

MARCUM

Commercial Construction ▶

Index

Issue 19
FIRST QUARTER 2017

IN THIS ISSUE

Private Nonresidential Construction Spending Outlook Remains Upbeat

Exhibit 1. Nonresidential Spending, March 2017 - CHART

Joe's View

Exhibit 2. Construction Employment Growth in 20 Largest U.S. Metropolitan Areas, March 2016 v. March 2017 - CHART

Exhibit 3. Nonresidential Construction Spending, March 2015 through March 2017 - GRAPH

First Quarter 2017 Performance - CHART

MARCUM
ACCOUNTANTS ▲ ADVISORS

Private Nonresidential Construction Spending Outlook Remains Upbeat

By Anirban Basu, *Chief Construction Economist, Marcum LLP*

Private Sector Construction Spending Easily Outpaces Public Spending

If economic performance reflected ebullient consumer and business sentiment, the U.S. economy would be in the midst of a historic boom. As an example, a recent issue of the National Federation of Independent Business' (NFIB) Small Business Economic Trends indicates that business confidence is at the 97th percentile of its series. In other words, business confidence is only as high as it is presently 3 percent of the time. According to the NFIB, the "remarkable surge in small business optimism that began in November of last year was sustained in March . . . Small business owners remain optimistic about the future of the economy and the direction of consumer confidence. We are encouraged by signs that optimism is translated into economic activity, such as capital investment and job creation."

Without question, the job market remains strong for those Americans in the labor force. In April, the nation added another 211,000 net new jobs, conclusively indicating that March's much weaker performance was a weather-induced fluke. Unemployment is down to 4.4 percent, near a 10-year low. Despite a divided American electorate, the Consumer Confidence Index has recently been at levels last observed in December

2000 (which represented the tail end of the tech boom-led recovery that began in 1991). All of this bodes well for the U.S. construction sector, which stands to benefit from a combination of consumer and business spending growth.

Many observers might be confused by the ebullience expressed by corporate America, consumers, and equity market investors. After all, during the year's first quarter, the U.S. economy expanded just 0.7 percent on an annualized basis, according to Bureau of Economic Analysis data. Consumer spending was weak, with personal consumption's contribution to GDP growth smaller than it had been for many quarters. Export growth remains challenging in the context of modest global economic expansion and a strong dollar. There are also indications of growing difficulties in the U.S. auto sector, with many households already having purchased a vehicle this cycle and a large number of automobiles in decent shape coming off of leases.

On top of that, the Administration's initial attempt at healthcare reform was aborted. The second attempt was more successful, but needs to pass through the grinder known as the U.S. Senate. Implementation of major portions of the President's pro-growth agenda remains elusive, including promised

corporate tax cuts, personal income tax simplification, and an infrastructure-led stimulus package. Geopolitical events ranging from missile testing in North Korea to the WannaCry cyber attack continue to dominate headlines.

Despite it all, asset prices are on the rise, employment continues to expand, and there are indications of expanding business investment. The only conclusion one can reach is that those who control large sums of capital, including large company CEOs, remain confident that President Trump's pro-business agenda will be implemented to a sufficient degree to allow for faster economic growth going forward.

Remarkably, despite the anticipation among many that faster growth is on its way and that the Federal Reserve will tighten monetary policy again in June in response to ongoing growth, long-term interest rates such as the 15- and 30-year fixed mortgage rates have hardly budged recently. The result is a perfect recipe for home price appreciation, with dwindling inventory meeting a growing number of workers able to leverage low rates. It is often said that commercial construction follows residential construction. If that is true, then the commercial construction cycle may have a few more birthdays in front of it.

Spring is in the air, and the construction industry is back, hard at work! It seems that we have overcome what we had speculated (hoped) was a weather-related slow start to the year and have some great numbers to show for it. Q1 of 2017 has already demonstrated nonresidential spending levels at their highest in the history of that metric. In other good news, national unemployment is as low as it has been in the past decade, with 5,000 new construction jobs just in April. As always, I'll balance my excitement by saying that low unemployment can mean tough hiring for contractors looking to grow, so start early and be prepared for increased wage pressure and scarcity of talent.

At Marcum, we always say that our greatest asset goes home every night. People, good people, can make a company great. I hope you agree and bear it in mind as you staff up.

