

A FORECAST YOU CAN BELIEVE IN

BY JOHN CROSS, P.E.

When it comes to predicting the construction economy, accuracy is in the eye of the beholder.

THERE IS AN OLD STORY about an enterprising young economist who decided to supplement his income by publishing a newsletter in which he predicted economic trends for Wall Street investors. As a first step, he purchased a mailing list of 20,000 investors. He then wrote two newsletters based on different views of the economy. One newsletter indicated stock prices would rise, while the other indicated they would fall. He sent each complimentary newsletter to 10,000 investors from his mailing list; no one got both newsletters. A month later he again wrote two newsletters with the same message—one up and one down. But he only sent these complimentary newsletters to the 10,000 investors that had received the newsletter with the accurate prediction from the month before. This time 5,000 investors received the “market is going up” newsletter and 5,000 received the “market is going down” newsletter. The process was repeated at the end of the next month, with 2,500 investors receiving a free “up” newsletter and 2,500 a free “down” newsletter.

At the end of the third month he changed his approach. Instead of sending out another set of free newsletters, he sent out a letter to the remaining 1,250 investors that had received three accurate newsletters. The letter read “Dear Investor: You have now received three free newsletters that accurately predicted market trends for the past three months. No other investment service can claim that level of accuracy. In order to allow you to continue to benefit from this level of keen insight on the current economy and how the economy will impact stock prices, we are pleased to offer you our newsletter on a subscription basis for just \$395 per year.” Half of the remaining investors subscribed, generating \$250,000 in revenue.

The moral of the story for the structural steel industry is that if you listen to enough economists, you will eventually find one that has accurately predicted the construction economy for the past several years. Does that mean that the next prediction will be accurate? The decision is yours!

Every forecaster lives in fear that someone will pull out an old forecast to check the accuracy of the predictions. But a bit of accountability is always good. Over the past four years the forecasts presented in this column and at NASCC have been relatively accurate for overall building construction (all non-residential and residential in excess of four stories).

These forecasts were based on a model that evaluates the level of gross domestic product (GDP), the rate of change of GDP, overall non-farm employment and the rate of growth of employment. In mid-2014 it is anticipated that a significant

economic event will occur when employment reaches the same level (138 million) it was at prior to the beginning of the recession in late 2007. It will have taken the U.S. nearly seven years to regain the jobs lost in the recession. However, GDP growth will still remain below the 3% threshold, indicating that construction growth will still be moderate.

	Growth Forecast	Actual	Square Footage
2010	-10%	-10%	679 million
2011	6%	7%	734 million
2012	6%*	15%	847 million
2013	10%	11% (estimated)	940 million

*Note: The original forecast for 2012 was 6% growth based on a high level of uncertainty relative to the 2012 fiscal cliff. When the cliff was avoided early in 2012, the projection was adjusted to 12% growth.

