THE 2012 CONSTRUCTION HIRING AND BUSINESS OUTLOOK

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The Associated General Contractors of America * 2300 Wilson Blvd., Suite 400, Arlington, VA 22201 * (703) 548-3118

Summary

The outlook for the construction industry is mixed for 2012, as firms must balance growing demand for certain private sector market segments with continued weakness in key sectors, the near end of the stimulus and declining overall demand for public sector construction. Indeed, according to an analysis of survey responses from more than 1,300 construction firms conducted by the Associated General Contractors of America and Computer Guidance, the industry is not likely to experience a recovery until at least 2013 despite some growing positive trends.

Private Sector Market Outlook Improving, Public Sector to Weaken

With the power, hospital and higher education sectors leading the way, demand for construction should continue to stabilize during 2012. Indeed, a clear majority of firms expect the dollar volume of projects they compete for to either grow or remain stable in every market segment identified in the survey. However, the stability masks two divergent trends – growing demand for private sector construction activity offset by declining public sector demand.

As the final impacts of the stimulus wrap up and public budgets continue to shrink, firms are becoming increasingly pessimistic about key publicly funded market segments. For example, 40 percent of firms expect highway funding to decline in 2012 while 44 percent of firms expect the amount invested in public building projects to drop and 38 percent of firms expect funding for other categories of transportation – including airport and transit projects – to decline. In contrast, 34 percent of firms expect demand for hospital and higher education facilities to grow and 31 percent expect demand for power facilities to increase this year.

It is important to note that significant weaknesses remain even within private sector market segments. Thirty-five percent of contractors responding to the survey expect demand for new retail, warehouse and lodging facilities to decline in 2012, while only 22 percent expect demand to grow. The outlook is similar for the private office construction market, where 36 percent of firms expect demand to continue declining while only 21 percent expect demand to increase.

Construction Employment to Improve... Slightly

Significantly more firms (32 percent) plan to add staff this year than plan to lay off staff (9 percent). This is a marked improvement from 2011 when 37 percent of firms reported cutting staff while only 34 percent added employees. Despite the fact more firms plan to hire staff this year, those additions are likely to be modest at best. Seventy-seven percent of firms report they plan to hire 15 or fewer new employees in 2012. For most firms (85 percent) these additions will expand their total workforce by 25 percent or less.

Fortunately, the firms planning to cut staff also expect to make relatively modest changes to the size of their workforce. Ninety-one percent of firms estimate their planned layoffs will amount to 15 or fewer positions being cut. For most firms these layoffs will shrink their total workforce by 25 percent or less.

Regardless of construction market type, contractors' answers were relatively consistent when it came to their staffing plans with firms working in the private sector slightly more likely to hire than firms working on publicly funded projects. Firms working primarily in highway construction reported they were least likely to hire new staff in 2012, with only 27 percent reporting they plan to add staff. Firms working in the manufacturing sector were next, with only 29 percent saying they planned to add staff this year. On the flip side, firms working in hospital and higher education construction are more likely to add employees this year, with 34 percent reporting they plan to hire. They were followed by firms in retail and warehouse construction and working in private office construction, with 33 percent firms doing both types of work reporting they plan to hire new staff.

Conversely, 11 percent of firms working in both highway and water & sewer construction reported they plan to make layoffs this year, the highest percentage for any type of firm. Firms working in private office construction were least likely to lay off staff this year, with only 9 percent reporting plans to downsize in 2012.

Tight Credit is Delaying or Canceling Many Projects

Tight credit conditions do not appear to be affecting most firms' ability to attract new credit. Yet cautious lending practices are having what appears to be a significant impact on the construction market. That is because tight lending conditions are forcing many owners to delay or cancel construction projects, according to the survey results. While only a small number (14 percent) of firms report being directly impacted by tight bank credit conditions, nearly half (49 percent) report that tighter lending conditions have caused their customers to delay or completely cancel construction projects.

Construction firms working in the highway sector were least likely (46) to have projects they were working on canceled or delayed because of a lack of financing. Conversely, firms working in private office development were most likely (54 percent) to have projects delayed because of tight credit. Meanwhile, highway as well as water and sewer contractors were more likely to have had difficulty attracting financing for their firms (16 percent). And interestingly enough, contractors working on private office buildings were least likely (13 percent) to have had difficulty attracting financing for their own firms.

