



THE BROAD DIMENSION

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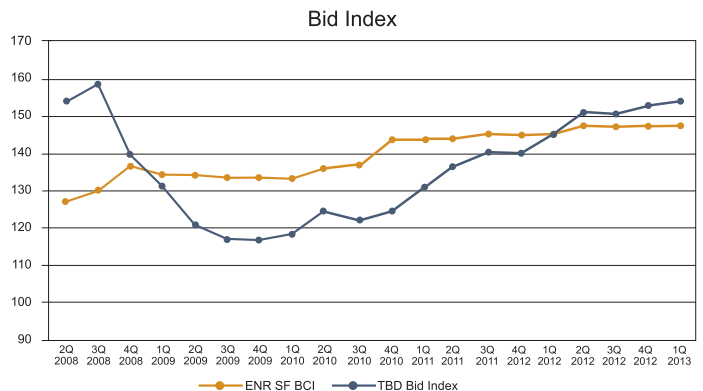
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Bay Area Market Report

Towards the end of last year, our San Francisco office conducted a survey in which eight local contractors participated, and the following is a summary of the findings.

Market Sector Overview, Reflection & Future Predictions

The commercial market had strengthened in 2012 as the demand for office space resulted in increased rental rates for San Francisco and the South Bay. Tenant Improvements and New Office construction projects are also reappearing after a hiatus. Healthcare continues to be a strong market with many renovation and new build projects being planned, designed or bid out.



Biotech and Advanced Technology have been strong sectors and show no sign of slowing down which reflects the Bay Area's renowned resilience in these markets. Large scale projects such as the Transbay Transit Center, Central Subway and the 49ers Stadium have now really started to move forward and the bidding of associated trade packages has been encouraging for subcontractors. Despite funding problems in the education sector, it still remains an area where many GC's feel optimistic and are planning to target throughout 2013.

Other mega projects such as the Apple Headquarters, Warriors Stadium, California Pacific Medical Center and the Moscone Center Expansion are on the horizon which

should mean there will be more for the industry to cheer about in the forthcoming year. However, the last four years have taught us not to take anything for granted. The housing market in the City has finally shown signs of life and looks like it will continue to be positive at least for the short term. Funding from the private sector is becoming available again based on projected growth within the Bay Area's thriving Biotech and Advanced Technology industries, among others. Many young professionals appear to be arriving in the city which has resulted in a rapid increase in residential rental rates.



Market Competition & Bidding

Most General Contractors report they are receiving reasonable bid coverage for sub-trades and are again able to include a profit margin in their bids. It appears the days of taking work at minimal profit to maintain cash flow and keep staff occupied are ending for most of the quality contractors. All GC's reported a steady increase in pricing they received from sub trades this year. Some warning flags have been raised regarding MEP trades, where volatility and high bids have arisen, with some indicating fears over shortage of workers and qualified subs to fulfill the order books.

Public & Private Funding

In the public sector funding remains a challenge that is not likely to go away soon. Although agencies are continuing

to move their projects through the planning process, the jump from paper to shovel still appears to be too long. The private sector has provided much needed work for many medium to small sized General Contractors. Traditionally buoyant Bay Area markets, including Biotech, Healthcare and Advanced Technology, will continue to provide steady growth. Property Developers who have been sitting out the recent recession have started to return to the market as they have seen vacancy rates decline.

Escalation

Generally speaking we expect labor and material escalation to move into the range of 3-5% over the next 2-4 years. On larger projects with more risk and fewer qualified bidders we would expect market forces to drive that higher as contractors and subcontractors start to take higher markups.

Delivery methods

The larger private sector projects have been trending towards CM/GC with the General Contractor coming onboard to provide preconstruction services. Other GC's considering larger public sector projects are investigating other delivery methods such as Integrated Project Delivery (IPD) and whilst many have not necessarily put that label on it, they have admitted that IPD qualities have been present in their recent delivery methods.

Other Trends

It has been reported that the MEP and Exterior Envelope trades are being considered more for the use of the Design / Build delivery method. Furthermore, some of these trades face an approaching labor shortage as a significant portion of their skilled workers near retirement age at the same time when fewer recruits are being attracted to the industry to replace them. This situation will only be exacerbated if and when the market fully turns around and they become in higher demand.

Design-Build – Pros & Cons

Sometimes it is assumed that Design-Build is a relatively new concept, but it has been said that it can be dated back to the medieval master builders, like Henry de Reyns who built Westminster Abbey in London.



The basic precept behind Design-Build is in having a single point of responsibility for both design and construction. One intention is that supposedly this will eliminate the inherent conflicts between designer and contractor, reducing litigation and claims. Normally the Design-Build (D/B) entity is not one united entity, but rather a joint venture, almost always led by the contractor because they have the bonding capacity. So the possibility of litigation between designer and contractor is not eliminated, but at least the building owner isn't in between them.

There is also normally an expectation that D/B will result in breaking ground on a construction project faster than the traditional route of design, bid, build. It is also expected that the construction period itself can be tightened to result in completion on or ahead of a typical schedule, since the contractor is often involved from very early in the planning, in answering his or her own design questions, and can ensure that efficiency and constructability are central to the design. This can often be the main driver for employing the D/B procurement strategy, with modern times dictating that 'time is money'.

Another anticipated benefit is that constructability and value engineering ideas that the contractor can bring to the design will lead to more competitive prices.

