THE CHALLENGES FACING A GROWING INDUSTRY: THE 2016 CONSTRUCTION HIRING AND BUSINESS OUTLOOK

The Associated General Contractors of America (AGC) is the leading association for the construction industry. Over 26,000 firms, including more than 6,000 of America's leading general contractors, nearly 9,000 specialty-contracting firms and almost 11,000 service providers and suppliers are associated with AGC through a nationwide network of chapters. Visit the AGC Web site at www.agc.org.

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SUMMARY

"The future for the next three to four years looks very promising if we can address key industry challenges..."
Survey Respondent

The construction industry will continue to recover in 2016 as many firms add headcount amid growing demand in a range of private and public sector construction markets. However, the industry faces a number of challenges that have the potential to dampen, and possibly undermine, the recovery. Among those challenges are workforce shortages, the growth in federal, state and local regulations and rising health care costs.

Perhaps because of the challenges they face, contractors are slightly less optimistic about their prospects for 2016 than they were at the start of 2015, especially when it comes to the percentage of firms who plan to hire and their outlook for various market segments. Yet they are optimistic enough to increase their investments in information technology as they seek to make their operations more efficient and more competitive in a market that is demanding increasing levels of sophistication from firms. Many firms also remain worried about worker shortages and their related impacts.

Most participants in this year's Outlook expect the industry's recovery to continue but appreciate that with growth will come challenges. While significant, these challenges can all be overcome. The 2016 Outlook makes clear that firms will succeed when the industry and public officials find effective ways to recruit and prepare future workers, make sure they are safe, manage health care costs and encourage smart investments in technology. In other words, 2016 won't be easy, but should definitely be a good year for many construction firms.

MIX OF PRIVATE AND PUBLIC SECTORS WILL DRIVE DEMAND

A mix of private and public sector market segments will drive demand for construction services in 2016. As measured by the net positive reading – the percentage of respondents who expect a market segment to expand vs. the percentage who expect it to contract – respondents are most optimistic about the outlook for retail, warehouse and lodging (21 percent net positive) followed by hospital (19 percent net), private office (19 percent net), multifamily residential (14 percent net) and higher education construction (13 percent net).

Respondents were similarly optimistic about these categories a year ago. This year they expressed greater optimism than before about the prospects for K-12 schools (12 percent net) and public buildings (12 percent net). Contractors are less optimistic about other private and public segments, including water and sewer (8 percent net), manufacturing (7 percent net), highway (6 percent net), other transportation, including rail, transit and airports, (3 percent net) and power (1 percent net). As was the case a year ago, they are pessimistic about the outlook for the direct federal construction market (-1 percent net). However, the survey was completed prior to enactment of federal legislation to increase funding for highways, transit and direct agency spending, and to extend the expiration date for wind, solar and other tax provisions helpful to construction.

While contractors were also bullish about the retail, warehouse and lodging segment in 2015, they were a lot more optimistic about demand for the manufacturing and power sectors last year than they are this year. Overall, contractors had higher expectations for many market segments heading into 2015 than they do now heading into 2016. For example, the net positive for the retail, warehouse, lodging segment in 2015 was 33 percent whereas this year it is only 21 percent.

MOST FIRMS WILL PLAN TO ADD TO THEIR HEADCOUNT IN 2016

Seventy-one percent of construction firms say they will increase their headcount in 2016. In most cases, however, that hiring will only lead to modest increases in the overall size of most firms. Indeed, 63 percent of firms report their planned hiring will only increase their total headcount by between 1 and 25 percent. Meanwhile only 6 percent of firms report they will expand their headcounts between 26 and 50 percent while only two percent of firms say they plan to expand their headcounts by 51 percent or higher.

Fortunately, very few firms – 6 percent – plan reductions in their total headcounts in 2016. Yet even as most firms plan to expand headcounts in 2016, those expansion plans appear less ambitious than in 2015 when 80 percent of firms reported plans to increase the size of their workforce. This is consistent with the fact that a smaller share of respondents expect expansions in most construction market segments in 2016 than in 2015.