Cautious Firms are Quicker to Lease, Instead of Buy, New Equipment

As the commercial construction industry remains mired in a downturn that began in earnest in 2008, they continue to evolve their equipment strategies. Instead of purchasing new equipment, many firms report leasing. While 49 percent of firms reported purchasing new equipment in 2011, significantly more (69 percent) reported leasing construction equipment. Even when firms added new equipment, however, their investments were relatively modest. For example, 60 percent of firms reported that their equipment purchased totaled $250,000 or less last year while 70 percent leased equipment totaling less than $250,000. Given the fact many new pieces of construction equipment cost well into the six figures, this means appetite for new equipment is tepid.

The trend towards leasing, instead of buying, new equipment is likely to accelerate in 2012. While only 40 percent of firms report they plan to purchase new equipment this year, nearly two-thirds (66 percent) report they plan to lease new equipment. As with 2011, firms' appetite for new equipment is likely to be modest this year. Fifty-seven percent of firms will invest $250,000 or less on new equipment purchases in the new year while 70 percent of firms plan to lease $250,000 or less worth of construction equipment.

Despite the relatively bleak outlook for new highway construction, more firms working in that market segment reported they were likely to purchase new equipment (47 percent) than in any other market segment. More firms working in private office development (62 percent) reported they were not planning on purchasing new construction equipment. Meanwhile, more construction firms working in the retail, warehouse and lodging segment (66 percent) reported plans to lease new construction equipment in 2012 than any other segment. Thirty-eight percent of firms working in manufacturing reported no plans to lease new equipment, more than for any other market segment.

While the Stimulus Helped Most Firms, It is Fading Fast

With nearly two years of stimulus-funded construction activity wrapping up, it is clear the measure's $135 billion for construction had an outsized impact on the $800 billion construction industry. Indeed, most firms (51 percent) report they were awarded at least one stimulus-funded project to date. However, most firms performing stimulus-funded work reported the total amount of stimulus work they provided was modest. Sixty-three percent of firms reported receiving stimulus work totaling $5 million or less.

For most firms, these relatively small stimulus contracts meant most of their employees were not directly engaged in recovery projects. Indeed, 66 percent of firms report than 25 percent or less of their staff was engaged in stimulus activity while another 21 percent said less than half of their staff worked on stimulus activity.

Unfortunately, the benefits of the stimulus are fading fast. Three-quarters of firms reported they do not expect to perform on any stimulus-funded projects in 2012. Even among the firms expecting to perform stimulus work in 2012, 46 percent say they expect that work to total $1 million or less and 83 percent of those firms say stimulus work will total a quarter or less of their total 2012 revenue.

The stimulus had a more profound impact on firms working on publicly funded projects than firms that work on private sector projects. For example, 64 percent of highway contractors reported receiving stimulus-funded projects, while only 47 percent of private office building contractors worked on projects associated with stimulus dollars. Interestingly enough however, a high number of firms working in manufacturing construction reported working on stimulus projects. This could be a combination of the fact the stimulus included funds to boost manufacturing of solar and other renewable energy devices and that firms performing manufacturing work were more willing to chase business outside their core competency in order to stay afloat.

Health Care Costs Keep Rising Despite Health Care Law

Despite the fact the controversial health care law – which AGC opposed in its final form –was enacted in 2009, health care costs continued to accelerate in 2011 for the 96 percent of firms that provided insurance for their workforce. Despite this, and the fact most firms expect health care costs to continue rising in 2012, the same percentage of firms (96 percent) plan to offer health care this year. Indeed, 81 percent of firms responded that the cost of providing health care for their employees went up in 2011, while only 3 percent reported that their costs went down. And 82 percent of firms expect their health care costs will continue rising in 2012 and even fewer (2 percent) expect costs to decline this year. Those results were largely consistent across the various market segments – with the power segment least likely (80 percent) to expect increased health care costs in 2012 and hospital and higher education firms more likely (82 percent) to expect their health care costs to increase.

Firms are Paying More For Materials While Earnings Remain Stagnant

Construction firms continue to be squeezed between rising materials costs and stagnant earnings for work provided in 2011, a trend that is likely to continue this year. Eighty-three percent of firms reported that the price they pay for key construction materials increased in 2011 while only 2 percent reported declining materials prices. The price increases were not overly extreme – 67 percent of firms reported materials price increases of 10 percent or less. However, those increases occurred even as 62 percent of firms reported cutting bid levels (what they charge to perform work) in 2011 and another 2 percent reported setting their bid levels so low they actually took losses on their work.

The materials price squeeze is likely to continue in 2012. Eighty-six percent of firms report they expect materials prices to increase in 2012, even as 80 percent of firms say they expect bid levels to either stagnate or decline this year. While lower bid levels mean construction owners are likely to get a good deal on construction, current economic conditions mean firms are generating less revenue for the work they perform even as they pay more for key materials. Firms of all types were consistent in reporting their expectation that materials prices would increase in 2012.

