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BY JOSEPH NATARELLI & ROGER GINGERICH

INDUSTRY OUTLOOK: *Attitudes & Expectations*

While some contractors were taking recession-proof measures such as containing expenditures and keeping a watchful eye on tariffs prior to COVID-19, the overall economy was optimistic. In addition to strong job growth, consumer confidence, low inflation, and low interest rates, state and local governments were finally climbing out of deficits stemming from the Great Recession, and construction spending continued to increase.

This article takes a look at attitudes and expectations throughout the U.S. construction industry just prior to and immediately following the onset of the COVID-19 pandemic using data from the "2020 Marcum National Construction Survey"[1] launched in the first quarter of the year.

The Survey

GCs, subcontractors, construction management, and other industry partners were asked to weigh in on a range of topics, including access to credit, bonding, overhead expenditures, growth opportunities, top priorities, political issues, competition, and challenges. Survey respondents represented companies ranging in size from fewer than 10 to hundreds of employees. Questions were intended to gauge respondents' views of their businesses over the past 12 months as well as for the year ahead.

With the spread of COVID-19, construction companies had to make sudden adjustments to address workplace safety issues and reexamine growth strategies, which are reflected in respondents' answers. This survey report, released in the second half of 2020, conveys respondents' views before and after COVID-19 had fully impacted the U.S.

As a result, aggregate responses reflected an increasing caution about long-term growth, competition, and replenishing healthy project backlogs. Even so, survey respondents remain generally optimistic about the future of the construction industry.

The Black Swan Event

While most U.S. construction workers were deemed essential and have continued to work throughout the pandemic, survey responses reflected a shift in top priorities and concerns. For example, among early respondents, the availability of credit barely registered as an industry threat for the forthcoming 12 months; however, this issue was identified as a challenge by more than twice as many respondents during the pandemic.

Locating new sources for building materials was identified as another growing concern. When the epicenter of the coronavirus was in China, that country's economic shutdown had an immediate ripple effect on the construction materials pipeline, an issue that has caused many contractors to look for alternate sources and has impacted job costs and bid pricing.

Credit Availability

While optimism about lending dipped slightly as the pandemic gained steam, the respondents remained positive – so long as project owners could obtain financing or funding for new projects. Ninety percent of construction respondents reported that their access to financing has stayed the same or increased.

Going forward, contractors will need to prove to lenders that they have plans in place to diversify suppliers, deliver on contracts, and manage their labor issues. With so much uncertainty about the future, contractors should demonstrate the ability to quickly adjust as necessary to complete projects. If there is federal and state infrastructure legislation released soon, contractors will stand a far greater chance of obtaining the financing they need to begin these projects.

Bonding

When asked about the percentage of their work that requires bonding, almost half (47%) reported bonding requirements on less than 20% of their jobs and 15% reported requirements on 21-40% of their jobs. Before COVID-19, only 16% of respondents expected their ability to obtain bonding to become more difficult. This percentage increased modestly to 21% among late respondents.

Bonding requirements for new contracts will likely be affected by the COVID-19 economy. It is possible that sureties will make underwriting and the ability to obtain additional bonding more difficult in the months ahead.

Backlog

Construction companies typically experience a delayed effect in an economic downturn due to current work and existing backlog. While most construction work continued during the shutdown, there were some exceptions, notably in California, Massachusetts, New Jersey, New York, and Pennsylvania. Still, a healthy backlog can carry contractors forward even in the worst of times. Almost 50% of survey respondents project their 2020 backlog to increase over one year, and another 29% predict it will remain unchanged.

"While many contractors will continue to work through backlog for the balance of 2020, it may be difficult to secure work for 2021, as fewer projects are bid out and project starts become increasingly rare," said economist Anirban Basu.[2] "There are exceptions…Backlog in the heavy industrial category has increased and many contractors are reporting more activity in fulfillment and data center construction as the e-commerce boom persists."[3]

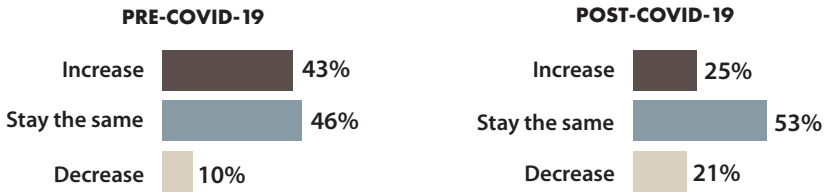
Competition

Average job size and the number of bidders on a job are significant indicators about the health of the U.S. construction industry. A low number of bidders is indicative of a healthy market and better margins, and 56% of survey respondents report bidding against 1-4 bidders. More than one-third of respondents report bidding against 5-9 bidders.

When asked about average job size for the previous 12 months, 48% of respondents report that their average job size grew and 46% report it remained stable.

Subsequent to the Marcum survey, anecdotal information suggests that competitive bidding pressures have increased significantly in recent months as a result of the pandemic, which has the effect of diminishing profit margins.[4]

Exhibit 1: **In the future (next 12 months), your company's budget for overhead expenditures will:**



Overhead Expenditures

When contractors hold the line on general and overhead expenditures, it is often a signal of market uncertainty. Respondents were asked about the current state of their expenditures, and only 11% reported that they decreased costs over the prior year, while 48% of respondents increased expenditures. The rest reported that their overhead was unchanged.

Looking ahead, only 36% of total respondents plan to increase expenditures in the next 12 months. The 12% drop year-over-year likely takes into account two factors: the expectation of a recession (which ultimately came to pass in February 2020) and the COVID-19 pandemic.

