



Construction Outlook 2014: Positive Economic Momentum Spurs Steady Growth in Commercial Construction Market



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After a long, uphill battle, the construction industry appears to finally be on the road to a slow, but steady recovery. Since the National Bureau of Economic Research reported that the end of the recession 'officially' took place in June 2009, recovery of the U.S. economy has been slow and

uneven. Bright prospects have been dimmed by caution and uncertainty slowing the normal pace of recovery. Many analysts now believe that growth is much more sustainable in 2014. "There was strength in some important sectors of the economy at the end of last year," Paul Dales, an economist at *Capital Economics*, said. "2014 could be the year where the recovery really starts to gain some ground."

In fact, construction spending rose 1% in November to a seasonally adjusted annual rate of \$934.4 billion, the U.S. Commerce Department reported. That's the highest volume reported in more than four years. Spending on single-family home and multi-family apartment construction rose 1.9% to their highest levels since June 2008 while commercial project spending increased 2.7% led by the office, communication and transportation markets.

A slightly stronger U.S. economy is anticipated for 2014 as indicated in recent reports published by several industry-leading economists and analysts. Representatives from the Association of General Contractors of America (AGC of America), FMI, McGraw Hill Construction and Reed Construction Data mutually agree that even though the economy appears to be settling into a quiet, but steady growth, there are still several potential risks ahead that could impact the future.

One of the economy's inherent risks to confidence and growth in 2014 is the continued uncertainty of the federal budget and debt ceiling. However, the recent budget deal passed in the U.S. Senate in mid-December narrowly avoided another government shutdown with the extension of a temporary funding measure that was set to expire on January 15, 2014. This measure does not yet address the debt limit crisis,

setting up a potentially complicated confrontation in late February or early March.

There is also continued uncertainty as to the impact of expected deep cuts to the federal government's spending in the near term. Energy and oil cost predictions also significantly impact positive momentum in the economy and the unknown implications and costs of the nation's Affordable Care Act have yet to be manifested.

Notwithstanding the above potential constraints to the nation's slowly recovering economy in 2014, there is cautious optimism to this year's construction outlook with predictions of modest increases in overall spending. Several noteworthy economists and industry analysts have projected the following for 2014:

AGC of America's, Chief Economist, Ken Simonson, predicts that total construction spending will rise from 6% to 10% per year from 2014 to 2017.

McGraw Hill Construction's Robert Murray, Vice President of Economic Affairs, suggests that total construction starts could rise by 9% in 2014 reaching \$555 billion.

FMI's prediction of a 7% uptick in growth for construction

Construction Outlook 2014...

continues on page 4



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Construction Outlook 2014...

continued from page 1

put-in-place will total \$977 billion in 2014 as compared to the total of \$909.6 billion in 2013.

The volume of work within the architectural community also denotes upcoming levels of new construction projects that would be realized within the following 9 to 12 months. Kermit Baker, Chief Economist with the American Institute of Architects (AIA), reported a pronounced increase in architectural billings in 2013 providing a solid indicator that construction growth is on the horizon. Currently, architectural and design billings have reached their highest volume since the recession began in late 2008.

Bernard Markstein, the U.S. Chief Economist with Reed Construction Data, also comments on the close connection between residential construction and its impact on the commercial construction market. He notes that there is typically an 18- to 24-month lag between the two markets furthering his prediction of steady and continued commercial construction growth buoyed by the continued expansion of the residential building market. Markstein predicts that this improvement will continue through 2014 and 2015.

Construction growth trends can also be identified within many market segments and geographical regions. Several notable milestones and market changes are propelling the positive outlook for the real estate and construction industries including:

The boom in the exploration and mining of shale oil and gas, currently referred to

as the shale "gale", is generating significant construction activity in the form of new access roads, site preparation, storage ponds and piping requirements. Increased new construction and expansion at petrochemical, power and steel plants is underway to support this increased production of natural gas. In fact, the U.S. is producing more natural gas than ever before and plans to export this commodity as liquefied natural gas or LNG. This rapid increase in U.S. natural gas output can be attributed to the extraction of the commodity from shale formations. Natural gas and crude oil have contributed to the U.S. producing 14% more of its own energy as compared to 2005, according to data from the Energy Information Agency.

The expansion of the Panama Canal is also impacting construction at U.S. port cities, primarily along the East and West Coasts, that extends beyond piers and dredging work to include warehouses and rail facilities to handle the influx of new product at these U.S. entry points.

The residential recovery is expected to continue and to begin to impact single-family construction as well as the multi-family market. Murray refers to the multi-family sector as the "star of the construction industry" showing steady and strong growth that is anticipated to hold through 2014. Increases into 2015 are also expected. Single-family housing starts were estimated to reach one million in 2013; 1.22 million in 2014; and 1.57 million in 2015. Although still shy of typical volume levels (1.6 to 1.8 million per year), the continued positive growth expectation in this market is welcome news to the

commercial markets that enjoy the benefits of consumer and institutional spending supporting the velocity of growth within the residential market.

The manufacturing sector is also predicted to maintain its upward growth pattern due primarily to the resurgence of the auto industry and the energy sector. Expectations of this segment's growth vary since forecasts on the amount of this market segment's actual increase will not materialize until the coming years.

All major sectors of the construction industry are forecasted to improve in 2014. The commercial and industrial markets will accelerate at the fastest pace while the greatest increases will be experienced within the Western and Southern regions of the country. FMI is forecasting a 5% uptick in retail construction in 2014 while the AIA predicts that the institutional construction recovery will slowly begin this year. In addition, the unknown components associated with the Affordable Care Act have slowed new health-care construction significantly – basically 'flat lining' the industry over the past two years. However, it's predicted that in 2014, a slight uptick in new construction within the stand-alone emergency care, outpatient surgery and urgent care centers is likely to occur.

Simonson at the AGC of America predicts that the hospitality sector will continue to enjoy additional growth in construction primarily due to the development of new extended stay properties, particularly within

Construction Outlook 2014...

continues on page 6

Construction Outlook 2014...

continued from page 4

the oil and gas regions, and to the continued remodeling and reconstruction of resort and vacation properties. Public sector work remained flat in 2013 with another 5% decrease

anticipated in 2014. The educational sector recorded its fifth year of declining figures in 2013, but Murray of McGraw Hill Construction predicts recovery in 2014. FMI concurs that within certain regions of the country where new single-family residential construction is occurring with associated increases in tax revenues will propel growth in the educa-

tion sector that may rise over 4% in comparison to 2013's numbers.

Notwithstanding the obstacles that still remain in the nation's economic recovery path, the overall prediction is that a positive momentum in construction growth will take place in 2014 reflecting a modest, but steady, strengthening of the industry.

Jeffrey A. Raday, P.E. serves as President of McShane Construction Company, a national multi-market construction services firm, headquartered in Rosemont, Illinois. He is also Chairman of the Builders Association, the Chicago Chapter of the Associated General Contractors of America (AGC of America).

