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Third Quarter Construction Update: The Good, (The Strictly Okay), The Bad, and The Ugly

By Anirban Basu, Chief Construction Economist, CBIZ

Despite high interest rates, tight lending standards, policy uncertainty, and labor shortages, the construction industry continues to hold up remarkably well. While certain segments, like office and retail construction, have struggled in 2024, federally incentivized manufacturing projects and federally funded infrastructure projects have kept nonresidential contractors busy. With the presidential election completed, decision-makers should have a better idea of the policy environment they will operate in over the next four years.

Joe's View

Predicting the future may be a fool's game but it's hard to resist as we prepare for a new (or, in this case, returning) administration in Washington. Still, after several months of campaign messaging, we have hints of how the next four years could play out, with major implications for our industry.

I'm sure many share my top concern. I worry that deportations and increasingly strict immigration policies could further exacerbate the longstanding labor crisis in our industry and others. On a more hopeful note, we've seen what the CHIPS Act has done to support the construction of specialized manufacturing facilities. The future may hold more of a good thing in the form of re-shoring incentives for manufacturers outside of the tech space or even home builders.

I expect the much-discussed tariffs to be a mixed bag. Certain material and components costs will rise while encouraging domestic production capabilities. Meanwhile, rising geopolitical tensions threaten to disrupt global trade and increase costs further. My feeling is that the world has seen far too much conflict over the past few years and simply has no appetite for more. Let's hope if any of these predictions is proven right, it's that one.

So, there you have it! A little indulgence in an admittedly foolish game of fortune telling. I invite you to share your own perspective with me on the months and years ahead and look forward to hearing from you.

Joseph Natarelli, CPA

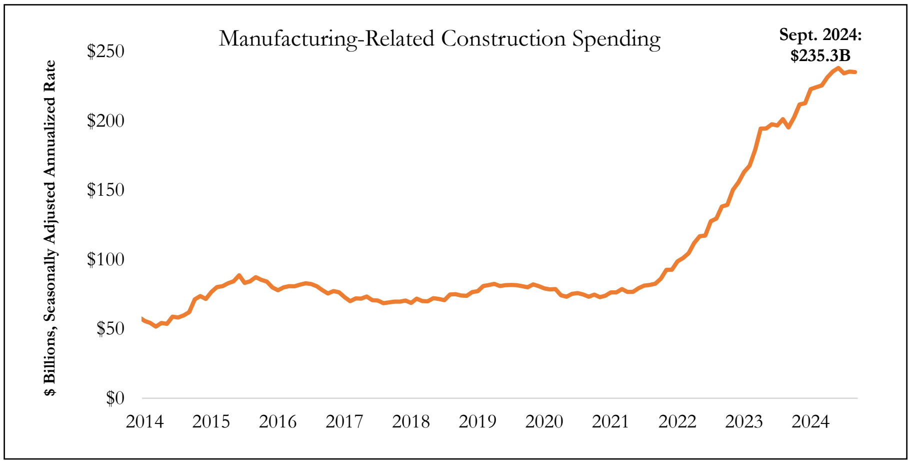
National Construction Industry Group Leader, CBIZ.

The Good

Manufacturing Construction

Manufacturing-related construction spending remains extraordinarily elevated due to federally incentivized megaprojects and a broader effort to reshore production capacity. While the incoming presidential administration may be less amenable to legislation like the CHIPS and Science Act and the Inflation Reduction Act, its trade policy should induce more reshoring, supporting ongoing momentum in the manufacturing segment.

