

# CONSTRUCTION MARKET UPDATE

Q3 2023

Mark Twain once wrote to a journalist seeking confirmation of the famous writer's death that his death had, in fact, been an "exaggeration."

It's still premature to apply the *Huckleberry Finn* author's quip to the rumors of a pending recession, but strong GDP, an easing of inflation and a low unemployment rate suggest **a recession may not necessarily be a foregone conclusion.**

Still, high interest rates and maddeningly long lead times for some industrial equipment continue to keep those involved in the construction of capital projects on edge.

However, **certainty does exist along two fronts for the construction industry:** 1) Skilled labor demand exceeds supply, and 2) lead times significantly exceed historical expectations for major electrical equipment and large engineered equipment.

## THREE TAKEAWAYS

1. RECESSION IS NOT A FOREGONE CONCLUSION.
2. DEMAND FOR CONSTRUCTION LABOR EXCEEDS SUPPLY.
3. SUPPLY CHAIN CHALLENGES FOR SOME EQUIPMENT STILL EXIST.

As we strive to meet project deadlines, the labor situation continues to frustrate us as we struggle to hire workers to meet the growing demand for critical infrastructure. And on the supply chain front, while prices for construction inputs have fallen or remained steady, **lead times for many pieces of equipment are 50%-100% longer than pre-2020 conditions.**

While challenges continue to exist in the industry, there are financial incentives available through the Infrastructure Investment and Jobs Act and other programs.

Hannah Morrey Brown of our consulting subsidiary 1898 & Co. walks through what you need to know about the grant application process on the last page of this update.

Thanks for reading and stay safe.



**BRETT WILLIAMS**  
PRESIDENT  
CONSTRUCTION GROUP

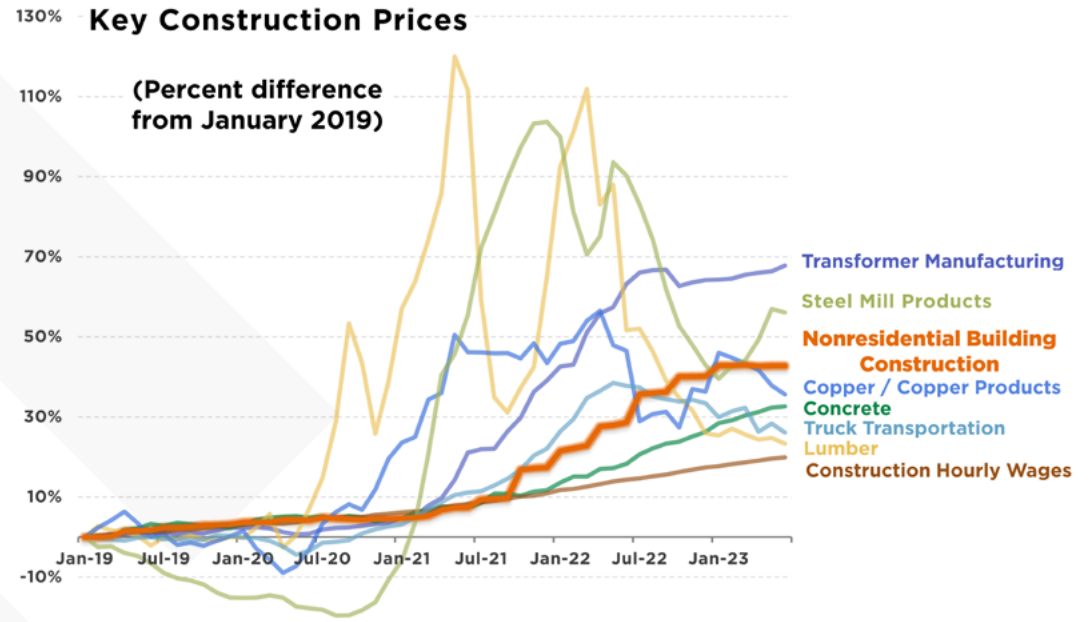
## ECONOMIC OUTLOOK: OPTIMISTIC?

Many economists as well as the Federal Reserve predicted a recession in 2023. Some even said it was necessary to reduce inflation. However, prices continue to drop, and **the economy remains strong**. Unemployment is low (3.5% in July), and GDP rose by 2% in the first quarter of 2023.

## INFLATION

Inflation continues to fall, with the Consumer Price Index, up 3.1% over the last year. Energy prices and core goods (excluding food and energy) were the primary drivers of inflation in 2021 before peaking in early to mid-2022. Rising prices for [core services](#) garnered attention in late 2022. Inflation from core services peaked in February 2023 but has fallen the last four months. Consumer and business inflation expectations also have been decreasing.

The Federal Reserve, however, is not yet convinced and may raise rates again this year. The Fed's preferred measure of inflation, the core Personal Consumption Expenditures Index had been flat for several months but **fell to a 4% year-over-year change in June**.



## SUPPLY CHAIN

Overall, **supply chain issues continue to improve**, with a few sticking points. The percentage of manufacturers citing materials shortages has fallen from over 40% in Q3 2021 to 24% in Q1 2023. Computers, electronics and electrical equipment have the largest remaining shortages.