This cash squeeze is likely one reason why firms continue to remain cautious about making new hires or acquiring new construction equipment. After all, relatively few contracts (12 percent) expect the overall construction market to grow in 2012. Instead, 36 percent expect the market to finally expand in 2013, while 34 percent expect the rebound will not come until 2014. Troublingly, nearly one in five (18 percent) do not expect the overall construction market to recover until 2015.

More firms, 15 percent, working in the “other transportation” segment (typically airport and transit projects) reported they expect demand for construction to increase in 2012. Firms working in K-12 school construction were more likely (38 percent) to report they expect the market to expand in 2013. Thirty-five percent of highway firms expect the market to improve in 2014, more so than for any other segment of the industry. And 21 percent of firms working in power construction say they don’t expect the market to improve until 2015, the highest percentage for any type of firm.

Use of Building Information Modeling is Prevalent and Growing

Firms reported using Building Information Modeling (BIM) technology in 35 percent of their projects in 2011, which is up considerably from the 8 percent of firms that reported using BIM on their projects in 2010. BIM technology typically uses three-dimensional, real-time, dynamic building modeling software to increase productivity in building design and construction. Construction firms clearly expect demand for BIM to continue growing, with 47 percent reporting they expect use of BIM to increase in 2012. Meanwhile, only 1 percent of firms expect the use of BIM to decrease this year. This likely reflects a growing appreciation among construction firms of the cost savings and increased productivity that come with BIM technology, as well as the need to compete with others who already offer BIM.

BIM use definitely varies based on market segment. For instance, relatively few (39 percent) highway contractors expected to work on more BIM projects in 2012, the least amount for any segment. Meanwhile, 53 percent of hospital and higher education contractors expect to work on more BIM projects in 2012, more than for any other market segment. This likely reflects the increasing complexity of hospital and higher education projects – which often include sophisticated designs to handle the many different uses and equipment needed for universities and hospitals.

A Cool Down for Green Construction Projects?

After years of growing demand for "green" construction projects – projects seeking one form of environmental performance certification or another – most firms do not expect demand for these kinds of projects to grow in 2012. Indeed, 60 percent of firms expect demand for green projects to stagnate or even decline in 2012. This could reflect the fact that many firms feel that either market conditions are too weak to warrant new green projects, or that the market is already too saturated with green building projects. Expectations for demand for green construction projects also vary by market segment. As might be expected, firms working on building projects are more likely to expect demand for green projects to increase in 2012 while firms working on horizontal infrastructure projects are less likely to expect an increase in demand. Overall, firms working in hospital and higher education construction are more likely (46 percent) to expect demand for green projects to grow this year while firms working in highway construction are least likely (36 percent) to expect growth in green demand.

Construction Firms Continue to Invest in Software and Technology

Despite difficult market conditions and caution in hiring and equipment plans, the majority (55 percent) of construction firms report they plan to invest in their information technology departments in 2012. However, their investments are likely to be relatively modest, with 64 percent saying they will invest $50,000 or less in new IT investments this year. Meanwhile, only a relatively small percentage of firms (9 percent) report they plan to purchase new financial and job cost software in 2012. Yet those firms report more ambitious budgets, with 51 percent of firms planning to acquire this type of software reporting they plan to invest over $50,000 in those programs in this year. This could explain why one-third of firms (34 percent) reported they would consider investing in new financial and job cost software if they could either lease it or if there were financing options available.

Construction Firms Begin to Embrace the Cloud?

Nearly one out of every four construction firms (24 percent) report they plan to switch their financial, job cost or operational software applications to the Cloud in 2012. This most likely reflects the fact that transitioning to Cloud-based computing is likely to save firms considerable sums of money. Indeed, 76 percent report their Cloud-based investments in 2012 will total $10,000 or less. In other words, transitioning to the Cloud will cost firms significantly less than acquiring new software will.

Regional Market Trends

The employment outlook varies based on geography, with 57 percent of firms in Wisconsin planning to hire, more than in any other state. No contractors in South Carolina reported plans to make layoffs this year. Meanwhile, 18 percent of firms in Missouri plan layoffs for this year, the highest percentage from any state. Only 16 percent of Virginia firms say they expect to hire in 2012, the lowest percentage for any state.

Contractors in Ohio are the most optimistic about growth for the highway market, with 38 percent of firms saying they expect an increase in highway funding for 2012. In contrast, 81 percent of contractors in Pennsylvania expect there to be less highway funding in 2012 than there was in 2011, the most pessimistic result for any state.

