

23rd Weekly Crisis-era Message to Contractors from: Dr Tom Schleifer
Reader Questions and Answers

Question: *Dr Schleifer, If our industry lags the economy by 12 to 18 months and the economy is still headed downward so that recovery is at least a year away, does that mean it's two and a half years before we even start to recover? And how long is the recovery cycle? That is, how long will it take to return to 2019 levels?*

I was tempted to avoid this question because the subject is complicated and it requires a long response, but there were a number of similar inquiries about the timing. There seems to be some confusion possibly because I address the lag time in so many different contexts and readers may not clearly differentiate between the "US economy" and the "construction market". The foundation of this topic is that the construction market is cyclical and follows the US economy almost in lockstep but lags it.

When the US economy cycles down, the construction market continues to grow (or flatten out) for a minimum of one year (the lag) and then cycles down. The reason is that the majority of the construction projects in progress and those already funded continue through completion; and the average length of construction projects, being plus or minus a year, continues to provide revenue for some time.

When the US economy cycles up, the construction market continues to decline for a minimum of one year. Economic recovery begins to stimulate new construction, but it takes time to decide which new projects will move forward and additional time to design the projects. It also takes time to fund them, to seek approvals and proposals, and to contract for the projects to be constructed before the projects generate construction revenue. As the construction market begins to grow again, it takes a minimum of one year for it to rebound to its pre-downturn size.

Both the lag at market decline and the lag at market recovery vary depending on the length of the cycle and the amount of the market decline (depth). The "lag times" I use are the averages of the major downturns since WWII converted to a median range. I leave out the shortest and longest lengths because they are extreme and would distort the results rendering them of limited use. The current range I am using (which may change after the downturn we are in) is 12 to 18 months at both the decline and recovery. *(In this current ongoing research the calculated range changes almost monthly as new information is applied, but I do not publish it because I believe an ever-changing range will add confusion, which seems to exist.)*

In this crisis the construction market, which usually prospers for some time after an economic downturn, declined rapidly because of delayed and canceled projects. This lag, which is favorable to the construction industry, was the shortest on record. You might call it the "good lag". *(The recent short lag is an "outlier" which will dramatically change the average if it were applied.)*

Response to First Question: *...does that mean it's two and a half years before we even start to recover?* No if you mean US economic recovery. Unknown if you mean construction market recovery. Technically the US economic recovery may have started, but each time it reverses, as it has been, it is a new start date for these projections. Further detail below.

Response to Second Question: *...how long will it take to return to 2019 levels?* As the economic recovery progresses and becomes a certainty, canceled projects will begin to be reconsidered and ideas for new projects germinate, but nowhere near what it takes for the construction market to rebound. The US

economy is “recovered” when the Gross Domestic Product rebounds to the pre-pandemic amount at which time the limited pace of the construction market recovery will strengthen and with pent-up demand progress to full recovery at 2019 levels.

These two 12 to 18 month average lags may appear to mean 24 to 36 months, however, the construction market recovery initiates during the US economic recovery and the two overlap to a varying extent. There are too many variables to get into here but the adjusted average time between the start of a major US economic downturn and the recovery of the construction market is 18 to 36 months. Until some of the variables unfold there is not enough data to forecast the length of the two cycles in the current circumstances. Additional stimulus funding could shorten the time but, at this point, probably not very much.

These are averages only and are not projections of the current downturn. However, as I have been saying for months, the minimum projection is long enough to plan for:

- the amount of available work to diminish
- aggressive competition to drive prices down
- industry-wide profits to shrink.

These conditions demand defensive action.

The questions allow readers to steer the conversation and because there is not enough space to get to all of them we will continue next week.

Next week: **Continued response to questions and comments from readers. Send questions/comments to tom@schleifer.com.**

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Note: Information on overhead management can be found on letstalkbusiness.net click on “Manual”, then Managing Overhead in the table of contents.