



Board Report

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CONSTRUCTION COMMITTEE SEPTEMBER 15, 2022

SUBJECT: LOS ANGELES CONSTRUCTION MARKET ANALYSIS- 2022 UPDATE

ACTION: RECEIVE AND FILE

RECOMMENDATION

RECEIVE AND FILE the Los Angeles Construction Market Analysis 2022 Update.

ISSUE

Since the passage of Measure M, the construction industry has experienced significant challenges related to the cost and availability of labor and materials. The COVID-19 pandemic has exacerbated these issues, creating extreme volatility and implications regarding Metro's ability to deliver an ambitious capital program.

BACKGROUND

In August 2021, Metro published the 2021 Construction Market Analysis. Since the 2021 report, Metro staff have regularly presented construction market updates on inflation, material prices, bid prices, labor and employment, outlook, and trends. This status report provides updates on the construction market through the second quarter of calendar year 2022.

DISCUSSION

Inflation - Based on the latest U.S. Department of Labor's Bureau of Labor Statistics (BLS), inflation has climbed to 9.1% compared to a year ago. This is the highest inflation rate in the last 40 years. In previous updates, construction inflation has increased at a faster rate than consumer inflation, but now consumer inflation has caught up with the pace of construction inflation nationally. However, construction inflation in California (based on ENR's Building Cost Index for Los Angeles and San Francisco) is still trending higher than both national consumer and construction inflation

Materials Prices - While material prices have had wild swings over the past year, such as steel and lumber, most construction materials are beginning to stabilize. For example, steel, aluminum and copper/brass, products have all decreased in the past month. On the other hand, diesel fuel has skyrocketed over 100% within the past year due to increased demand and Russia's invasion of

Ukraine.

Nevertheless, construction materials are still expected to see volatility and supply-chain issues over the next few months, but prices are not anticipated to have long-term increases. With high interest rates and a potential recession looming, prices will likely experience a downswing for most construction material prices in 2023, according to Engineering News-Record 2022 Second Quarterly Cost Report.

Bid Prices and Construction Costs - Both nonresidential construction inputs (the cost of construction) and producer price index (bid prices) from BLS have continued in an upward trend this past quarter. Within the past year, the cost of construction has increased by 16%, primarily due to the volatility in material prices. Similarly, bid prices rose 18% over the past year to compensate for the volatility. Bid prices will likely remain high as the construction industry has been competitive in labor compensation to attract and retain skilled labor workers.

Labor and Employment. - Construction labor rates are increasing due to a 50% drop in construction unemployment over the past year from 7.5% in 2021 to 3.7% in 2022. According to the Association of General Contractors, the construction industry's 3.7% unemployment rate is at its lowest point in the data's 23-year history. The demand for construction is outpacing the supply of workers. The number of construction-industry job openings at the end of May 2022 was 466,000, a 39% increase from the previous month. Yet, the number of unemployed construction workers looking for work is down 47% from last year, suggesting there are very few experienced job seekers in the construction industry.

Outlook and Trends - There are positive signs, with a 6% increase in construction starts in the past year and a 13% jump in heavy civil construction within the past month. The Infrastructure Investment and Jobs Act is also growing the pipeline of projects as bellwether indicators, such as the Dodge Momentum Index, forecast strong future construction demand.

Concerns over high interest rates and a potential recession could temper this and reduce the demand for construction. The dwindling number of skilled workers also continues to plague the construction industry. In industry surveys, contractors also forecast a declining market through the end of 2023.

With mixed market signals, the construction industry is at a crossroads and facing many uncertainties in the broader U.S economy. Despite this, the construction industry continues to be a "contractors" market for the time being. This will depend on the Federal Reserve's response to inflation and interest rate, and the level of economic impact from any future waves of COVID-19 variants.