It is well known that the three goals of any construction project are schedule, cost and quality, and there is a consensus that you can have any two of those but not all three. Consequently, since we are saying that schedule and cost are anticipated benefits of the D/B process, it should not be surprising to find that there are concerns about quality control and lack of design excellence. There

is also concern about the loss of unbiased professional advice. However, you only have to think back to the idea of the medieval master builders as Design-Builders to see that architectural excellence is not always a problem with this procurement method. Having the D/B builder utilize its own expertise and innovative skills can lead to interesting designs. But the concern about design quality is one reason why MEP disciplines and industrial projects are often seen as ideal subjects for this method.

Another potential problem that has been noted in connection with Design-Build is interpretation of the performance specification by the D/B builder to his advantage, rather than to that of the building owner. Design may be non-existent at the time the project goes out to bid, or the design may have been completed up to a certain stage, often about 50% or 60% complete. In the former case, the performance specification is the only document that really defines what the building owner expects, and it needs to be very well worded. In the latter case, you can sometimes lose a substantial amount of the potential benefits from D/B, since large parts of the design are already fixed, and potential innovations affecting that design could be costly in design work and affect the schedule, unless there is enough flexibility carefully crafted into the original design to eliminate this danger.

Another potential issue that arises in connection with bidding a project on performance specification only, is that the cost of bidding such projects can tend to reduce the number of qualified bidders.

Traditionally, the public sector has had more reservations about Design-Build because of the difficulty of demonstrating that they are achieving the 'best buy'. It might not always be apparent, but public bodies do have a responsibility for how they are spending taxpayers' money, and the more traditional method of bidding out a fully designed project is often seen to be less subjective than the Design-Build process.

So the Design-Build procurement method has its pluses and minuses, as does every other procurement method, and building owners will need to evaluate the procurement strategy for each project.

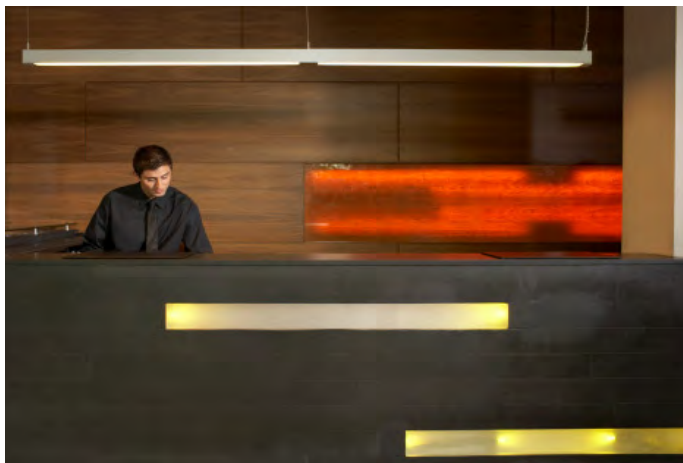
Brian Tolland and Jamie Milliner of TBD Consultants contributed to this article.

Hotel Design Issues

Unlike office or housing developments, where the occupants sign up for the medium or long term, hotels have a constantly changing list of guests, all of which would normally have a range of hotels to choose from. This puts hotels into a higher risk category, and means they have more incentive to be efficient, while maintaining the feel and ambiance of the place. Hotels are very cost-sensitive, because they are one of the harder types of building to make work financially.

Hotel guests select a hotel based on a number of criteria, including price, convenience, atmosphere, service, and amenities. Keeping the price competitive while providing for those other criteria is the challenge for the design team.

Hotel lobbies used to be grand, high volume spaces, and this has been an area that has been made a lot more efficient. While the size of main entrance lobbies has been coming down, the quality of finishes has not – after all, this is the guest's first impression of the place. But the space that remains is often utilized for dining areas and other functions, as well as the more traditional check-in/check-out facilities.



The guest rooms constitute the largest part of any hotel, and these need to serve multiple functions, as bedrooms, offices, and relaxation areas. Maintaining the appearance of traditional elegance, while also allowing the room to function efficiently for the traveling businessman, is another challenge that designers have to meet. The guest room block will also contain corridors, stairs, elevators, vending area, linen closet and other storage. The area of

actual guest rooms to total guest room block, can range from about 75% for a very efficient hotel, down to around 60%, with about 66% being a common figure.



Restaurants tend to not be money makers for hotels, so fewer hotels these days have multiple restaurants, instead having maybe one restaurant and a coffee/donut facility (often the ubiquitous Starbucks).

Meeting rooms are designed for efficiency and flexibility, allowing their use for multiple types and sizes of functions, and thus increasing revenue.

Hotels are not immune to the cycles that affect investments, and sometimes building new will be more cost effective, and at other times purchasing an existing building and renovating it will prove to be the better option. But renovation work in an existing functioning hotel always faces the problem of minimizing noise and inconvenience for the hotel guests.

The cost of hotel buildings is often stated as a cost per room, or as a cost per square foot of overall floor area. The former option is more variable, due mainly to the extent of meeting rooms, size of fitness center facilities, etc. Other issues that create variations, whether you are dealing with cost/room or cost/SF, include the extent of balconies, whether underground parking is required, the type of mechanical systems and extent of landscaping.

Of course, hotels come in a range of types and ratings, and may be part of a chain of hotels. Some hotel chains have made use of a standard design that gets adapted as necessary for each location, but hotels in the higher price range still tend to be one-offs.