CFOS UPBEAT HEADING INTO ‘17

THE CONFINDEX™ NUMBER

Positive Trump Effect on Display

Ever since that fateful Tuesday in November, economists, among others, have been puzzling over what the election results mean for various U.S. public policies and economic performance. The President-elect has indicated that he will slash taxes, strengthen U.S. trading partners, and commitments to follow certain environmental rules, dramatically alter immigration policy, partially deregulate banking, and make drilling for oil easier. There may also soon be a new infrastructure-led stimulus package and significant changes to America’s health insurance setup.

The President-elect has suggested that these moves will help turbocharge the economy, which has failed to expand at a three percent pace or better since 2005. There are certainly many economists who have expressed skepticism regarding the wisdom of this package of economic measures, indicating that such policy shifts could spike the national debt, ignite trade wars, and accelerate inflation.

Perhaps, at least over the near-term, the U.S. economy is about to enjoy added stimulus at a time when full employment already approaches. The expected stimulus will likely push prospective economic weakness back to 2019, 2020, or beyond, but when the next recession arrives, it may be much deeper than it otherwise would have been.

The future rests with whether the stimulus to come significantly and sustainably accelerates economic growth and augments productivity in order to offset the impacts of presumed higher interest rates. The absence of a meaningful acceleration of growth would also elevate America’s need to address its ever-expanding national debt.

For now, construction industry chief financial officers are viewing the Trump glass as half full or better, at least according to the most recent CFMA CONFINDEX survey results. Responses to the survey came after November 8, which means that CFO responses embody the knowledge that Mr. Trump is headed to Washington.

Prior to the most recent survey administration, CONFINDEX levels were generally flat or declining during prior quarters. There were a number of reasons for this, but a growing fraction of CFOs was expressing concern regarding future construction spending volumes. Anecdotal data from certain leading markets, such as New York, Boston, and Miami, indicate that construction backlog growth had slowed as developers and their financiers became increasingly concerned by the possibility of overbuilding in certain key product segments.

For now, the gradual build in pessimism has been reversed. All the major survey indicators were up during the fourth quarter of 2016, including the Overall CONFINDEX reading, which rose to 127, fully 4.1 percent above its third quarter level. Overall confidence is 61 percent higher than it was in December 2008 when construction activity was in rapid retrenchment and when CFOs were looking ahead to the inauguration of President Obama.

The Business Conditions Index rose to 129 during the fourth quarter, up 4.9 percent from the third quarter. This index is still down 5.1 percent from a year ago, a reflection of the growth in pessimism during prior quarters. Between 2015’s final quarter and the third quarter of 2016, the Business Conditions Index slumped from 136 to 123.

Predictably, the Current Confidence Index also rose during the fourth quarter, from 126 to 129, an increase of 2.4 percent. The increase would have been more positive, one suspects, but for the fact that many of Trump’s proposed pro-business initiatives will take some time to implement and impact the volume of economic activity. As a result, the election’s implications are not as forcefully reflected in the Current Confidence Index.

It is also not surprising that the Financial Conditions Index improved. A disproportionate share of the financial market rally that has transpired since the election of Mr. Trump has pertained to banks. The conventional wisdom is that the burden of financial regulation is likely to be reduced substantially over the course of the next several years, allowing banks to deploy their capital and liquidity more aggressively while reducing compliance costs. All things being equal, this will translate into more financing available to both construction firms and the clients they serve.

Perhaps the most telling indication of Mr. Trump’s likely impact on American construction activity is reflected in the Year-Ahead Outlook Index, which surged from 117 during the third quarter to 124 during the fourth, an increase of six percent. Despite the general indication of growing optimism, CFOs are complicated economic actors and have much to consider. It is worth noting that the Year-Ahead Outlook Index remains below mid-2015 levels.

While many CFOs are encouraged by the likely positive economic impacts on construction activity associated with promised tax cuts and stimulus spending, an acceleration in construction spending will also presumably translate into larger workforce deficits and faster wage growth. The vast majority of CFOs remain deeply troubled by expanding human capital shortfalls, which have increasingly compromised profit forecasts. Higher interest rates represent another consideration, one that could further impact future construction firm profitability. The overall picture seems to be one in which average construction CFOs relish the idea that their firms will continue to be busy, but manifest constrained exuberance given the uncertain impact on profitability and the unknown duration of improved economic performance.

Looking to 2017

In our prior CONFINDEX report, we indicated, “Soon the election will be over and the most recent CONFINDEX survey suggests that the period thereafter is quite likely to represent a period of reaccelerating construction activity.” We were right. On average, CFOs are looking forward to a busy 2017, but as always, there is some level of trepidation that will greet the New Year.
A SIMPLE EXPLANATION OF CONFINDEX™

• The Overall CONFINDEX™ Number
  • Composite Index Comprised of 4 Sub Indices
    1) Business Conditions
    2) Financial Conditions
    3) Current Conditions
    4) 2017 Outlook – look ahead to December 2017

• Measurements Taken Using 8 Questions
  • Current Business Conditions
  • Future (1 year) Business Conditions
  • Current Bank Credit Availability
  • Future (1 year) Bank Credit Availability
  • Future (1 year) Bonding Credit Availability
  • Line of Credit Status
  • Current Backlog
  • Future (1 year) Backlog

• We calculate indices by taking the “net” of positive responses minus negative responses and adding 100. (Neutral and No Answers are excluded)

• Any index greater than 100 reflects more positives than negatives. Any index less than 100 reflects more negatives than positives.