EXIBIT 1. Manufacturing-Related Construction Spending

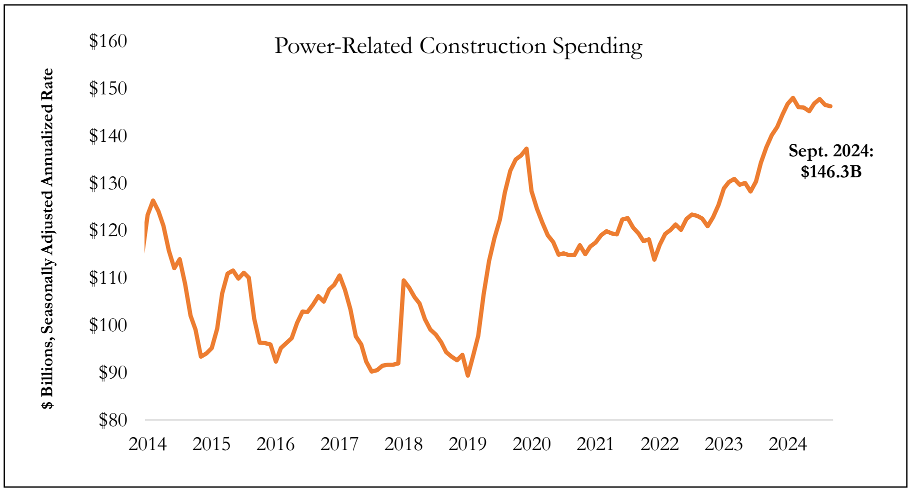


Source: U.S. Census Bureau; Note: Seasonally Adjusted

Power-Related Construction

Construction spending in the power category, which encompasses oil, gas, and electric, remains just below the all-time high established in February 2024. While it remains the case that almost all of the segment's momentum is due to electric projects (as opposed to oil and gas), the next presidential administration's policies will likely be a boon for fossil fuel-related construction activity. Although policy may shift to be less supportive of electrification, relaxed approval processes could very well lead to an uptick in electric-related construction as well.

EXIBIT 2. Power-Related Construction Spending



Source: U.S. Census Bureau; Note: Seasonally Adjusted

Materials Prices

Construction input prices increased 0.3% in October, according to the Bureau of Labor Statistics' Producer Price Index, but are down 0.2% over the past year. This continues a longer-term trend of input price moderation. Since reaching an all-time high in June 2022, materials prices have trended steadily lower, falling about 5%.

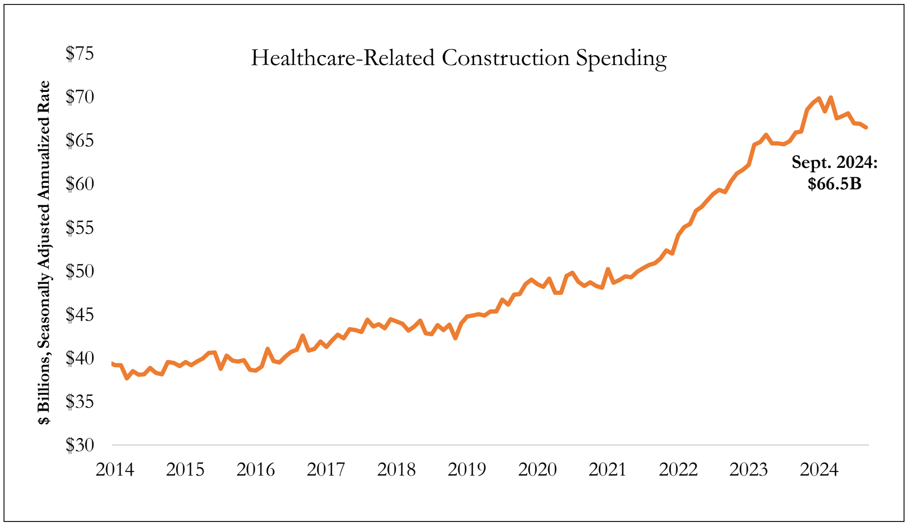
Despite this recent input price moderation, the next presidential administration's trade policies introduce significant uncertainty to the outlook. Tariffs could drive input prices higher, especially those that come primarily from China. If purchasers try to stock up on materials before the implementation of tariffs, prices could surge in the short term due to the sudden increase in demand.