Wishing you a healthy, safe, productive, and prosperous Spring,

Joseph Natarelli, CPA
*National Construction Industry Group
 Leader, Marcum LLP*

▼ **Exhibit 1.** *Nonresidential Spending, March 2017, Millions of Dollars, Seasonally Adjusted Annual Rate*

Subsector	March 2017	1-month % Change	12-month % Change
Nonresidential	\$708,642	-1.20%	1.00%
Communication	\$21,820	0.00%	18.50%
Office	\$73,342	-2.50%	15.70%
Commercial	\$80,511	-3.40%	10.90%
Amusement and recreation	\$23,178	-0.20%	9.20%
Lodging	\$28,384	0.70%	8.30%
Power	\$99,290	-0.60%	4.90%
Public safety	\$8,056	-1.10%	2.50%
Educational	\$90,801	-3.40%	1.00%
Health care	\$41,413	1.70%	-1.40%
Highway and street	\$91,821	0.40%	-2.40%
Conservation and development	\$7,507	5.40%	-4.20%
Religious	\$3,453	-1.30%	-7.30%
Manufacturing	\$69,587	0.60%	-9.70%
Transportation	\$39,695	-3.20%	-12.30%
Water supply	\$10,591	0.20%	-13.90%
Sewage and waste disposal	\$19,195	-2.60%	-22.30%

Source: United States Census Bureau

Although nonresidential construction spending fell on a monthly basis in March, it remains a largely positive indicator. February's nonresidential construction spending value of \$717 billion (seasonally adjusted annual rate) is the highest total since the Census Bureau began tracking the indicator. One major concern is public sector construction spending, which remains soft. The public segment contracted by 0.9 percent on a monthly basis and 6.5 percent on a yearly basis during the most recent construction spending release. Though the private sector experienced a more precipitous monthly decline (-1.3 percent), it has expanded 6.4 percent on a yearly basis.

Construction employment expanded by 5,000 net new jobs in April, the most recent month for which data are available from the Bureau of Labor Statistics. The nonresidential sector added 3,200 net new jobs in April after adding 8,500 in March. The industry's unemployment rate, which is only available on a nonseasonally adjusted basis, fell by 2.1 percentage points in April and stands at 6.3 percent. Due to seasonal factors, industry unemployment almost always plummets from March to April. Since 2009, that decline has averaged 2.3 percentage points.

The national unemployment rate inched down from 4.5 percent in March to 4.4 percent in April. This represents the lowest national rate since May 2007. As with virtually all things economic, this represents a combination of good and bad news. The good news is that lower unemployment implies a tighter labor market, which in turn translates into faster wage growth. That represents a foundation for faster household spending growth beginning with the second quarter of 2017.

However, the lower unemployment rate, including in construction, also means that firms will have to work harder to fill available job openings and likely pay more for the workers they hire. This in turn implies higher inflation and interest rates, neither of which is likely to be positive for construction, all things being equal. Arguably, construction is among the industries most beset by skills shortages due to a lack of market entry by younger workers. Many of these workers have been encouraged to enter professional fields, including computing, even though their inherent skills and interests fit more neatly with skilled trades.

Looking Ahead

The U.S. economy should generate decent economic growth in 2017. Tax cuts or the belief that they are on the way has stimulated confidence among many households and businesses. Consumer spending will likely pick up during the second quarter, and business spending is also likely to improve. Data regarding the number of job openings in the U.S. suggest that job growth will continue to be sufficient to move the nation towards full employment.

▼ **Exhibit 2.** Construction Employment Growth, 20 Largest U.S. Metropolitan Areas, March 2016 v. March 2017, Not Seasonally Adjusted

Rank	MSA	Percent Change	Rank	MSA	Percent Change
1	Detroit-Warren-Livonia, MI*	15.4%	11	Dallas-Fort Worth-Arlington, TX*	4.0%
2	Riverside-San Bernardino-Ontario, CA	13.6%	12	Phoenix-Mesa-Glendale, AZ	3.7%
3	Tampa-St. Petersburg-Clearwater, FL	12.6%	13	Baltimore-Towson, MD*	1.7%
4	San Francisco-Oakland-Fremont, CA	8.4%	13	Philadelphia-Camden-Wilmington, PA-NJ-DE-MD*	1.7%
4	Atlanta-Marietta, GA	8.4%	15	Chicago-Joliet-Naperville, IL-IN-WI	0.4%
6	San Diego-Carlsbad-San Marcos, CA	7.7%	16	New York-Northern New Jersey-L. Island, NY-NJ-PA*	0.4%
7	Seattle-Tacoma-Bellevue, WA	4.8%	17	Houston-Sugar Land, TX	-0.5%
8	Miami-Fort Lauderdale-Pompano Beach, FL	4.5%	18	St. Louis, MO-IL	-0.8%
9	Los Angeles-Long Beach-Santa Ana, CA	4.4%	19	Washington-Arlington-Alexandria, DC-VA-MD-WV*	-1.7%
10	Minneapolis-St. Paul-Bloomington, MN-WI*	4.3%	20	Boston-Cambridge-Quincy, MA-NH	-3.7%