FIRMS WILL CONTINUE TO COPE WITH WORKER SHORTAGES

"Experienced workers are getting harder and harder to come by with baby boomers retiring..."
Survey Respondent

One factor that appears to be affecting hiring plans in 2016 is the continued shortage of available qualified workers. Seventy percent of firms report they are having a hard time finding qualified workers, including salaried and craft professionals. And 69 percent of respondents predict that labor conditions will remain as tight, or get worse, during the next 12 months.

Many firms report they are increasing pay or benefits to retain or recruit qualified staff as a result of these worker shortages. Forty-nine percent of firms report they have increased base pay rates, 30 percent report they are providing incentives and/or bonuses, and 23 percent report they have increased contributions to employee benefits. Fifteen percent of firms report they are considering increasing pay and/or benefits in the near future to cope with worker shortages.

Even as firms increase compensation to recruit and retain workers, they are also investing in training and development programs for current and new workers. Nearly half of firms (46 percent) report they plan to increase their investments in training and development in 2016 compared to 2015.

Contractors' assessment of the labor market, and the steps they are taking to address worker shortages, are very similar to last year's Outlook, where a comparable percentage of firms reported challenges finding qualified workers, as well as the fact they planned to boost pay and/or benefits to help retain and recruit workers. In other words, after 12 months of raising pay, increasing benefits and working hard to attract new workers into the industry, contractors remain as worried about the lack of qualified workers as they were at the beginning of 2015.

LABOR, COMPETITION AND REGULATIONS ARE TOP CONCERNS

When asked to identify the issues that are the biggest concern to their businesses, a majority of contractors (52 percent) said they were worried about worker shortages. Forty-five percent of contractors reported they were worried about worker quality, which is also clearly related to the challenge of worker shortages. And 40 percent said they were worried about rising direct labor costs.

Even as contractors worry about competing for workers, they are also very worried about the challenge of competing for work. 43 percent of firms cited increased competition for projects as among their major concerns. They are also worried about the continued expansion of regulatory burdens, with 39 percent reporting they were worried about the growth in federal regulations and 34 percent responding that they were worried about the growth in state and local regulations as well.

LACK OF SKILLED WORKERS MAY IMPACT SAFETY

The shortage of qualified construction craft and salaried professionals is the most likely threat to workplace safety according to survey respondents. Forty-seven percent report that inexperienced skilled labor and worker shortages are a major challenge to the safety and health of workers. Another 37 percent cite worker shortages as a minor challenge.

Many contractors are also worried about the safety and health performance of the subcontractors with whom they work. Eighteen percent of contractors list poor subcontractor safety and health performance as major concerns and another 47 percent said it was a minor concern. Much of the concern about subcontractor performance is likely connected to the same workforce worries that contractors cite for their own safety challenge.

Contractors are also concerned about the continuing shift away from the hallmark collaborative approach to safety that has helped bring about significant improvements in construction safety since the mid-1990s. The current administration has made it clear that its preferred regulatory approach is enforcement over collaboration. Thus it is not surprising that 19 percent of contractors cited the lack of cooperation from federal regulators as a major safety concern while another 40 percent said it was a minor concern.

CREDIT CONDITIONS CONTINUE TO IMPROVE…

Credit and lending conditions continue to improve for construction firms and remain stable for developers according to the Outlook survey results. Only 4 percent of firms reported having a harder time getting bank loans compared to a year ago, which is down from 7 percent in last year’s Outlook and 9 percent in 2014. Credit conditions appear stable for developers as well, with 24 percent of respondents noting that credit conditions have caused their customers to delay or cancel projects, the same percentage as in 2015.

…AS HEALTH CARE COSTS CONTINUE TO GROW

"Obamacare is killing us. Nothing left for pay increases."
Survey Respondent

While credit and lending conditions are improving, health care costs continue to climb for the vast majority of construction firms. Seventy-nine percent of firms report the cost of providing healthcare for their employees increased in 2015. In addition, 81 percent of firms report they expect their healthcare costs to increase in 2016. These figures are almost identical to last year, when 76 percent of firms reported their health care costs went up in 2014 and 81 percent expected their costs to increase in 2015.

