The year did not start off well. That was not completely surprising. Economic momentum ebbed during last year’s final quarter, at least when measured in terms of output growth. Nonresidential construction spending growth also sputtered as 2015 came to an end.

2016 began with considerable financial turmoil, as bad economic and financial news from China sent commodity and other prices reeling. Though employment growth has remained reasonably strong in America, corporate profitability has been eroded by a number of factors, including a strong U.S. dollar, weak global economy, and sagging energy sector.

It would be difficult to identify a construction industry CFO who does not remember the onset of the Great Recession. Economic conditions deteriorated quickly, with many construction firms quickly transitioning from elevated profitability and lengthy backlog to eviscerated pricing power and a dearth of opportunities to bid for work.

Accordingly, CFOs are justifiably concerned when financial markets become turbulent and economic data disappoint. Construction firms are busy today but many CFOs are waiting for the next hammer to fall and some level of jitteriness is to be expected even after several years of recovery.

The expression of growing concern regarding economic and construction industry prospects is neatly reflected in the latest release of CFMA’s CONFINDEX. During 2016’s first quarter, the Overall Confidence Index slipped to 123. This represents the lowest index reading since December 2012. That’s not to say that the construction industry is on the verge of recession. Rather, the most recent data suggests that the pace of backlog growth may slow just a bit for the typical contractor.

Recovery Somewhat Waning

CFOs do not seem to collectively believe that the profit growth cycle is at an end. 41 percent of surveyed CFOs expect profit margins to be slightly better (38%) or significantly better (3%) a year from now. That compares to the 14 percent of CFOs who expect profit margins to be slightly worse (13%) or significantly worse (1%) a year from now.

The only sub-index to hold its own during the year’s initial quarter was the Financial Conditions Index. Despite recent financial turmoil, money to fund development continues to be available, which is consistent with observations regarding ongoing construction starts. The Financial Conditions Index now stands at a reading of 120, essentially unchanged relative to the prior three CONFINDEX readings.

Despite the growing focus on cyclical issues, it is a structural issue, skills shortages, that continues to dominate the CFO list of concerns. Nearly three quarters (73%) of CFOs are either very or highly concerned about skills shortages. However, the proportion that is highly concerned, which represents the most intense level of concern, declined from 45 percent during last year’s final quarter to 37 percent during this most recent reading. This represents another indication that CFOs are expecting less vigorous industry expansion going forward, which will alleviate the degree of skills shortages.

Interestingly, though much focus is being given to the current presidential election cycle, CFOs have become less concerned by issues of public policy. In December 2015, only 22 percent of CFOs indicated that they were not concerned at all by demand for construction. One quarter later, this proportion had fallen to 17 percent.

The Current Confidence Index, which reflects all current business conditions, such as levels of bank credit availability, bonding, working capital, and backlog, dipped nearly four percent on a quarterly basis and has fallen by nearly nine percent over the past year. Perhaps most telling, the Year Ahead Outlook Index fell to 117, 12 percent below where it was one year ago. This sub-index pertains to anticipated future business conditions, future bank credit, bonding, and backlog.

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Interestingly, though much focus is being given to the current presidential election cycle, CFOs have become less concerned by issues of public policy. In December 2015, only 22 percent of CFOs indicated that they were not concerned at all by public policy regarding construction. By the first quarter of 2016, this proportion had risen to 27 percent. There are a number of possible explanations for this diminished concern, at least among CFOs in certain segments. One explanation is that many firms stand to benefit from the recent passage of a federal highway bill. The federal government also recently avoided another shutdown.

Uncertainty Sums It Up

This first CONFINDEX survey and results of 2016 stands for the proposition that the nation’s construction recovery will remain in place for the foreseeable future, but may become a bit less brisk. While financial conditions remain supportive, there is more uncertainty regarding future economic prospects, which might induce a higher fraction of project owners to postpone starts. Financial market turbulence can also impact the availability of capital and interest rates.

The good news is that economic and financial data have recently improved despite recent financial turmoil. Despite recent financial turmoil, money to fund development continues to be available, which is consistent with observations regarding ongoing construction starts. The Financial Conditions Index now stands at a reading of 120, essentially unchanged relative to the prior three CONFINDEX readings.
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 March 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.