111 Pine Street
Suite 1315
San Francisco
CA 94111

415 981 9430
415 981 9434 fax
info@tbdconsultants.com

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TBD Consultants

California Current Market Conditions – Sept 2020.

Our previous report in June 2020 focused on COVID-19 impact on the construction market and the immediate impact on current ongoing projects. The impact of the stoppages and added safety measures are still being processed and subject to resolution on a project by project basis.

For construction projects are now up and running the picture is muddy based on directions from the state, counties, and cities. These entities often have a different interpretation of emergency regulations.

Privacy rules can prohibit asking if a person has tested positive for the virus, however it is OK to ask if the person has flu like symptoms. Construction has always needed boots on the ground to get work done and there has historically been an attitude for hourly workers to show up even if they are unwell. Clearly that attitude has to change for everyone's wellbeing. An expedited testing system is urgently needed to identify and control the wellbeing on construction sites.

Recapping of where we are in September 2020:

-COVID-19 pandemic and recession have a significant negative impact on construction sector

-Nationwide construction has taken a hit in last five months.

-Construction starts have plummeted.

-All sectors have declined: residential and non-residential:
  Non-residential bore the brunt falling 19%
  Residential only fell 3%

-Consumer confidence and business confidence will be major factors in path of recovery

-Financing has tightened -Access to capital for project financing has gotten tougher in last 6 months

-COVID-19 will create some work as Owners try to reposition and upgrade buildings e.g. Building owners and client organizations are studying what has to be done to make buildings safe. Employer are trying to identify what they have to do to their building to enable their employees to return to their place of work, even for a limited work week.

-It may be early days however certain trends are developing in response to the migration of office worker to working from home. Developers and owners are looking at ways to reposition their typical office buildings e.g. housing from previous office development and renovating office space for life sciences functions.

-The amount of office space on the market has exploded as many employers exit their spaces in favor of downsizing or changing their business models. Expect office lease rates to fall from previous highs.

-In California, the current fires have already destroyed hundreds of buildings with no end in sight. Reconstruction will again stimulate the housing market and other construction sectors.

Market Indicators

-Market optimism: Latest ENR Construction Industry Confidence Index dropped 20 points to 36. (any reading less than 50 is negative) This is the lowest it has been for a decade. Retail and hospitality sectors ratings have fallen more than other sectors.

-Historically, Bay area is typically one of the last areas to experience a recession and one of the first to recover.

-Material pricing for common items e.g. steel and lumber- expect prices to be flat for the next year or may drop slightly due to falling demand.

-Worker shortages no longer a concern.

-Salary freeze ongoing for most supervisory and management staff in construction firms.

-Majority of California General contractors and subcontractors have enough backlog to last 15-18 months.

Escalation

For the last eight years in Bay area escalation across all construction sectors has averaged approx. 7% per annum.

For the last 8 months (though August 2020) escalation has been flat.
COVID-19 has added costs due to productivity losses and safety measure however there is more interest from sub-contractors and more competition in the trades to secure work. These competing factors tend to cancel each other in the current market.

We expect escalation to be flat for next 18 months. Thereafter we expect to see modest escalation in the region of 3.5%-4.5% for the following two years.

In Summary we would recommend the following escalation factors:

Year	Escalation
2020	**0%**
2021	**1%**
2022	**3.5%**
2023	**4.5%**
2024	**5.0%**