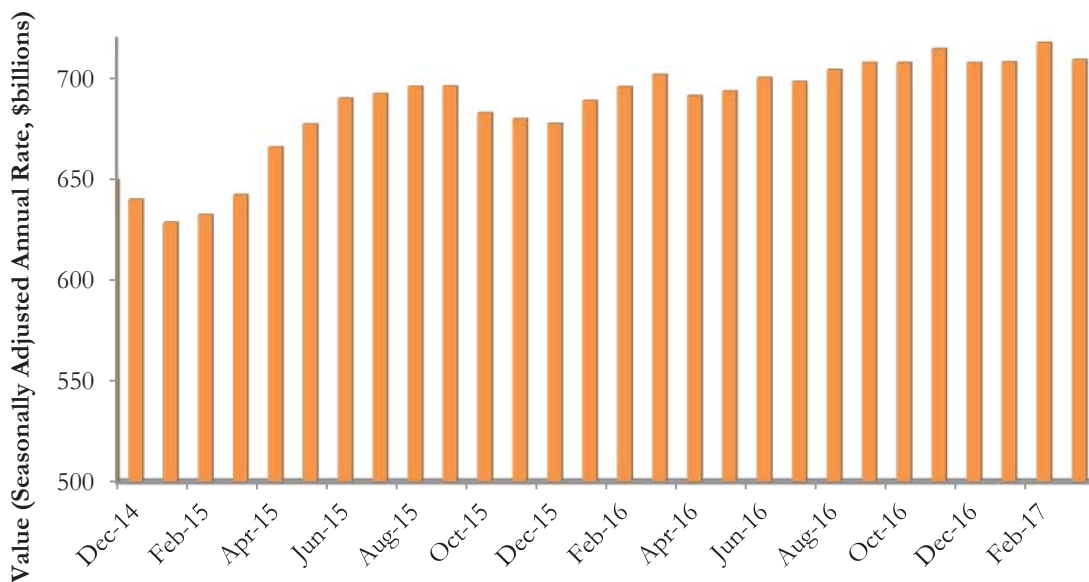
*Construction, Mining, and Logging are included in one industry; Source: Bureau of Labor Statistics

While the creation of jobs and rising wages are generally deemed to be good news, this is both blessing and curse. Wage pressures are building along with other sources of inflation like the cost of housing. One would expect that this will translate into rising interest rates, which could not only interrupt current housing market momentum, but could also negatively impact the values of stocks and bonds in household portfolios. Of course, economists and others have been spelling out this scenario for years, only to express puzzlement at stubbornly low interest rates and the meteoric rise in asset prices.

There are also geopolitical risks to the economic outlook, though financial markets do not appear to be unduly concerned with harshly negative global outcomes presently. The most likely scenario is that the U.S. economy will continue to expand in 2017, that jobs will continue to be created, and that interest rates will rise, but not by enough to completely undermine current housing market or commercial construction momentum or the momentum in the broader economy.

At the heart of the presumption of improving economic performance in 2017 is the notion of confidence, both among households and businesses. Should the new administration in Washington fail to deliver on meaningful elements of its pro-business agenda, confidence could be quickly reversed. Because of this, the economist is put in the uncomfortable position of having to predict political outcomes in order to generate economic forecasts. For now, markets seem fairly confident that something positive will happen, whether in the form of corporate and/or personal income tax reform, removal of unnecessarily burdensome regulation, or an infrastructure-led stimulus package that heavily leverages available private capital.

