TRUMP TURMOIL CURBS Q2 CONFIDENCE

A combination of anecdotal information and survey data indicate that certain purchasers of construction services, including commercial real estate developers, are now experiencing tighter credit conditions. However, there is roughly an equal amount of information suggesting that financing conditions have not changed significantly during the past six months.

The Current Confidence Index fell 2.3 percent during the quarter indicating a modest loss in optimism regarding the near-term. This sub-index is the only one to be down on a year-over-year basis. The implication is that some CFOs have begun to see clouds on the horizon. With the president’s pro-business agenda continuing to lack legislative momentum, the feeling may be that growing business volume will not countervail the negative impacts of rising materials and labor costs to the extent expected.

This coincides with shifting expectations regarding profitability. Two quarters ago, 46 percent of CONFINDEX respondents believed that their enterprises’ profit margins would be significantly better or slightly better a year hence. By the second quarter, that proportion had slipped to less than one third (30%). More than half of the respondents (54%) expect profit margins to be roughly unchanged in one year and about one sixth of the respondents expect slight deterioration in profitability.

Perhaps most revealing, the Year-Ahead Outlook Index declined 9.2 percent, during the second quarter, to 119. During the prior quarter, this sub-index had climbed from 124 to 131. No sub-index sustained as large a quarterly decline as the Year-Ahead Outlook Index, perhaps an indication that many CFOs have concluded that many of the new administration’s pro-business policies will ultimately fall short of seeing the light of day.

Still, the average CFO remains more upbeat than he or she was a year ago. The Year-Ahead Outlook Index is up 7.2 percent from a year ago, which happens to be the largest year-over-year increase in any of the indices.

While most industry stakeholders remain firmly fixated on skills shortages, materials prices have also emerged as an increasingly pressing concern. The share of respondents who perceive that materials prices are worse increased from 47 percent during the first quarter to 53 percent during the second. Moreover, 47 percent of respondents expect prices to be slightly or significantly worse a year from now.

Slow Growth Trajectory?

Confidence may continue to wane if the new administration is unable to deliver meaningfully on its pro-business agenda. Perhaps no feature of that agenda has captured the imagination of construction executives more than a proposed infrastructure-led stimulus package to revolve heavily around public-private partnerships.

With the stalled “repeal and replace” of the Affordable Care Act and midterm elections edging closer, CFOs may more firmly conclude during the third quarter that America’s slow growth trajectory will remain in place. That would likely result in further declines in the overall CONFINDEX and in key sub-indicators. Of course, predicting political outcomes is a treacherous affair, particularly when those outcomes depend so intensely on one Donald J. Trump.

Pro-Business Agenda Remains Unfulfilled

It’s not that CFOs are expressing widespread pessimism. Rather, it’s simply that the ebullience that characterized the first quarter was largely reversed during the second.

Since the president’s election in November 2016, there has been a sense that U.S. economic growth prospects have improved. This was not only reflected in surveys of business executives. Interest rates raced higher shortly after the election – a reflection of forecasts for faster economic growth and stepped up inflation expectations.

The new administration has offered a litany of pro-business ideas ranging from deregulation of key economic segments to corporate tax cuts and a trillion-dollar infrastructure package designed to efficiently leverage private capital. Some key ideas were to have been implemented on day one; others within the first 100 days. By mid-June, the 100-day mark had been long eclipsed and hopes for a supercharged America remained unfilled. America appears poised for another two percent growth year in 2017.

Accordingly, the overall CONFINDEX reading declined by more than five percent during the second quarter, and is now up less than two percent on a year-over-year basis. Overall, CONFINDEX stood at 123 during the second quarter, after increasing to 130 during the year’s first three months.

The Business Conditions Index declined by almost nine percent during the second quarter and is also up by less than two percent on a year-over-year basis. In other words, business conditions have barely budged since mid-2006, when the economy was on its way to posting 1.6 percent growth for the year. Still, the Business Conditions Index is up 97 percent from its December 2008 reading of 63. The implication is that many construction firms remain busy. Available data suggest that backlog remains elevated and has expanded recently across a number of key construction segments.

Two sub-indices posted less dramatic declines during the second quarter. The Financial Conditions Index slipped by 1.6 percent during the quarter and now stands at 123. That’s up 2.5 percent from one year ago.

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**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) 2018 Outlook – look ahead to June 2018

- **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.