The Strictly Okay

Healthcare Construction

Construction spending in the healthcare segment has fallen from the all-time high established in the first quarter but remains elevated by historical standards. Even with recent declines, investment in healthcare structures should remain elevated due to changing demographics. Construction

EXHIBIT 3. Healthcare-Related Construction Spending



Source: U.S. Census Bureau; Note: Seasonally Adjusted

Employment & Labor Supply

The construction industry added jobs for the fifth consecutive month in October, and job gains would have been faster if not for hurricanes Helene and Milton. The industry has hired new workers at a blistering pace over the past year, adding employees at exactly twice the rate of the broader economy. Staffing levels have expanded even faster for nonresidential contractors, with the subsegment's employment levels up nearly 4% over the past year.

While contractors are still struggling to fill open positions, especially in certain skilled trades, industry-wide labor shortages have eased in recent months. As a result, construction workers are no longer quitting their jobs at the historically elevated rates observed over much of the past few years.

Regionally, 15 of the nation's 20 largest metro areas added construction jobs over the 12-month period ending in September 2024. Hiring activity remains elevated in the south and parts of the Midwest, while western and northeastern metro areas have added construction jobs at a slower pace, if not lost them.

EXHIBIT 4. Construction Employment Growth, 20 Largest U.S. Metropolitan Areas, September 2023 v. September 2024

Rank	MSA	% Change	Rank	MSA	% Change
1	Miami-Fort Lauderdale-West Palm Beach, FL	8.9%	11	Seattle-Tacoma-Bellevue, WA	1.3%
2	Detroit-Warren-Dearborn, MI*	8.1%	12	Boston-Cambridge-Nashua, MA-NH*	1.0%
3	Houston-The Woodlands-Sugar Land, TX	7.1%	13	Los Angeles-Long Beach-Anaheim, CA	0.4%
4	Washington-Arlington-Alexandria, DC-VA-MD-WV*	3.5%	14	Chicago-Naperville-Elgin, IL-IN-WI	0.1%
5	Atlanta-Sandy Springs-Roswell, GA	3.4%	15	St. Louis, MO-IL*	0.0%
6	Dallas-Fort Worth-Arlington, TX*	3.4%	16	San Francisco-Oakland-Hayward, CA	-1.1%
7	Tampa-St. Petersburg-Clearwater, FL	3.3%	17	Minneapolis-St. Paul-Bloomington, MN-WI*	-1.5%
8	San Diego-Carlsbad, CA	2.1%	18	Riverside-San Bernardino-Ontario, CA	-1.5%
9	Philadelphia-Camden-Wilmington, PA-NJ-DE-MD*	1.6%	19	New York-Newark-Jersey City, NY-NJ-PA*	-2.1%
10	Phoenix-Mesa-Scottsdale, AZ	1.3%	20	Baltimore-Columbia-Towson, MD*	-2.2%