▼ **Exhibit 3.** Nonresidential Construction Spending, March 2015 through March 2017



Sources: U.S. Census Bureau

First Quarter 2017 Performance	Quarterly Values			% Change from	
Gross Domestic Product	2017Q1	2016Q4	2016Q3		
Overall Real GDP	0.7%	2.1%	3.5%	NA	NA
Nonresidential Fixed Investment in Structures	9.4%	0.9%	1.4%	NA	NA
Construction Spending, Seasonally Adjusted (in \$millions)	Mar-17	Feb-17	Mar-16	Feb-17	Mar-16
Total Construction	\$1,218,285	\$1,220,735	\$1,176,380	-0.2%	3.6%
Residential	\$509,643	\$503,736	\$475,094	1.2%	7.3%
Nonresidential	\$708,642	\$716,999	\$701,287	-1.2%	1.0%
Lodging	\$28,384	\$28,187	\$26,219	0.7%	8.3%
Office	\$73,342	\$75,222	\$63,365	-2.5%	15.7%
Commercial	\$80,511	\$83,332	\$72,606	-3.4%	10.9%
Health care	\$41,413	\$40,720	\$42,016	1.7%	-1.4%
Educational	\$90,801	\$93,960	\$89,910	-3.4%	1.0%
Religious	\$3,453	\$3,498	\$3,725	-1.3%	-7.3%
Public safety	\$8,056	\$8,144	\$7,860	-1.1%	2.5%
Amusement and recreation	\$23,178	\$23,215	\$21,229	-0.2%	9.2%
Transportation	\$39,695	\$40,990	\$45,285	-3.2%	-12.3%
Communication	\$21,820	\$21,818	\$18,421	0.0%	18.5%
Power	\$99,290	\$99,939	\$94,682	-0.6%	4.9%
Highway and street	\$91,821	\$91,419	\$94,054	0.4%	-2.4%
Sewage and waste disposal	\$19,195	\$19,717	\$24,704	-2.6%	-22.3%
Water supply	\$10,591	\$10,567	\$12,304	0.2%	-13.9%
Conservation and development	\$7,507	\$7,122	\$7,839	5.4%	-4.2%
Manufacturing	\$69,587	\$69,151	\$77,066	0.6%	-9.7%
Employment, Seasonally Adjusted (in thousands)	Apr-17	Mar-17	Apr-16	Mar-17	Apr-16
National Total Nonfarm	146,063	145,852	143,826	0.1%	1.6%
Construction	6,877	6,872	6,704	0.1%	2.6%
Residential building	763	766	732	-0.4%	4.2%
Nonresidential building	763	759	761	0.5%	0.2%
Heavy and civil engineering construction	969	965	956	0.4%	1.4%
Residential specialty trade contractors	1,929	1,925	1,850	0.2%	4.2%
Nonresidential specialty trade contractors	2,453	2,458	2,405	-0.2%	2.0%
Producer Price Index ¹	Mar-17	Feb-17	Mar-16	Feb-17	Mar-16
Finished Goods (seasonally adjusted)	110.5	110.6	106.3	-0.1%	4.0%
Inputs to Construction Industries	213.5	212.9	204.5	0.3%	4.4%
Nonresidential general contractors	104.3	104.4	102.5	-0.1%	1.8%
New nonresidential building construction, National	112.5	112.3	110.9	0.2%	1.4%
New nonresidential building construction, Northeast	104.6	104.3	103.5	0.3%	1.1%
New nonresidential building construction, South	105.3	105.1	103.6	0.2%	1.6%
New nonresidential building construction, Midwest	102.9	103.1	101.9	-0.2%	1.0%
New nonresidential building construction, West	105.4	105.1	103.4	0.3%	1.9%

⁽¹⁾ The Producer Price Index (PPI) program measures the average change over time in the selling prices received by domestic producers for their output. The prices included in the PPI are from the first commercial transaction for many products and some services. All figures are indexed from a base year, that base year being different for each individual index.

Services ▼

Marcum LLP is one of the largest independent public accounting and advisory services firms in the nation, with offices in major business markets throughout the U.S., as well as Grand Cayman, China and Ireland. Headquartered in New York City, Marcum provides a full spectrum of traditional tax, accounting and assurance services; advisory, valuation and litigation support; and an extensive range of specialty and niche industry practices. The Firm serves both privately held and publicly traded companies, as well as high net worth individuals, private equity funds and hedge funds, with a focus on middle-market companies and closely held family businesses. Marcum is a member of the Marcum Group, an organization providing a comprehensive array of professional services.

▼ Assurance

Marcum's Assurance Services Division provides independent audit, attestation and transaction advisory services to both publicly traded and privately owned companies in a wide variety of industries. The Firm provides clients with an independent and objective view of their financial condition and results of operations, while maximizing the transparency and reliability of financial information.