CONTRACTORS ARE INCREASING THEIR INVESTMENTS IN I.T.

In a Sage information technology (IT) survey conducted over the past two years only 32 percent of contractors surveyed indicated they spent at least 1 percent of revenue on IT. The 2016 Outlook shows that percentage increasing from 32 percent to 42 percent of companies saying they spent at least 1 percent of revenue on IT in 2015. In addition, 41 percent say that compared to 2015 their 2016 investment in IT will increase. Investment will continue in core business systems such as accounting (25 percent of respondents), estimating (22 percent), project management (21 percent), document management (20 percent), and scheduling (19 percent).

Many contractors are also making sure their investments are strategic. According to the Outlook survey, 42 percent of respondents have a formal IT plan that supports their business objectives and an additional 11 percent plan to put a formal plan in place in 2016. Still, nearly half of respondents do not include IT in their business planning process.

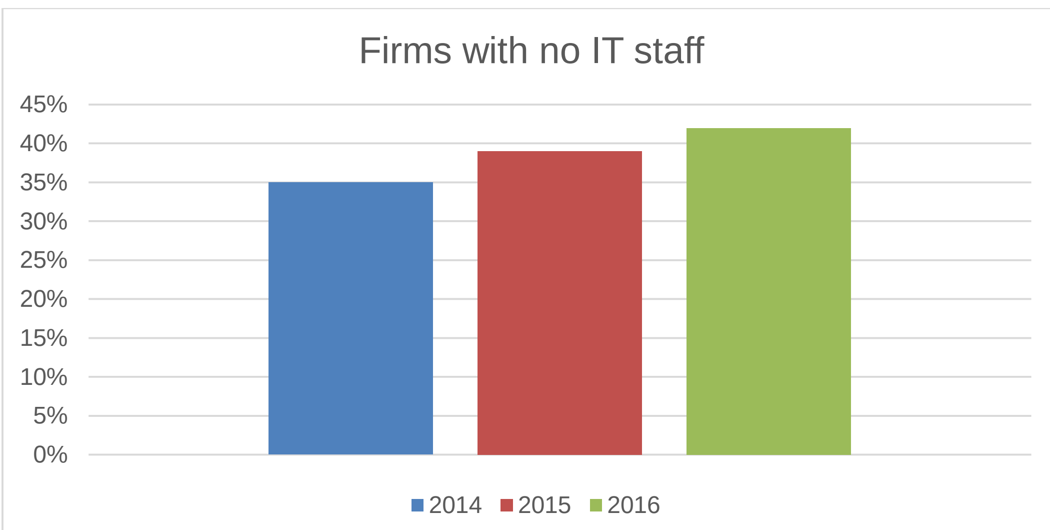
CLOUD TECHNOLOGY IS NO LONGER JUST FOR EARLY ADOPTERS

Back in 2012, 45 percent of respondents to a Sage IT survey indicated that they were not familiar with "the cloud" and 44 percent were only somewhat familiar with the technology. That no longer is the case. According to the Outlook survey, 59 percent of respondents currently use or plan to use cloud-based software. The ability to access information anytime and from anywhere is the main reason survey respondents (63 percent) say they are adopting cloud-based software.

Concerns about security were the main reason 23 percent of respondents are not using cloud-based software.

SMALLER COMPANIES ARE LIKELY TO OUTSOURCE THEIR I.T.

Since 2014 Sage surveys have revealed a gradual increase in the number of firms that have no in-house IT staff (from 35 percent in 2014, to 39 percent in 2015, and to 42 percent in 2016). According to the 2016 Outlook survey, the majority of contractors (69 percent) rely on outsourced services to manage their IT functions. Outsourcing is especially prevalent among smaller construction firms. More than 3 out of 4 survey respondents in firms under $50 million in revenue outsource their information technology.

