



# Slow and Steady

ECONOMIC OUTLOOK SEES  
THE CONSTRUCTION GLASS AS HALF FULL

BY SHERYL S. JACKSON



## **A concern throughout the industry is availability of construction workers if there is a significant upturn in construction spending.**

**IT'S A GOOD NEWS, BAD NEWS** situation. The good news is that September 2013's construction employment was up 3.4 percent over 2012 and construction spending reached a four-year high of \$915 billion, a 7.1 percent increase over 2012. While experts anticipate this course to continue throughout 2014, no one foresees dramatic increases.

Ken Simonson, chief economist of AGC of America, sees good but uneven growth, fueled in part by three areas that are helping many sectors and regions:

### **1. "SHALE GALE"**

Extraction of shale gas through a drilling process known as hydraulic fracturing or "fracking" is not only building supplies of natural gas to produce energy but is also having a positive effect on the construction industry. "States including Pennsylvania, South Texas, Colorado and North Dakota are experiencing an increased need for roads, site preparation, housing for the machinery, pipelines and storage tanks associated with the drilling operations," explains Simonson. Along with construction directly related to the drilling site, there is increased spending from employees visiting restaurants, renting houses and purchasing from local stores. This economic lift to the local towns can result in renewed construction activity in the town.

### **2. PANAMA CANAL**

Even though the Panama Canal is not a U.S. construction project, the 2015 opening of the new locks that can handle larger container ships has led to the deepening and widening of harbor channels in U.S. port cities in preparation for the super-sized vessels. In conjunction with harbor projects that will allow the ships to dock, port authorities are expanding their storage yards and lengthening piers. Inland

transportation projects include improving rail systems and roadways to and from the port to accommodate increased truck traffic, as well as raising bridges and building tunnels.

### **3. RESIDENTIAL REVIVAL**

A surge in single family (32 percent) and multifamily (49 percent) new construction in August 2013 were partly driven by a 7.2 percent increase in house prices from mid-2012 through the second quarter of 2013. This increase encouraged new residential construction. "I believe single-family growth will flatten in 2014 due to tight credit and demographic shifts," says Simonson. "Multifamily construction's upturn should last through 2014 due to low vacancy rates in most cities and a fear of locking into a long-term mortgage when the job market is still unstable."

Another positive sign for multifamily construction is a growing preference for urban living, which is evident in Washington, D.C., says Terry Edmondson, project executive at DPR Construction, a member of several AGC chapters. "Young professionals want to live in the city so we are seeing growth in the Rosslyn and Ballston areas of Arlington, Va.," he says. "Multi-use construction is in high demand in these areas."

Pent-up demand is another reason some areas will see construction growth, says Edward Zarenski, estimating executive for Gilbane Building Company, a member of multiple AGC chapters. The uncertainty of the economy in recent years has put construction projects on hold, but the need for those buildings or those roads has not diminished, he points out. "Organizations that have access to private funds will start to build."

Just as he sees three areas that are supporting growth, Simonson also identifies three factors that are suppressing it:

### **1. LESS GOVERNMENT SPENDING ON SCHOOLS AND INFRASTRUCTURE**

At the federal level, funding for highway and infrastructure improvements or replacements is still uncertain, points out Simonson. "MAP-21 [Moving Ahead for Progress in the 21st Century Act] is only funded through 2014 and the Highway Trust Fund is supplemented with transfers from the general fund." As automobiles become more fuel efficient, people are paying less gas tax, which has been the primary source of funding for the Highway Trust Fund. "At this time, there is no indication that additional taxes will be approved, even though gas receipts are dropping."

**Read "On the Bright Side" on Page 16 for more information on the workforce shortage and what some AGC members are doing to combat it.**

Declining tax revenues are also the reason schools are not being built, points out Zarenski. "Until tax revenues return to the levels seen four or five years ago, public school boards do not have the funds to build new schools."

While public schools may not be adding to their facilities, educational institutions with access to private money will begin to build soon, says Zarenski. "Harvard University is a good example of an institution that uses private funds for construction but postponed projects during the past few years due to the uncertainty of the economy," he points out. "They are

building again because the demand that was there three years ago is still there and they have the funds.”

Private funds may also play a part in infrastructure construction. Elaine Ervin, CPA, national practice leader for the construction industry at Moss Adams, an AGC member of multiple chapters, predicts a growth in public-private partnerships to address infrastructure needs such as highways and bridges. “There is a demand for these projects that have been put on hold but public funds are not available.”

