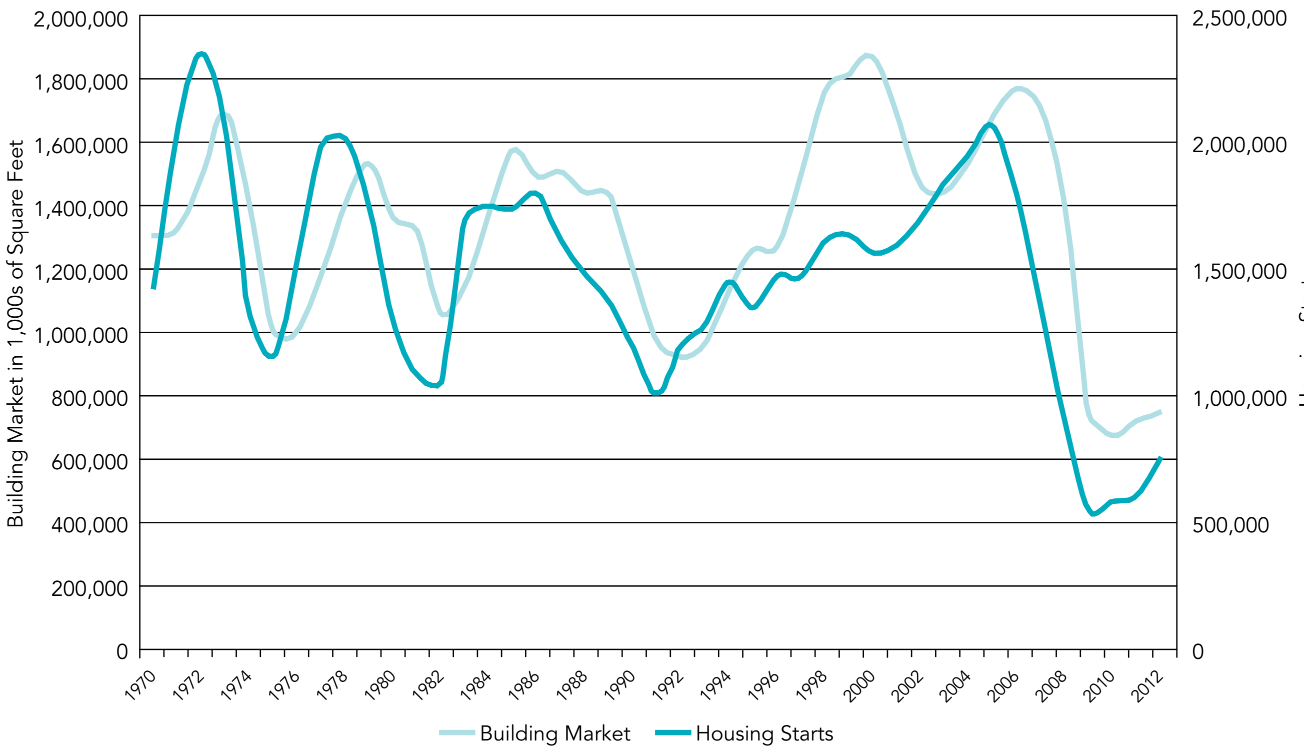
economics

OUT WITH THE OLD, IN WITH MORE OF THE SAME

Next year's construction climate will be very similar to this year's.

BY JOHN CROSS, P.E.



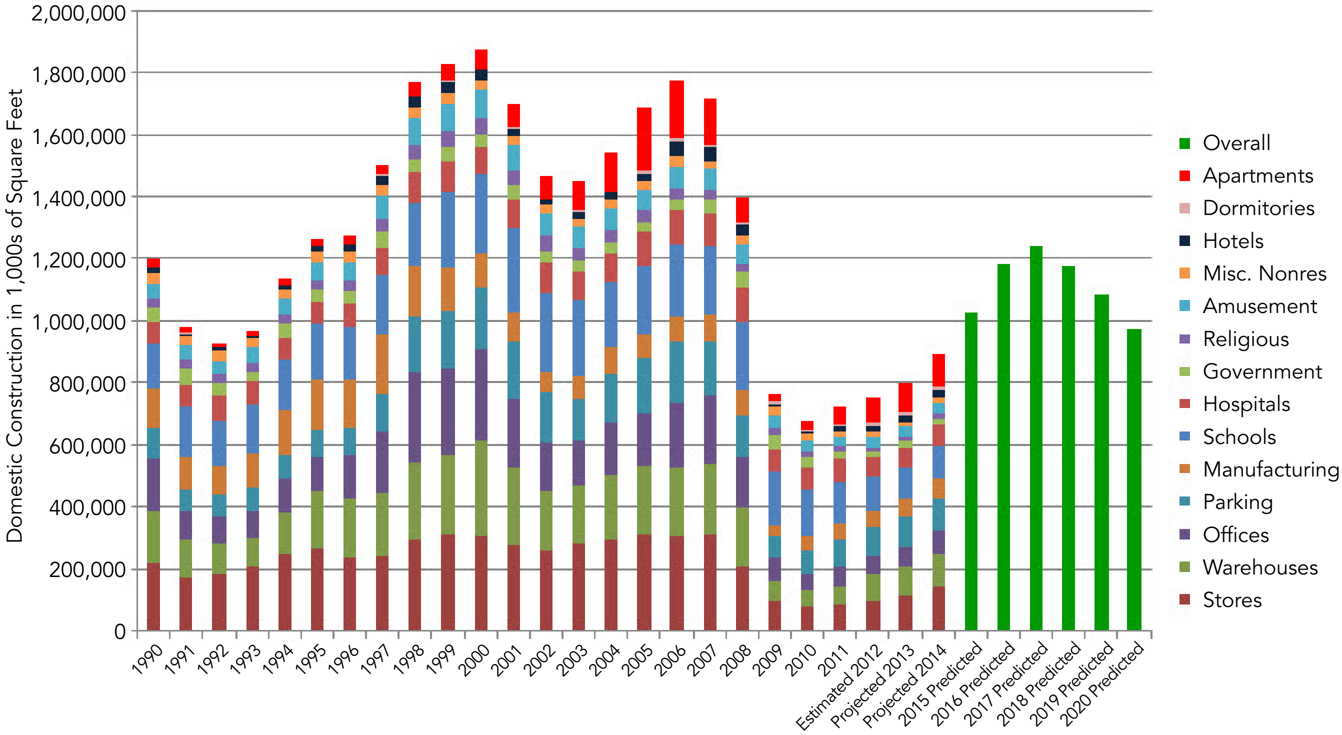
SOMETIMES THE MORE THINGS CHANGE, the more they stay the same.