As one respondent stated, "There is potential for lack of work due to projects being postponed or terminated due to COVID-19...[That will] create overhead issues regarding personnel after the SBA loan dollars run out."

Exhibit 1 at left further emphasizes how the pandemic has impacted expenditures. Only 25% of later survey respondents plan to increase expenditures, and it is believed that a contractor's ability to manage its overhead during this pandemic will be key to its success when the economy returns to normal.

Top Political Issues

There is no better time than a general election year to ask contractors about the political issues that will most impact their work. Health care reform/insurance rates and material price volatility have been chief concerns among contractors for the past 10 years, and were ranked as the top two most important political issues for their businesses by survey respondents. The percentage of respondents who chose price volatility increased as the pandemic worsened, which indicates heightened concern about the availability of materials and higher prices.

Contractors will be carefully watching material price volatility as they consider additional sources. Some may be willing to pay more in order to ensure materials are accessible for timely project completions.

Top Priorities & Threats

When asked to rank their top priorities, strategic planning was most important for 56% of respondents (Exhibit 2). This issue was followed by organizational planning and finding solutions to skilled labor shortages, which tied as the second-most important priorities, according to 45% of survey respondents. Managing material vendors increased by 8% as a top priority by those respondents answering later in the survey period.

As contractors swiftly implement COVID-19 safety protocols, they will need to continue adhering to safe worksite protocols (i.e., staggered workforces, sanitization, and employee protection and support) to ensure uninterrupted work in the future, avoid being short of workers, and prevent a shut down. They must also focus on new strategies to diversify their supply chains and reexamine business interruption insurance and force majeure provisions in their contracts.

The ongoing skilled worker shortage adds complexity to these issues. When asked what they see as the biggest threat to their businesses over the next year, 34% of respondents said securing skilled labor was the top threat. As one respondent stated, "The lack of skilled labor is keeping us from growing and pursing new markets."

As shown in Exhibit 3, 51% of respondents are increasing compensation to address the skilled labor challenge, followed by employee recognition and appreciation programs.

It is interesting to note how respondents answered this question both before and after the coronavirus-induced government shutdowns. Prior to the pandemic, skilled labor shortage was the top threat; however, after the pandemic hit, the availability of work became the top threat for respondents.

For most of the past decade, contractors have wrestled with this issue, and the economic downturn doesn't necessarily ease this threat. The construction industry lags the overall economy when it comes to downturns. In a study conducted during the economic expansion following the Great Recession, the U.S. Census Bureau determined that 59% of construction workers who lost their jobs found employment in other industries.[5] Clearly, construction companies will need to remain focused on attracting, developing, and retaining workers as part of their ongoing strategic and organizational planning.

Growth Opportunities

Despite the pandemic and other industry challenges, respondents remained confident about growth opportunities both within and outside their regions – with certain concerns expressed toward the end of the survey period.

Within their regions, 25% of respondents are seeing the same opportunities, while 60% are seeing more. Only 15% of respondents predict a decrease in opportunities over the next three years.

When looking outside their region, 46% of respondents predict growth over the next three years, and 40% of respondents predict the same amount of opportunities. According to one respondent, "We need to continue to expand our business development efforts outside of our home market area."

In the nearly 200 open-ended comments from respondents, many are looking forward to infrastructure projects once funding becomes available to back the projects. As one respondent noted, "Growth opportunities are enhanced by deteriorating infrastructure and increasing tax receipts by municipalities."

Looking Ahead

In looking toward 2021, industry confidence will largely depend on the ability of project owners to secure the financing and funding for their projects, as well as contractors' ability to find new sources for building materials and to work safely and efficiently on jobsites. Securing new contracts will also depend on strict safety protocols and strategic long-term planning.

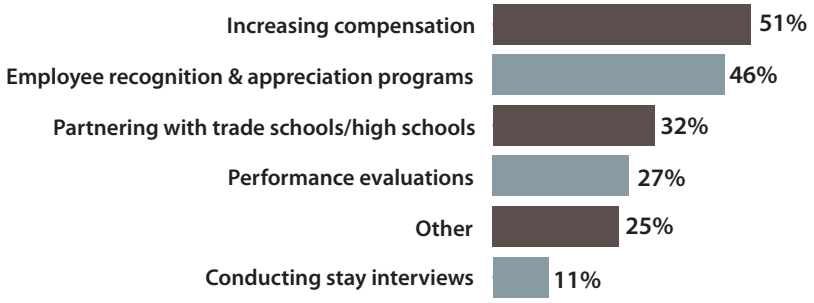
If construction company leaders work with their internal teams and professional advisors, examine their contracts and business insurance, and have plans in place to address material sourcing and new labor safety protocols, they will have a better chance of emerging from this pandemic on solid ground. ■

Endnotes

1. "2020 Marcum National Construction Survey." Marcum. 2020. *online. flippingbook.com/view/658351/2.*

Exhibit 2: **Which of the following actions are among your company's top priorities?**

Exhibit 3: **What are you doing to address the lack of skilled labor?**



2. "ABC's Construction Backlog Indicator Down in July; Contractor Optimism Falls." Associated Builders and Contractors' Central Ohio Chapter. August 24, 2020. *www.centralohioabc.org/abcs-construction-backlog-indicator-down-in-july-contractor-optimism-falls.*

3. Ibid.

4. "Monthly Construction Input Prices Rise Again in July, Says ABC." Design Cost Data. August 14, 2020. *www.dcd.com/articles/monthly-construction-input-prices-rise-again-in-july-says-abc.*

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