Source: U.S. Census Bureau; Note: Seasonally Adjusted

The Bad

Residential Construction

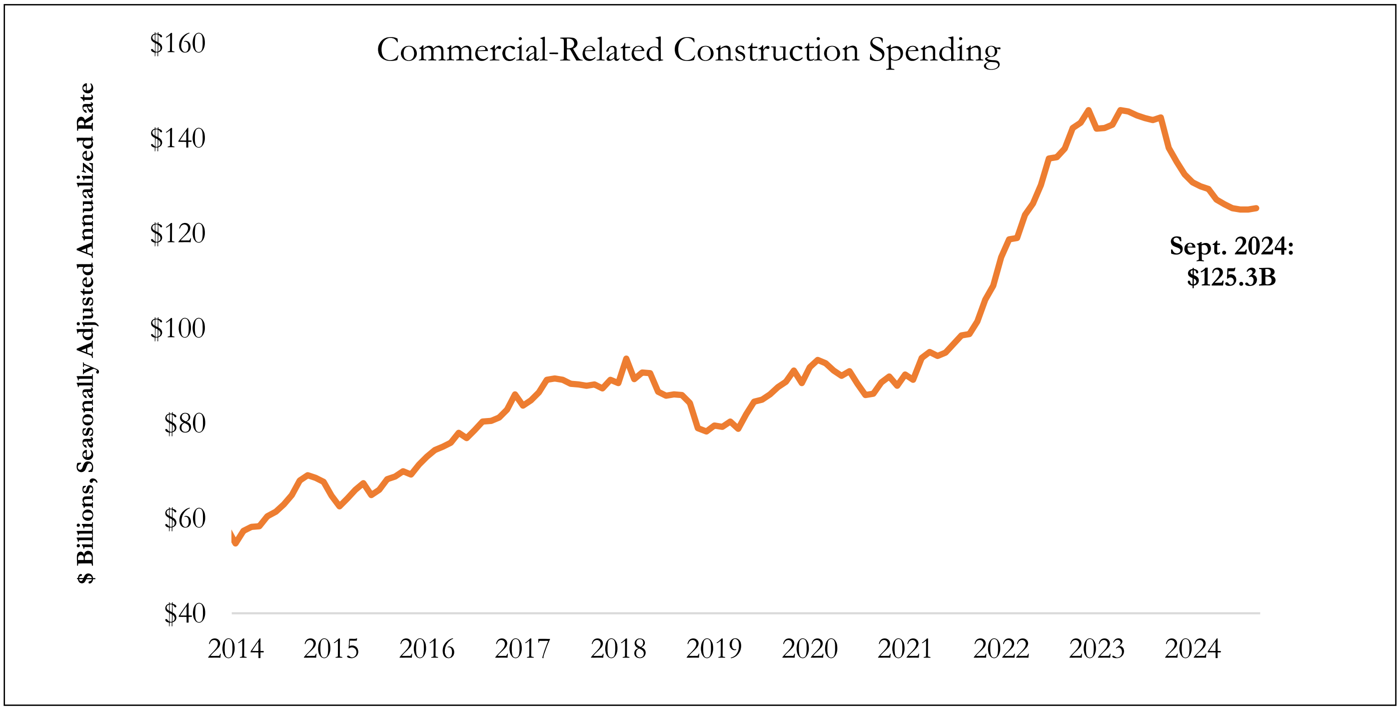
Residential construction spending is up just 4.2% over the past year and has struggled in recent months as mortgage rates remain elevated despite the Federal Reserve beginning to cut the target range of the federal funds rate. Multifamily construction activity, which surged during the early years of the pandemic, has fallen off sharply and is down 8.1% over the past twelve months. Construction of single-family homes has held up somewhat better, though spending on new units is up just 0.9% year over year. Of course, this slowdown is coming off of historically high levels of residential construction activity; there were more new housing units finished in August 2024 than in any month since early 2007.

While there remains a structural shortage of housing units in this country—a shortage that homebuilders will eventually address—residential activity will likely fall in the coming quarters. It won't rebound until interest rates are meaningfully lower. Based on current bond yields, the market expects the next presidential administration's trade policy to keep borrowing costs higher for longer.

Commercial Construction

Commercial construction spending fell sharply during the final quarter of 2023 and the first half of 2024 but appears to have leveled off in recent months. Despite the recent decline due to warehouse construction activity falling back from the record highs seen in early 2023, overall commercial-related construction spending is still up about 36% since the start of the pandemic. While the next administration's trade policy will likely suppress some retail construction, increased domestic truck and train shipping should benefit the warehouse and distribution segment.

EXIBIT 5. Commercial-Related Construction Spending



Source: U.S. Census Bureau; Note: Seasonally Adjusted

The Ugly

Interest Rates

Despite two interest rate cuts by the Federal Reserve, borrowing costs have yet to show a meaningful decline. In fact, mortgage rates have actually risen considerably since reaching a cyclical low in late September, with the average rate on a 30-year fixed mortgage rising from 6.08% to 6.79% as of the first week of November. As rates have risen, banks have kept their stringent lending standards in place, at least according to the Federal Reserve's Senior Loan Office Opinion Survey.