Since the beginning of the construction downturn in 2008, economists have looked for signals that would mark the beginning of a non-residential construction turnaround.

John Cross is an AISC vice president. He can be reached at **cross@aisc.org**.

Historically, the signal that non-residential construction was about to gain momentum has been an upturn in housing starts. But the argument that the non-residential market needed to wait for a rebound in the housing market was largely downplayed in this recession. The conditions that triggered the housing downturn seemed to preempt a near-term housing rebound. The combination of the collapse of the sub-prime mortgage market, the tightening of lending standards, a glut of foreclosed homes on the market and a precipitous drop in housing values led industry observers in 2009 to write off a housing rebound anytime in the foreseeable future.

The long-maintained view that non-residential construction lags housing starts by two years was abandoned, and the search began for a new sector to lead non-residential construction out of its historic low volumes. The Obama administration gambled on an infusion of publicly funded capital projects, in the form of the 2009 stimulus program, to generate traction in the non-residential construction market. It didn't happen. By 2010 the discussion focused on the manufacturing sector and whether manufacturing and exports could lead the way out of



the construction recession. It didn't happen. In 2011 the focus turned to energy projects with hopes that alternative energy, nuclear and natural gas might produce the needed impetus to drive overall construction. It hasn't happened.

Instead, non-residential construction continued to limp along at historically low levels. After a free-fall of 67% in overall volume between 2007 and 2010, the market did stabilize and show limited growth in 2011 and 2012. But that growth only recovered 214 million of the 1.04 billion (21%) of the construction volume that had been lost.

So what about 2013? The building construction market in 2013 will look disapprovingly similar to the market of 2012. While the rate of growth for building construction will increase from 3.9% in 2012 to 6% in 2013, the dynamics of the market will remain constant. Public projects including courthouses, schools and prisons will continue to decline in volume, while privately funded projects will grow at modest rate, with only the retail, warehouse, hotel and multi-story residential markets posting double-digit gains.

The reelection of President Obama signals that there will be little change in the construction climate in 2013. The current administration will remain at odds with Congress over deficit reduction and tax rates. Independent of decisions regarding funding entitlement and defense programs, there is little possibility of any significant increase in any building program using federal funds. There may be some increase in private healthcare construction based on an increasing confidence that the funding formulas of the Obamacare can be relied upon for capital projects.

At the same time any hope of construction growth in 2013 is highly contingent on avoiding the fiscal cliff being approached at the end of 2012. If sequestration occurs as a result of the inability of Congress and the revitalized Obama administration to reach agreement, 2013 construction volumes will retreat 6% to 10% rather than growing by 6%.

So when will the non-residential construction market move into the range of double-digit growth and recover its earlier volumes? Contrary to the opinion of nearly every observer of the construction economy (myself included), it looks like home building is again positioned to lead non-residential construction back into a significant growth mode. Home building has picked up momentum in 2012 and it looks like that momentum will continue into 2013. The housing market is beginning its growth from a very low starting point, but it is starting to grow. If the long-term pattern of housing starts and non-residential starts are compared, it is obvious to even a casual observer that non-residential construction lags housing starts by roughly two years.

It certainly appears that the historic pattern of housing starts and non-residential construction may still be holding true. If that is the case, then double-digit growth in the non-residential sector should occur in the 2014/2015 timeframe. Interestingly this is probably the same point in time when U.S. employment levels will surpass the level when the recession began in late 2007, and GDP should be growing at a level greater than 3%. This will result in non-residential construction growth through 2017, reaching a peak that's roughly 25% below the peak of 2006/2007. MSC