Firms that work in the “other transportation” category, which includes transit and airport construction, are most optimistic about 2012 in Tennessee, where 27 percent expect the market to grow. Conversely, more contractors in Iowa (71 percent) expect this market segment to shrink this year than in any other state.

Contractors who report working in the water and sewer market are the most optimistic about this year in Nebraska, where 54 percent expect the market to expand. However, 64 percent of contractors in Colorado, more than from any other state, report they expect the market segment to contract in 2012.

Regional expectations for the power market vary, with more contractors in Indiana (55 percent) expecting the market to expand this year than in any other state. Meanwhile, 43 percent of contractors from Hawaii and Iowa expect this market to contract in 2012, more than in any other state.

Michigan contractors are the most optimistic about the manufacturing segment, with 50 percent saying they expect it to expand this year. Meanwhile, 43 percent of contractors working in the manufacturing sector in Massachusetts expect that market to shrink in 2012, more than in any other state with a large enough sample size.

A higher number of South Carolina-based contractors (61 percent) expect the hospital and higher education market to improve in 2012 than in any other state. In contrast, 56 percent of contractors working in the hospital and higher education market in Hawaii expect the amount of money invested in those projects this year to decline, more than in any other state.

The retail, warehouse and lodging sector outlook for 2012 looks relatively bright in Massachusetts, where 40 percent of contractors working in that market expect activity to increase, more than in any other state. In contrast, 50 percent of contractors from Colorado working in that segment of the market expect construction activity to decline this year.

Massachusetts-based contractors are the most optimistic about the public building sector for 2012, with an industry-leading 58 percent reporting they expect activity to increase this year. Contractors in Florida, however, are the most pessimistic about the public building outlook, with 68 percent reporting they expect that market to decline and none reporting an expected increase in activity.

Likewise, Kansas-based contractors are the most optimistic about private office construction activity in 2012, with 36 percent reporting an expected increase in activity in that market. Contractors in Missouri are expecting the biggest decline in private office construction, with 55 percent reporting an anticipated decline in spending in that market segment this year.

And, South Carolina-based contractors are more optimistic about the chances for growth in the K-12 school construction market than in any other state, with 42 percent expecting the market to improve in 2012. Conversely, more Florida contractors (67 percent) expect a decrease in K-12 school construction spending than in any other state.

Conclusion

While the outlook for the construction industry appears to be improving in 2012, significant challenges remain. On the positive side, construction employment is likely to see modest gains as demand for some private sector construction projects improves. At the same time, most firms remain cautious in the face of continued weakness in retail, office and warehousing construction and declining demand for all manner of publicly funded construction work. In addition, construction firms remain caught between increasing health care and materials costs and stagnant amounts for what they can charge. In other words, while conditions will improve for many firms this year, the industry should not expect a broad-based recovery until 2013 at the earliest.

Public officials and policy makers can accelerate that recovery by enacting measures designed to further stimulate private sector demand and committing to much-needed investments in the nation's aging infrastructure. Acting on long-delayed infrastructure bills to address water, highway, transit and airport infrastructure – including addressing funding challenges with each of those programs – will certainly help employ more construction workers while simultaneously improving the systems that underpin the broader economy.

Washington and state officials should also look at current regulatory and tax policies with an eye towards eliminating measures that needlessly restrain construction demand. Environmental permitting for many types of construction projects is often measured in terms of years, instead of the weeks or months that most market cycles demand. Meanwhile, it is clear that additional steps need to be taken to address the threat of rising health care costs for the vast majority of construction employers.

Even as market conditions remain difficult, many construction firms are taking steps to become more efficient, to embrace new technology and to become more competitive. By leasing new equipment instead of purchasing it, construction firms are better able to adapt to swings in demand. By embracing new finance software and new technology, firms are improving their operational efficiency and reducing back office costs. And by embracing business practices like Building Information Modeling and Cloud-based computing, firms are finding ways to cut costs without losing productivity.

Even as 2012 may not bring about the kind of recovery that many firms have been hoping for, conditions are clearly improving even as the industry continues to adapt and evolve. With a little luck and a lot of work, the construction industry will be well poised to fully recover once demand for new construction from both public and private sources recovers.

About the Survey

AGC and Computer Guidance Corporation conducted the survey that serves as the basis for the 2012 Construction Hiring and Business Forecast during the final three weeks of December 2011. Over 1,300 firms – primarily from among the 20,000 general contractor or specialty subcontractor members of the Associated General Contractors of America – completed the survey. Contractors who completed the survey were entered into a raffle to win a $100 Amazon gift certificate. Other than that, firms and their employees were not compensated or in any other way reimbursed for completing the survey.