## 2. CONSUMER SWITCH FROM STORES TO ONLINE BUYING

The growth of suburbs resulted in construction for retail stores that were convenient to new neighborhoods. Now, with the rise in online purchasing and the collapse of the home market in suburbs, there is less need for retail space, says Simonson. “Shopping center vacancy rates are high and center managers are turning to innovative uses of space for leases, such as community colleges or exercise and yoga programs.” The growth in online purchasing has spurred new construction of warehouse and distribution centers but that is a small percentage of previous retail construction.

## 3. SPACE FOR EMPLOYEES AND SERVICES SHRINKING

Even when office buildings are leasing, companies are leasing smaller facilities because they are allocating less space per employee, says Zarenski. “An employer that previously located 300 employees on a floor now has 400 employees on the floor.”

Healthcare is also changing the way services are offered, Zarenski points out. “Instead of building hospitals or larger buildings, services are provided in urgent care centers located in shopping center space, or in clinics located in existing retail stores.”

The uncertainty of healthcare reform has caused some of the slowdown in healthcare construction, says Edmondson. “Health systems with plans to build are holding their cash close to their vest until they know more about how changes in the industry will affect them.” He adds, “The aging population creates a demand for health services, but how many of those

consumers will receive assistance in a long-term care facility as opposed to an acute care facility?”

## BUDGET REQUIRED FOR STRONGER GROWTH

When asked what is necessary to create a stronger construction recovery, Ervin suggests that a federal budget must be approved. “Investors are hesitant to commit funds when there is so much uncertainty about the country’s finances,” she says. “Good or bad, a budget enables people to plan and to move forward.”

Job growth outside construction is another factor that will contribute to construction growth, says Zarenski. As more people become employed, there will be more demand for housing and other services.

A concern throughout the industry is availability of construction workers if there is a significant upturn in construction spending. “The availability of employees differs from state to state,” says Zarenski. “In Rhode Island, we’ve recovered only 4 percent of the jobs lost in the construction downturn but Boston has recovered 75 percent of construction jobs lost.” The good news for Rhode Island and Boston is experienced construction employees in Rhode Island are available to work in Boston, he says. “The challenge for all contractors will be finding good employees to replace those who left the area to find work, or left the construction industry.”

Because construction companies have had to do more with fewer employees and have adopted new technologies, such as building information modeling (BIM), that require fewer employees, contractors should be able to find workers, says Edmondson. “The real concern is the number of Baby Boomers who are nearing retirement or who have left the industry,” he says. Another disadvantage of Baby Boomers’ retirement is the fact that few young people want to enter skilled trades, he says. “A lot of young people want to work in the technology side of construction, not carpentry.”

“Contractors know they are losing institutional knowledge and I’m seeing some companies take steps to prepare younger employees,” says Ervin. Enhanced training and mentoring programs enable employees to learn from

each other, she points out. Working with local technical schools to provide internships not only generates interest in the industry but also creates a pool of potential employees.

“I’ve also seen an increased interest in improving how contractors work,” says Ervin. “More construction companies are embracing Lean construction principles to be more efficient, more competitive and more thoughtful about work.” BIM is a more widely adopted innovation that enables contractors to cut and assemble pieces before they reach the jobsite, she adds.

**A key to improving construction productivity will be industrialization of the industry, says Dr. Perry Daneshgari, president and chief executive officer of MCA, a strategic consulting firm with an expertise in productivity improvement. Fabricating components of a building at a production site and transporting them to the building site is a way to improve quality and productivity, he says.**

**Building in a factory setting is also an effective way to attract and keep skilled labor, points out Daneshgari. “You can more easily train someone to work in a factory setting because the task is repetitive and predictable.” Older employees are more likely to stay in the workforce longer if a factory setting is available because, generally, the work is less physically demanding.**

## Additional information on trends in prefabrication can be found in the article on Page 16.

Even with a slow and steady upturn in construction activity, there is one pitfall contractors must avoid, warns Ervin. “Labor intensive contractors must be careful when ramping up,” she says. “They get overly optimistic about the number of new jobs and their cash flow suffers.” Adding employees that will be paid every two weeks, when payment for the project might be 90 days out puts a strain on anyone’s cash flow situation, she says. “Make sure you understand your cash flow needs and be sure you have cash in hand or have a plan to use your line of credit.” ♦