CONSTRUCTION CFO CONFIDENCE IS RESTORED

Pace of Recovery Expected to Accelerate
The nation’s nonresidential construction recovery continues, though most indicators suggest that the pace of recovery remains only gradual. That perception of slow and steady progress in reinforced by the latest CONFINDEX survey conducted by the Construction Financial Management Association (Q1:2014).

During the New Year’s initial quarter, the overall index rose 2.4 percent, from a reading of 127 to 130. One year ago, the index stood at 129, which means that the index has expanded by less than one percentage point over the past 12 months. A recovery could scarcely be more gradual.

In fact, the Business Conditions Index was unchanged (127) on a quarterly basis during the first quarter of 2014. The Current Confidence Index actually slipped 0.8 percent from 123 to 122 during the quarter and is only about 1 percent higher than it was a year ago. Weather may have played a part with the Northeast and the Midwest having been hammered by a seemingly endless winter and parts of the West impacted by drought.

The Financial Conditions Index, though rising from 111 to 116 (4.5%) on a quarterly basis, is only up by 0.9 percent over the past year.

Trend Since
Last Reading

THE CONFINDEX™ NUMBER

The readings described above would seem to indicate a stalled U.S. construction recovery. In truth, nonresidential construction spending has not expanded profoundly over the past year, which should come as little surprise given the fact that the national economy expanded less than 2 percent last year. Federal, state and local capital spending remains constrained, which has impacted spending in a variety of categories ranging from public safety to education.

But despite the apparent lack of statistical progress, the first quarter 2014 CONFINDEX survey actually points toward a brighter future. Importantly, the Year-Ahead Outlook Index surged during the first quarter, rising from 132 to 140, a gain of 6.1 percent. Of all the sub-indices, it is this one that reflected the most progress on a quarterly basis.

True, the latest reading is not particularly dissimilar from the year-ago level. CFOs approached with an elevated level of confidence only to be disappointed by the pace of recovery by mid-year. That led to meaningful declines in the Year-Ahead Outlook during prior quarterly survey assessments.

It is of course conceivable that CFOs will once again be disappointed in 2014, but for now there is a level of confidence in near-term dynamics that has rarely been observed in recent years. Among the comments supplied by respondents are “things have definitely improved, but I fear there are still some bumps in the road ahead” and “the flavor of construction seems to be improving.”

The more positive general outlook has impacted forecasts for profit margins. In the latest survey, only 2 percent of respondents revealed an expectation that their profit margins would deteriorate over the coming year. During the prior survey, that proportion was 11 percent. Fully 57 percent of respondents expect their margins to be fatter in one year with another 41 percent anticipating stable margins.

Potential Bumps in the Road
There are many reasons to believe that America’s construction recovery is set to accelerate, including reports of rising backlog and busier architects. But CFOs can largely be characterized as cautiously optimistic in recognition of the fact that there remains hurdles to overcome.

During the most recent quarterly assessment, many CFOs continued to express concern regarding skills shortages. Fully 60 percent of respondents reported worries regarding this form of shortage, by far the most common source of angst. Many also expressed concern regarding the impacts of healthcare reform, an inability to identify enough qualified disadvantaged businesses with whom to partner, and a lack of available public financing.

A growing number of CFOs are at least somewhat unnerved by the potential impact of rising construction materials prices. In the first quarter, 51 percent expressed an expectation that materials prices would rise, though the large majority of this group feel that the impact will be slight as opposed to profound. During the prior quarter, 48 percent of respondents expressed such a concern.

The notion that materials prices will present more of a challenge going forward is an intuitive one. The pace of construction recovery is expected to accelerate. This will lead to more rapid demand growth for materials, which in turn will cause prices to rise all things being equal. But all things are not equal. Recently, certain materials prices have actually been falling, in part because of evidence indicating that the Chinese economy is slowing faster than anticipated. It is possible that CFOs will be collectively and positively surprised by material price dynamics during the months ahead. Of course, it is also possible that outcomes will not be as benign as presently anticipated. Only time will tell.
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) 2014 Outlook – look ahead to June 2014

• 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.