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Bay Area Current Market Conditions – December 2016

We reported back in August of 2016 "The California market has now been in recovery mode for the last six years. All indications reflected a robust market which is firing on all cylinders, with the Bay Area leading the way in California in terms of volume and strength of backlog". There was talk of a bubble in the economy which would have ripple effect on the market if there was a hard or soft landing about to happen.

Since August we have had a General Election with no apparent slowdown in the economic factors driving the construction market. The TBD Bid Index continues to show an overall trend upwards and running ahead of what is considered a norm in construction escalation- currently in the 6-8% per annum depending on the project, location and other factors.

The following paragraph repeats what we iterated a few months back. "General contractors and sub-trades can now be very selective with regards to the work they will pursue, which means more time must be spent to generate interest. Clients should also be aware **that certain project types or locations will carry additional premiums**. In this heated market the public sector (especially Federal Government work), is not going to have the attraction it would have in a down market, so expect to see enhanced escalation in the public sector ".Many contractor order books are full with some refusing to bid any more projects in the short to medium term.

To update and expand on the above we have looked at the differences in Private and Public sectors -

Private sector: The market is now a contractors' market where they can pick and choose the projects that will be of interest, profit margins are up and subtrades willing to submit competitive bids are difficult to find. Most contracts will be CM/GC with the GC brought on early to ensure there will be interest and precontract services commissioned to maintain interest and commitment.

Owners, however, have started to discover that some projects are no longer viable given the increase in construction cost. Rental income for offices in certain areas e.g. Oakland cannot in some instances support the current construction costs. Some of these projects are on indefinite hold.

Public Sector: The tsunami of work has had more profound effect in the public sector. Most of the procurement relies on the hard bid, lump sum method of selecting the low bid from the open bidding process. These projects take a long time in the planning and approval process and lack the flexibility to adjust scope and/or budget to reflect the current bidding market. Based on a predetermined time line these projects are hitting a saturated market with adverse results.
These projects with budgets set in more predictable times will suffer from a lack of competitive and qualified bidders. Estimates, however, typically reflect a reasonable level of anticipated competition in all trades. To reflect the current saturated market we are advising clients to carry a bid contingency to cover for the anticipated lack of competition. (At least for the next 4-6 months)
We have looked at a broad band of public sector projects to advise clients on the percentage market factors and would recommend the following to be added to any estimate. These ranges are broad to cover the various added factors e.g renovation, phasing, schedule, number of alternates, etc., which will have compounding effect on bidding response

1) Projects in the $1m-$5M range
   Recommended Bidding factor 20-50%

2) Projects in the $5m-$10M range
   Recommended Bidding factor 20-30%

3) Projects in the $10m-$20M range
   Recommended Bidding factor 15-25%

4) Projects in the $20m-$50M range
   Recommended Bidding factor 10-15%

We appreciate the duress of recommending to public clients the need to account for above factors. It is, however uncomfortable, a dialogue we need to recommend.