32nd Crisis-era Message to Contractors from: Dr Tom Schleifer

Election Aftermath

The election tells us very little about the near future construction market. We are no closer to knowing when the construction market will rebound now that the election is over than we were before the election. There were three things affecting the timing of the construction market rebound before the election: A COVID-19 vaccine, the amount of federal construction spending, and stimulus funding. It is hard to see how the outcome of the election will affect the timing of the development and eventual distribution of a vaccine so it remains a race that is critical to the US and world economies, and subsequently, to the rebound and normalization of the construction market. There were some ambitious projections before the election that federal construction spending would be increased and current commentary suggests that may still happen during the lame duck session, however, those are just speculations. Additional stimulus funding seemed likely before the election but the big question was when? Now that the election is over the uncertainty about the timing has, if anything, increased and it remains anyone's guess.

The timing of additional stimulus is important because the construction market follows the US economy. There is consensus among economists about the need for another round of funding to prevent further economic decline but the stimulus may be DOA. The funding seems to have become a political football. The dispute over how much to fund does not seem to have been settled by the election, at least until inauguration day, and delaying stimulus funding risks recessionary pressure. There are some economists that feel the US economy will do all right without additional stimulus but a large majority are saying it is critical to continued recovery. The unknown is whether the opposing sides will agree on an amount of stimulus spending before January 20 or if we will have to wait until the new administration is in place. Either way the question remains, when will stimulus money gets into the hands that will spend it into the economy?

Economists are saying that the improvement in household spending over the last few months has been, in part, supported by the first round of stimulus funding. However, they warn that is running out and economic recovery will level off or decline without additional funding. If the economic recovery stalls, the construction market will be negatively impacted. The need for increased federal construction spending is important to help offset the drastic reduction in state and municipal construction spending resulting from their reductions in tax revenue. If we are able to get both additional stimulus funding and increased federal construction spending it still will not bring the construction market anywhere near its 2019 high. For that to happen municipal, state, and private construction spending would have to stop shrinking.

Other industry news is not encouraging. AGC reports that at least 75% of their contractors have experienced project cancelations or postponements. Also affecting our market is the fact that a considerable number of multibillion-dollar projects across the country have been canceled or postponed for lack of funding. Just a sampling includes: $8 billion highspeed train LA to Las Vegas; $10 billion Foxconn LCD panel factory in WI; $9 Billion Honolulu Rail Project just to name a few.

What I see is with a number of jumbo projects canceling or being postponed, the big contractors will trade down and the downward domino effect will take place. When I mention billion-dollar projects I get email from contractors saying they have no interest because they are not involved in that size work. They problem is when jumbo projects are taken out of the market, those very large contractors need to find something else to keep busy. They take other size projects and the domino effect of a declining market begins. When the very large firms take smaller projects, other contractors need to take smaller projects and so on down the line. When the billions mentioned above are taken out of the market there is simply less to go around and these three delayed or cancelled projects addressed earlier are just a drop in the bucket. The market will be down this year several hundred billion dollars which makes the critical question, what can we expect next year? Guessing doesn't help, but science, measurements, and calculations do. The current problem is lack of accurate information and the information we do have keeps changing, However, we can still learn from what we have. Unfortunately, all the current changes are for the worse which verifies beyond doubt that the start of the construction market rebound we need is not in sight. That will not happen until the it stops declining.

Some of you think I'm too negative and that things are looking up in construction. I get emails asking, "Why don't you look at the bright side?" I do and I will report it when it happens. I received a note the other day saying, "OK, you have been right so far, but the construction market's getting better." I wish that the communication had included some the data that indicates it is getting better. I saw a survey recently that reported that 90% of architecture, engineering and construction firms say they have experienced project delays or cancellations. If architects and engineers slow down, construction can't be far behind.

Risk management in the construction industry includes cooperating with the market. Obviously, that means planning for the anticipated market, which means "sizing" to the market. Unfortunately, sizing involves overhead expenses which are made up of plus or minus 90% personnel costs. The opposite of risk management is to attempt to maintain sales and size in a declining market by trying to capture work of a different type, size, or in an unfamiliar location at any price. The selling price of construction goes down in a declining market, so it is hard enough to profit from the cheap work available. Under these circumstances, performing less cheap work well and at a modest profit has less inherent risk than capturing and performing a greater amount of cheap work. It is a matter of measuring and calculating risk. A declining market has built-in, unavoidable risk. It is advisable to avoid magnifying the unavoidable risk by adding avoidable risk to it.

Send questions/comments to tom@schleifer.com. *To receive the free weekly Crisis Message send your email address to* tom@schleifer.com.

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