EQUITY PLATFORM

The proposed action is a receive and file update to the Los Angeles Market Construction Analysis 2022 update. The analysis aims to highlight the factors influencing construction bid prices and Metro's ability to deliver the transportation construction program. As part of the original analysis, there was a review of the economic impacts, especially from the pandemic, and found it has manifested differently across workers, businesses, and industries, with small businesses in nonessential industries experiencing the most economic distress, and women and minorities being

disproportionally affected. With mixed market signals, the construction industry is facing uncertainties in the broader U.S economy and in the wake of the COVID-19 pandemic. Metro's project labor agreement, construction careers and local hire policies are important to mitigate the impacts to marginalized communities. These policies assist equity focus communities and offer career opportunities through apprenticeships and pre-apprenticeships.

IMPLEMENTATION OF STRATEGIC PLAN GOALS

The recommendation supports Strategic Plan Goal #1 - Provide high-quality mobility options that enable people to spend less time traveling. This will be accomplished by planning and delivering multiple capital projects on time and on budget.

NEXT STEPS


Metro's Program Management department will continue monitoring market conditions, construction trends, and bid results to help produce realistic project budgets and cost estimates that align with the construction industry.

ATTACHMENTS

Attachment A - Metro Construction Market Analysis 2022 Update

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CONSTRUCTION MARKET ANALYSIS



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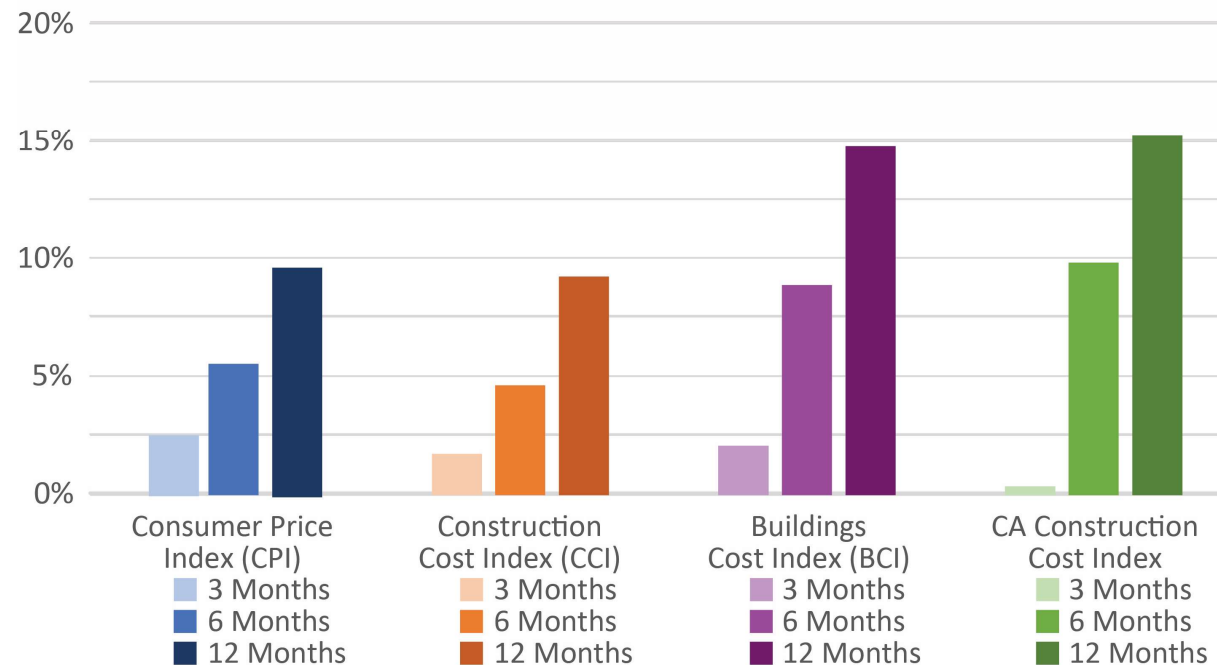
September Update

2022

CONSUMER INFLATION CATCHES UP TO CONSTRUCTION

- Inflation climbs to 9.1% compared to a year ago (highest in 40 years)
- Consumer inflation is generally rising at the same pace as construction inflation
- California construction inflation still much higher than the national average, but has plateaued over the past three months