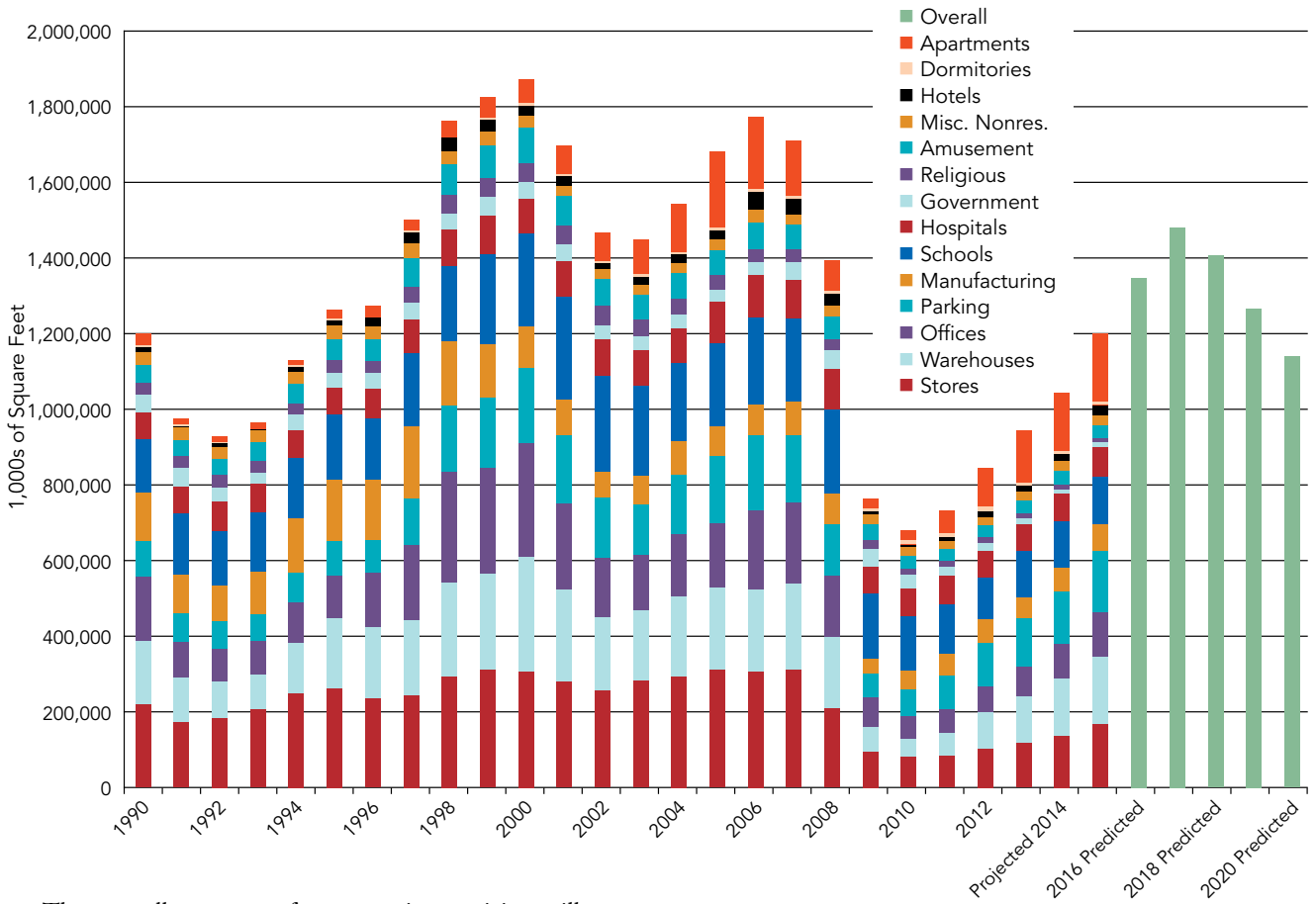
So what does this mean for building construction activity in 2014? On a square-footage basis of construction starts it is anticipated that the market will grow in 2014 by a rate very similar to that of 2013 (12%) with total construction activity crossing the one-billion-sq.-ft threshold.

But that overall growth rate of 12% in 2014 actually overshadows what should be even better news for the structural steel industry. Growth in the multi-story apartment and condominium market is actually expected to slow to 15% after a 2013 growth rate of 34%. At the same time the growth rate in the non-residential sector, where structural steel has a larger market share, will increase from 8% to 11%. The net impact would indicate an increase in demand for structural steel in the building market of 15% in 2014.

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The overall pattern of construction activity will continue to be characterized by several factors, including a reduction in publicly funded building construction, a rebound in the number of projects greater than four stories in height and a growth in project size. Interestingly, in several market sectors this growth in project square footage is quite noticeable. This is particularly evident in the warehouse sector where the average project is now 82,000 sq. ft compared to 25,000 sq. ft in 2009.

And no economic forecast is complete without a caveat: The outlook for construction growth is certainly dependent on a moderate level of confidence in the economy, security and governance of the U.S. A variety of factors such as more shutdown of government operations, default on government debt obligations, an increase in terrorist activity, a rapid tapering of quantitative easing and a general feeling of uncertainty could significantly reduce the level of construction activity.

So the “good news” newsletter forecast is that 2014 will look and feel very much like 2013, with a similar rate of growth of 12%. How much confidence can you put in that forecast? Unlike previous years, this forecast probably has more upside potential than downside risk. But whether or not you agree with the forecast probably depends on whether you would have paid \$395 for a newsletter subscription.

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