The overall costs for inputs to nonresidential construction have stabilized in the first five months of 2023, with individual components moving in different directions:

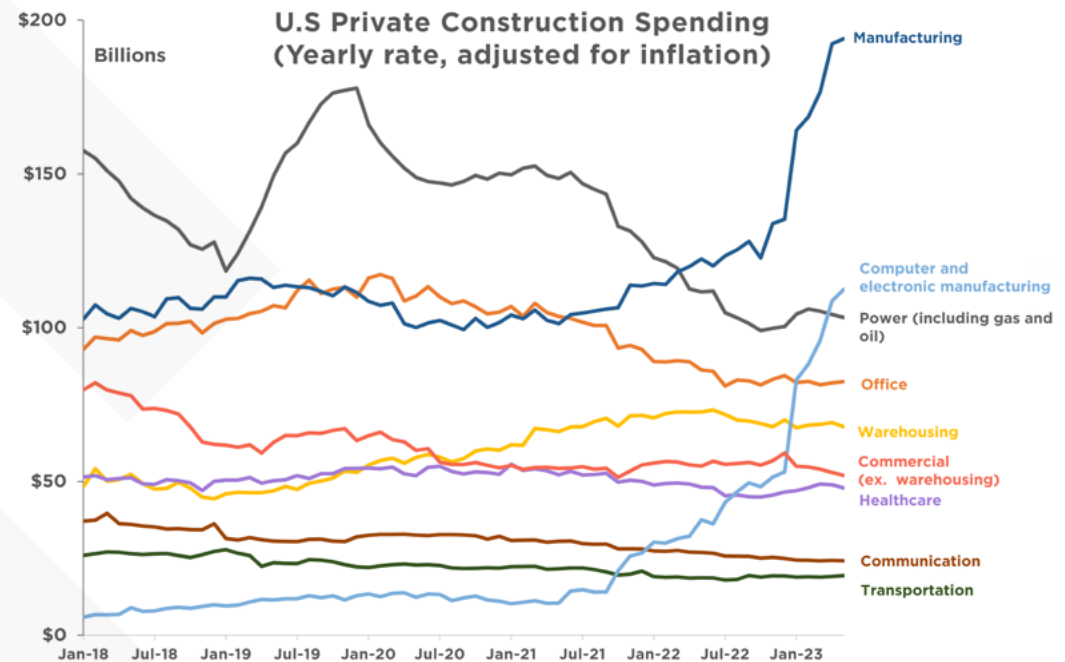
- Concrete and transformer prices continue to increase.
- U.S. steel prices rose in the first few months of 2023. Weakness in China's economy, especially its real estate sector, point to weaker steel prices globally.
- Copper prices and truck transportation prices continue to fall.

## CONSTRUCTION AND ENGINEERING

Industry sentiment has improved over the last two quarters as firms **have become more optimistic about the overall economy**. Engineering firms surveyed by the American Council of Engineering Companies reported an average backlog of 12 months for all firms and 14 months for firms with more than 500 people. Inflation and rising costs remain the No. 1 concern reported by firms.

Higher construction prices over the past two years indicated that while nominal construction spending increased, “real” spending (adjusted for inflation) decreased. Nonresidential construction spending remains \$80 billion (10%) less than its pre-pandemic peak, though it has been trending upward for the last year.

Since mid-2022, **construction spending in manufacturing has skyrocketed**, even after adjusting for inflation. The rise is driven by computer, electronics and electrical manufacturing (which includes semiconductors, batteries and solar panels); increased investment is incentivized by the Infrastructure Investment and Jobs Act, the Inflation Reduction Act and the Chips Act. Since January 2020, construction spending in this sector has increased over 700% and currently accounts for over 50% of total manufacturing construction.



Looking at other sectors, warehousing grew steadily throughout the pandemic, before falling over the past year. **Food and beverage construction spending is nearly 60% higher** than in January 2020. Power (including oil and gas), communications and chemical manufacturing remain well below pre-pandemic levels.

Job openings in construction have fallen to 4.6% of employment (as of May 2023). This is comparable to 2019, though still higher than historical levels.

## DIG IN: NAVIGATING THE IJJA GRANT FUNDING APPLICATION PROCESS

As of May 2023, more than \$220 billion in [funding from the Infrastructure Investment and Jobs Act \(IIJA\)](#) has been distributed, leading to the execution of 32,000 critical infrastructure projects nationwide.

Many funding opportunities fall under the decarbonization umbrella, are administered through the Department of Energy and have similar rigorous grant application requirements. If you have a construction-ready project — with a detailed estimate, schedule and strong but-for this funding argument — now is the time to [research and monitor available funding](#), understand how the administering agency directs funds, and know how to address essential application requirements to stand out among the sea of submissions.



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New to the grant application process because of IIJA is the [Community Benefits Plans](#) section. Though metrics haven't been established yet, each application requires this detailed information, broken down into four subsections:

- Community and labor engagement.
- American workforce investments.
- Diversity, equity, inclusion and accessibility advancement.
- Justice 40: This subset references 40% of nonmonetary benefits that will flow to disadvantaged communities, not 40% of project funding.

Knowing the importance behind this section, I recommend addressing it with the same level of care as the technical details. **If you can't speak confidently to [all four subsections](#), you will not receive funding.**

[Buy America](#) is another critical Biden administration initiative — and almost always a grant application requirement — that applies to nonfederal entities. If you are a for-profit entity, you are exempt from Buy America, but you will still be evaluated on your compliance against it as an additional program policy factor on most grants, i.e., your commitment to abide by it will benefit you on your application. The Office of Management and Budget [provides guidance](#) on how Buy America is administered.