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Economy, Inflation Join Construction Headwinds: Marcum

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Dr. Anirban Basu, chief construction economist, Marcum LLP

A deteriorating economic outlook and higher borrowing costs have added to the list of headwinds faced by the construction market, according to The Marcum Commercial Construction Index for the third quarter of 2022.

Although some construction segments retain momentum, there are signs that broader economic weakness have begun to drag on the industry.

Inflation hammers housing

The rapid increases in interest rates have caused a precipitous increase in borrowing costs, and that's wreaked havoc on the residential sector, with applications for new mortgages down to the lowest level since 1997, according to the report.

“The monthly payment on a $300,000 home at current rates is the same as the monthly payment on a $475,000 mortgage obtained at the start of the year,” said Dr. Anirban Basu, chief construction economist, Marcum LLP, in a statement. Basu wrote the report.

Even so, there are currently more new homes under construction than at any point since the Census Bureau began tracking it in 1970, although Basu suggests it may have more to do with longer lead time and market conditions as compared to a year ago.

“This is partially a reflection of how supply chain issues are prolonging construction from start to finish, and many of the homes currently under construction were authorized in 2021, when demand for homes was soaring and borrowing costs were historically low,” he said.

Labor shortage hampers construction

Labor shortages remain the most pressing issue for the construction industry, according to the report.

“The number of unfilled construction jobs increased to 422,000 in September, the most in any month since at least 2000 when the Bureau of Labor Statistics began tracking it,” said Basu. “Contractors have a level of work under contract that necessitates more hiring, but there simply aren’t enough willing and able workers to fill those positions.”

Material price increases have slowed dramatically in recent months, but elevated input costs remain a major issue for contractors, according to the report.

“Construction input prices have fallen ever-so-slightly back to Earth in recent months but, as of September 2022, remain 40.5 percent above pre-pandemic levels,” said Basu. “To put that meteoric increase into context, construction input prices increased just 12.2 percent over the decade immediately preceding the pandemic.”

‘Reshoring’ helps manufacturing construction

Although nonresidential construction spending remains below pre-pandemic levels in nominal terms, manufacturing-related construction spending continues to surge, according to the report.

“Supply chain issues related to the pandemic, tariffs implemented over the past half-decade, geopolitical unrest, and the resulting increase in energy prices, among other factors, have induced many producers to reshore manufacturing capacity,” Basu said. “This has led to a massive 46.3 percent increase in manufacturing-related construction spending since the start of the pandemic.”

Recession looms in 2023

Basu expects recession in 2023 as elevated inflation, worker shortages, and a weakening global economy drag domestic GDP growth into contraction.

“The economy appears headed off a cliff, but it is not clear how far it will fall,” he said. “Regardless of the breadth and depth of recession, an economic downturn would lead to a decline in construction volume.”