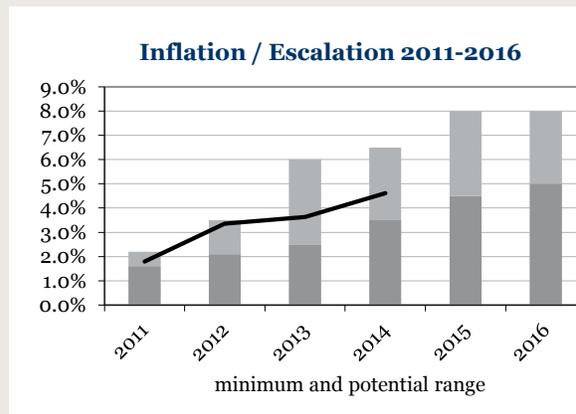
**IMPACT OF RECENT EVENTS:**

There are several reasons why spending is not rapidly increasing:

- public sector construction remains depressed
- public educational spending is the single largest contributor to the drop in public spending
- lenders are just beginning to loosen lending criteria for project financing but are not providing equal terms to lend working capital to subcontractors
- consumers are still cautious about increasing debt load, including the consumers' share of public debt
- we may be constrained by a skilled labor shortage

**FIGURE C:**

**Inflation / Escalation 2011-2016**



In order to capture increasing margins, future escalation will be higher than normal labor and material cost growth. Lagging regions will take longer to experience high escalation. Residential escalation is currently near, or even above, the upper end of the range.

- We advise a range of
- 3.5% to 6.5% for 2014
  - 4.5% to 8% for 2015
  - 5.0% to 8% for 2016

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The information in this report is not specific to any one region. The information is limited to the United States and does not address international economic conditions.

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## Data Sources

Along with countless news articles, these sources are used for data in this report:

- American Institute of Architects – [www.AIA.org](http://www.AIA.org)
- American Iron and Steel Institute - [Steel.org](http://Steel.org)
- American Recycler - [AmericanRecycler.com](http://AmericanRecycler.com)
- Associated Builders and Contractors - [ABC.org](http://ABC.org)
- Associated General Contractors of America - [AGC.org](http://AGC.org)
- Bloomberg L.P. Financial News - [Bloomberg.com](http://Bloomberg.com)
- Bureau of Labor Statistics - [Stats.BLS.gov](http://Stats.BLS.gov)
- Construction Industry Round Table – [CIRT.org](http://CIRT.org)
- Data Digest – [DataDigest](http://DataDigest)
- Economic Cycle Research Institute - [BusinessCycle.com](http://BusinessCycle.com)
- Engineering News Record - [ENR.com](http://ENR.com)
- Financial Trend Forecaster - [Fintrend.com](http://Fintrend.com)
- FMI Management Consulting - [FMINET.com](http://FMINET.com)
- IHS Global Insight - [IHS.com](http://IHS.com)
- Institute for Supply Management - [ISM.ws](http://ISM.ws)
- McGraw Hill – Dodge – [Construction.com](http://Construction.com)
- Metal Prices – [MetalPrices.com](http://MetalPrices.com)
- Producer Price Indexes - [BLS.gov](http://BLS.gov)
- CMD (formerly Reed Construction Data) - [CMDgroup.com](http://CMDgroup.com)
- RS Means - [RSmeans.com](http://RSmeans.com)
- U.S. Census Bureau - [Census.gov](http://Census.gov)

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