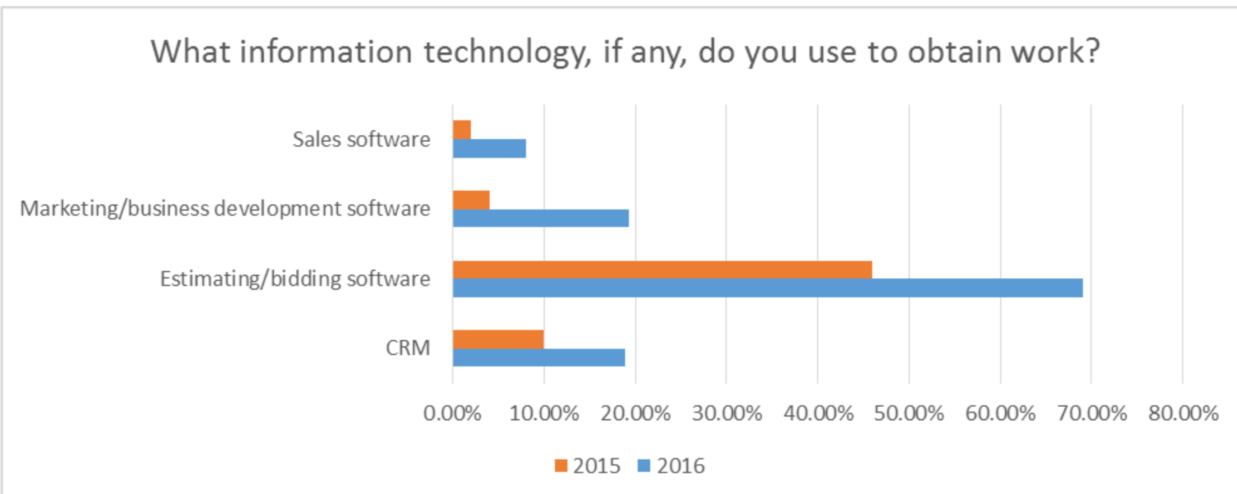


COLLABORATION TECHNOLOGY IS GAINING A FOOTHOLD

While email (used by 92 percent of respondents) and file sharing sites (used by 71 percent) are still the predominant methods contractors use for collaborating with project partners, more sophisticated online collaboration software has been adopted by 40 percent of respondents. Adoption of Building Information Modeling (BIM) and online collaboration software increases significantly with the size of the contractor.

MORE FIRMS ARE USING TECHNOLOGY TO WIN BUSINESS

Increased competition for jobs (listed among the three biggest concerns of Outlook survey recipients) appears to be driving more adoption of software tools aimed at obtaining work. A similar IT survey conducted by Sage last year shows how adoption of this type of technology is spreading:



MORE FIRMS ARE TAKING STEPS TO ADDRESS IT SECURITY

Overall, the industry is increasingly taking steps to protect company data. The majority of survey respondents (75 percent) said they currently have an overall IT security plan in place to protect against hacking. Tighter security around mobile devices is also occurring. In 2015 a similar survey conducted by Sage showed only 31 percent of respondents with a mobile security policy in place. The 2016 Outlook survey shows that number increasing to 46 percent with a mobile security policy in place. More companies are also opting to supply all mobile devices used at work. Last year's Sage survey showed 41 percent of companies choosing this method compared to 54 percent in this year's Outlook survey.

REGIONAL MARKET ANALYSIS

The outlook by market segment varies among the four different regions – Northeast, Midwest, South and West – the association analyzed. Contractors in the Northeast are most optimistic about multifamily construction (27 percent net positive), followed by higher education (20 percent net) and retail, warehouse & lodging (18 percent net). Midwestern firms are most optimistic about retail, warehouse & lodging construction (18 percent net), followed by hospital (17 percent net) and private office (13 percent net). In the South, contractors are most optimistic about the prospects for hospital construction (25 percent net), followed by retail, warehouse & lodging (23 percent net) and K-12 school construction (20 percent net). In the West, contractors are most sanguine about the private office market (28 percent net), followed by multifamily residential (27 percent net) and retail, warehouse & lodging (25 percent net).

