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Ninth Weekly Crisis-era Message to Contractors from: Dr Tom Schleifer

The Construction Market **Bracing for Long-Term Disruption**

Two things are required to support the construction market: The need for something to be built and the ability and willingness to pay for it. A decline in the US economy slows expansion in the private sector which reduces the “need” for new construction. In the public sector the “need” for construction such as infrastructure continues through an economic decline, but reductions in taxes and fees stall the funding of public construction.

When the economy slows, funding and borrowing capacity in the private sector suffer from reduced sales and profits. Funding sources that remain available go unused by a reluctance to spend and caution to conserve cash. One of the first things to be cut is capital spending, which results in the loss of construction funding.

The construction market lags the US economy. The “lag” occurs because of the 12 to 18-months it takes to design, fund and build a project. When the US economy slows down, the projects that are under construction usually get completed, (not all in this crisis) but the design and funding of future projects are interrupted. This means that as the current work in progress is completed over 12 to 18 months, it is not being replaced in the same proportion creating a “lag” as construction put in place declines. When the US economy recovers, the design phase is stimulated again as are the funding sources, but it takes 12 to 18 months (lag) for these projects to be designed and funded before they progress into the construction phase.

This brief description of the dynamics of the construction market confirms that construction will not rebound before the US economy, which is a condition precedent for construction to even “begin” to recover. It will then take time for the construction market to fully recover, which will be when it returns to its prior size and prior profitability. History tells us that until that happens aggressive competition will suppress profits so we can anticipate slim margins during both decline and recovery. Margins return when each enterprise’s appetite to regain their pre-crisis size is satisfied so competition can lighten up.

Construction Professionals need to approximate how long it will take for the US economy to rebound and how long after that for the construction market to recover. A logical first step in that process would be to evaluate where we stand today. I suggest we list what we know about the factors impacting the US economy so that you can assess for yourself what the timing might be and how that might affect your business:

US Economy Related Information:

- 33 million people on unemployment
- Unknown how many furloughed or on leave
- Weakness in GDP projected to be worst since 1930s
- Lifting of social restrictions in stages
- Some states extended restriction through May
- Vaccine in unknown future date
- States and municipalities suffering lost taxes and fees
- Private industry suffering lost sales and profits
- Capital spending will be affected for some time—conserving cash
- Uncertainty about return of consumer spending—When? How strong?
- Energy industry operating at half capacity
- Impact of stimulus funding unknown

Construction Industry Related Information:

- Construction workforce down 975,000 in a month, steepest drop since 1930s
- Industry jobless rate 16.6%
- Reductions in construction employment expected through May
- ENR reports a survey: 35% projects delayed, 14% canceled
- Same report--projects in design 41% delayed, 15% canceled
- New job site protocols will cost and will impact productivity
- Financing for some projects delayed with uncertainty in bond market
- Energy industry has cut spending 30%
- Some states already canceled 2020 transportation budgets
- Serious concerns over potential material shortages

I have been asked if there is any good economic news out there. Yes, but not nearly enough to sway the overwhelming national trends. Readers can add their information to these lists, and we will continue the discussion next week. To evaluate this information, you might want to place next to each item on the first list above the shortest time you think that issue might correct itself or be corrected. Then worst-case scenario, the longest it might take. I usually use the average of the two as the “likely” timing for discussion or decision-making purposes. As each item will have an independent score, you can use them separately or calculate another average to decide for yourself approximately when you think the US economy might recover. Using the same process, consider when and what the impact of each of the items on the second list might have on your business. If this seems like too much work, I will offer some projections next week.

Next week: When and where the construction market is heading.

To assure you will continue to receive the free weekly Crisis Message to Contractors, you will need to send your email address to tom@schleifer.com.

Note: Information on overhead management can be found on letstalkbusiness.net. Click on “Manual” and go to Managing Overhead in the table of contents