- ▶ Attestation Engagements
- ▶ Audits
- ▶ Compilations & Reviews
- ▶ Employee Benefit Plans
- ▶ International Financial Reporting
- ▶ IT Risk & Assurance
- ▶ Mergers & Acquisitions
- ▶ SEC Advisory Services
- ▶ SOC Reports
- ▶ Transaction Services

▼ Tax & Business

Marcum's Tax & Business Services Division offers all forms of accounting and regulatory compliance services. Our tax professionals are deeply experienced in advising large corporations, international businesses, foreign nationals, high-net-worth individuals, family business owners, local business operators and others on complex transactions at the local, national and international levels. Our high degree of specialization ensures that both the advice and services clients receive are specific to their needs.

- ▶ Accounting Services
- ▶ Bankruptcy and Insolvency
- ▶ Business Advisory
- ▶ Cost Segregation
- ▶ EB-5 Investor Services
- ▶ Financial Statements
- ▶ International Taxation
- ▶ Marcum Family Office
- ▶ State & Local Taxation
- ▶ Transaction Advisory
- ▶ Tax Controversy
- ▶ Tax Credits & Incentives
- ▶ Tax-Exempt Business
- ▶ Tax Return Compliance
- ▶ Trusts & Estates

▼ Advisory

Marcum's Advisory Services Division provides regulatory agencies, lawyers, trustees, financial institutions, insurance companies and business owners with answers to business and litigation matters. Our teams of asset managers, operational consultants, forensic experts and accountants have the experience and expertise to accomplish the specific goals of our clients.

- ▶ Anti-Money Laundering
- ▶ Bankruptcy
- ▶ Business Interruption Claims
- ▶ Business Process Outsourcing Solutions
- ▶ Civil & Criminal Fraud
- ▶ Computer Forensics
- ▶ Financial Advisory
- ▶ Forensic Services
- ▶ Insolvency Analysis
- ▶ Performance Improvement
- ▶ Risk Management
- ▶ Workplace Security & Investigations

▼ Valuation & Litigation Support

Marcum LLP is a leading provider of business valuation, litigation support, economic damages, and financial forensic investigations.

We are frequently retained to provide expert witness services relating to the value of a business; loss of a business or segment of a business; determination of reasonable compensation; and other financial matters. Our professionals are often court appointed or jointly retained by the parties involved in a dispute. In addition, our experts are regularly invited to peer and legal conferences to teach, and regularly publish in top industry journals.

- ▶ Business Valuations
- ▶ Litigation Support
- ▶ Financial Forensic Investigations
- ▶ Marital Dissolution



▼ Joseph Natarelli

Joseph Natarelli is the national leader of Marcum's Construction Industry Practice and partner-in-charge of the Firm's New Haven office. For more than a decade, he has served as a technical reviewer for the AICPA's Audit Risk Alert for Construction Contractors and the AICPA Accounting Guide – Construction Contractors. Joe has also chaired the annual AICPA National Construction Industry Conference.



▼ Anirban Basu

Anirban Basu is Marcum's chief construction economist. He is also a member of the Firm's National Construction Practice, as well as chairman & CEO of Sage Policy Group, Inc., an economic and policy consulting firm in Baltimore, Maryland. Anirban leads Marcum's research and analysis of the economic health of the commercial construction industry in America. Additionally, he writes the quarterly Marcum Commercial Construction Index and annual Marcum JOLT Survey analysis.

National Construction Industry Services Leaders

JOSEPH NATARELLI

National Construction Industry Group Leader
joseph.natarelli@marcumllp.com
203.781.9710

NEW ENGLAND:

ROBERT MERCADO

robert.mercado@marcumllp.com
203.781.9730

NEW YORK:

JOSEPH MOLLOY

joseph.molloy@marcumllp.com
631.414.4125

PHILADELPHIA:

EDWARD REITMEYER

edward.reitmeyer@marcumllp.com
484.270.2595

NASHVILLE:

JAMES LUNDY

james.lundy@marcumllp.com
615.245.4050

FLORIDA:

WHIT FOREHAND

whit.forehand@marcumllp.com
407.458.5210

CHICAGO:

TIM CROSBY

tim.crosby@marcumllp.com
847.282.6368

CALIFORNIA:

JAYSON MORGAN

jayson.morgan@marcumllp.com
949.236.5640