Contractors in all four regions provided relatively consistent answers regarding their plans to expand headcounts – ranging from 70 percent in the Midwest to 73 percent in the Northeast. Yet construction worker shortages appear to be less of a concern for contractors in the Northeast than in the rest of the country. Fifty-nine percent of contractors in the Northeast report having a hard time finding workers compared to 73 percent in the Midwest, 70 percent in the South and 73 percent in the West.

Otherwise, the Outlook for 2016 were remarkably consistent between regions, with similar responses for the remaining questions covered in the survey.

CONCLUSION

Contractors are expecting 2016 to be a mostly positive year. Most firms expect key market segments to expand or remain stable, they plan to expand their headcount and they are prepared to invest in new technologies. Yet their enthusiasm is tempered by the expectation that labor conditions will remain tight, new and relatively inexperienced workers will pose new safety challenges, the cost of complying with regulations will continue to grow, their health care costs will rise yet again and their new technology could pose new security threats.

Considering a host of other economic indicators, including construction spending and hiring data the Associated General Contractors of America closely tracks, contractors are right to be optimistic. Construction spending continues to expand at rates not seen since before the economic downturn nearly a decade ago. Construction employment has been steadily increasing nationally, in most states and in a majority of metro areas for more than two years now. And prior Sage studies have confirmed that many contractors understand the value of investing in new technologies.

Yet other data, including recent AGC of America workforce survey data, confirm the challenges contractors reported in the Outlook. Contractors have been consistently raising concerns about the lack of available qualified workers for the past two years. The association has also consistently raised questions about the expanding scope and cost of a series of new federal regulations that are better designed to generate positive headlines than actually protect workers or the environment. Federal and privately-gathered data confirm the continued increase in health care costs despite, or perhaps because of, the Affordable Care Act. And recent widespread instances of IT-related security breaches highlight the hazards that come with some new technologies.

These challenges are real, but they are not insurmountable. Indeed, many of the measures the association outlined in its recently updated Workforce Development Plan are designed to re-invigorate the pipeline for recruiting and preparing new construction workers. The association has also helped coordinate industry-wide efforts to ensure that any final new regulatory measures are effective and minimally disruptive. And software such as that offered by Sage can help with secure cloud-based software products that protect a construction company's data through encryption, regular software audits and other defensive measures.

As long as local, state and federal officials are willing to act on our workforce development measures, embrace a more rational approach to regulations, identify effective measures for controlling health care costs and protect internet-based transactions, the industry should continue to expand. Expanding construction companies, as well as the structures they produce, will contribute new energy and investments into the broader economy, helping ensure greater prosperity and economic security well beyond just the construction industry.

ABOUT THE SURVEY

AGC conducted the survey that serves as the basis for the 2015 Construction Hiring and Business Forecast during November and December 2015. Over 1,500 firms from the District of Columbia and every state completed the survey. (Varying numbers responded to each question.) Participating firms represent a broad cross-section of sizes. Thirty-five percent report performing $10 million or less worth of work in 2015. Twenty-six percent performed between $10.1 million and $30 million worth of work, 9 percent between $30.1 and $50 million, 10 percent between $50.1 and $100 million, 15 percent between $100.1 and $500 million, and 6 percent performed over $500 million worth of work. Thirty-two percent of firms report they employ union workers most or all of the time while the remainder are either exclusively open shop or only occasional employ union labor. Contractors who completed the survey were entered into a raffle to win a $100 Amazon gift certificate. Other than that, firms and their employees were not compensated or in any other way reimbursed for completing the survey.

The regions covered in the survey included the following states:

Northeast

Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, Vermont

South

Alabama, Arkansas, Delaware, District of Columbia, Georgia, Florida, Kentucky, Louisiana, Maryland, Mississippi, North Carolina, Oklahoma, South Carolina, Tennessee, Texas, Virginia, West Virginia

Midwest

Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, Wisconsin

West

Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, New Mexico, Nevada, Oregon, Utah, Washington, Wyoming