It appears likely that the Federal Reserve will reduce the federal funds rate by another 0.25 percentage points at its December meeting. Yet bond yields have risen since the election, suggesting that markets expect interest rates to remain higher for longer relative to previous forecasts.

EXHIBIT 6. Third Quarter 2024 Performance

Third Quarter 2024 Performance	Values			% Change from	
Gross Domestic Product (% Growth, SAAR)	2024Q3[1]	2024Q2	2023Q1		
Overall Real GDP	2.8%	3.0%	1.6%	-	-
Nonresidential Fixed Investment in Structures	-4.0%	0.2%	6.3%	-	-
Construction Spending, SA ($Millions)	Sep-24	Aug-24	Sep-23	Aug-24	Sep-23
Total Construction	$2,148,805	$2,146,048	$2,055,216	0.1%	4.6%
Residential	$925,359	$923,646	$888,453	0.2%	4.2%
Nonresidential	$1,223,447	$1,222,402	$1,166,763	0.1%	4.9%
Lodging	$23,483	$23,411	$25,202	0.3%	-6.8%
Office	$100,546	$100,598	$98,950	-0.1%	1.6%
Commercial	$125,304	$124,999	$144,449	0.2%	-13.3%
Healthcare	$66,508	$66,898	$65,905	-0.6%	0.9%
Educational	$129,245	$128,825	$124,592	0.3%	3.7%
Religious	$3,910	$3,815	$3,961	2.5%	-1.3%
Public Safety	$19,552	$19,570	$14,654	-0.1%	33.4%
Amusement and Recreation	$41,525	$41,570	$37,261	-0.1%	11.4%
Transportation	$70,127	$69,552	$65,400	0.8%	7.2%
Communication	$28,551	$28,649	$28,480	-0.3%	0.2%
Power	$146,275	$146,558	$137,584	-0.2%	6.3%
Highway and Street	$141,948	$141,361	$139,813	0.4%	1.5%
Sewage and Waste Disposal	$45,821	$45,575	$44,263	0.5%	3.5%
Water Supply	$33,551	$33,333	$28,667	0.7%	17.0%
Conservation and Development	$11,754	$11,935	$12,197	-1.5%	-3.6%
Manufacturing	$235,347	$235,755	$195,384	-0.2%	20.5%
Employment, SA (000s)	Oct-24	Sep-24	Oct-23	Sep-24	Oct-23
All Industries	159,005	158,993	156,832	0.0%	1.4%
Construction	8,310	8,302	8,087	0.1%	2.8%
Residential Building	957	956	932	0.1%	2.7%
Nonresidential Building	930	930	896	0.0%	3.8%
Heavy and Civil Engineering Construction	1,159	1,160	1,130	-0.1%	2.6%
Residential Specialty Trade Contractors	2,414	2,420	2,394	-0.3%	0.8%
Nonresidential Specialty Trade Contractors	2,851	2,837	2,735	0.5%	4.2%
Producer Price Index, NSA [2]	Oct-24	Sep-24	Oct-23	Sep-24	Oct-23
Finished Goods (SA)	143.5	143.4	143.2	0.1%	0.2%
Inputs to Construction Industries	318.8	317.8	319.6	0.3%	-0.2%
General Contractors (New Nonresidential Building Const.)	160.2	160.3	157.2	-0.1%	2.0%
New Nonresidential Building Construction (U.S.)	162.5	162.8	160.6	-0.2%	1.2%
Northeast	171.5	171.8	167.5	-0.2%	2.4%
South	158.9	159.0	159.3	-0.1%	-0.3%
Midwest	152.0	153.1	151.9	-0.7%	0.0%
West	170.0	169.9	164.8	0.1%	3.1%