Percent Change in Past 3-Months, 6-Months, & 12-Months by Index



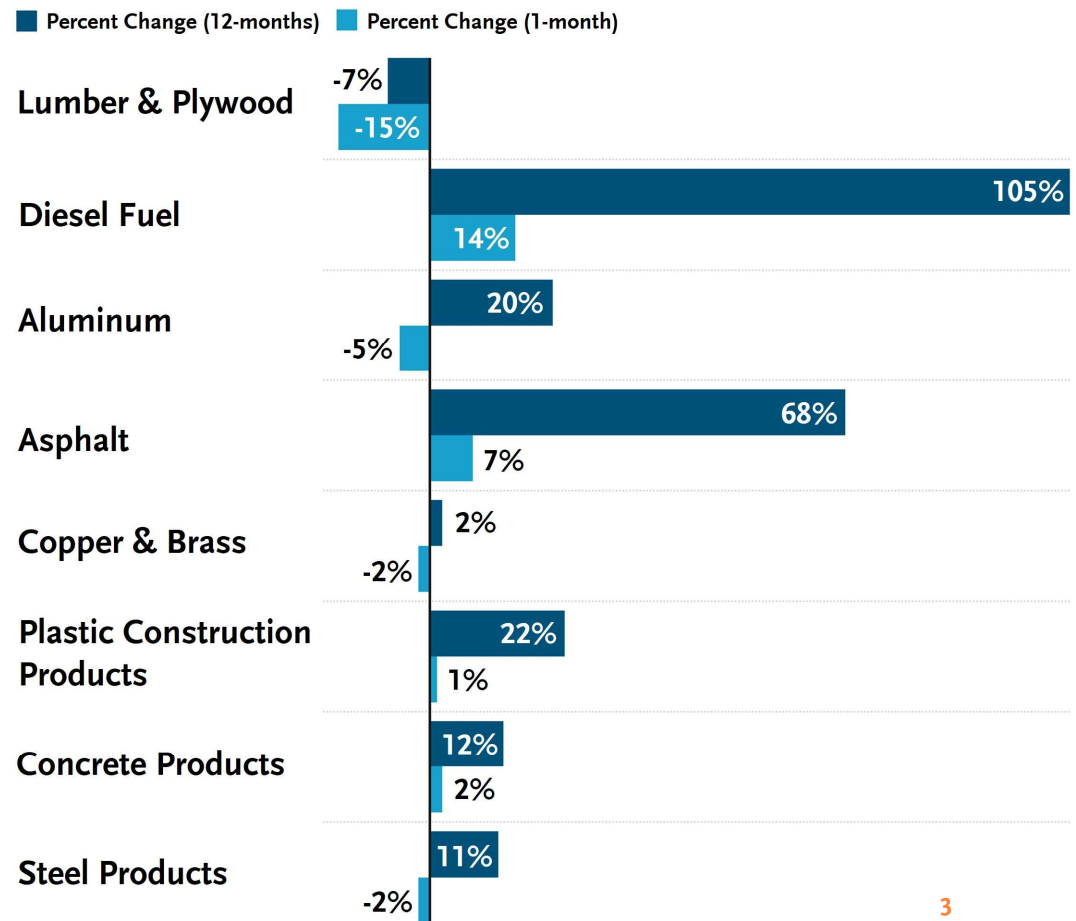
Sources: Bureau of Labor Statistics, Engineering News Record, California Department of General Services

MATERIAL PRICES ARE COOLING EXCEPT FOR DIESEL

- Material prices stabilizing following extreme COVID volatility, with exception of diesel fuel
- Volatility and supply-chain issues are still expected through summer
- High interest rates and potential recession suggest potential drops in material prices
- Lumber and steel appear to be trending down according to ENR's 2022 Second Quarterly Cost Report



Construction Materials Cost: Percent Change

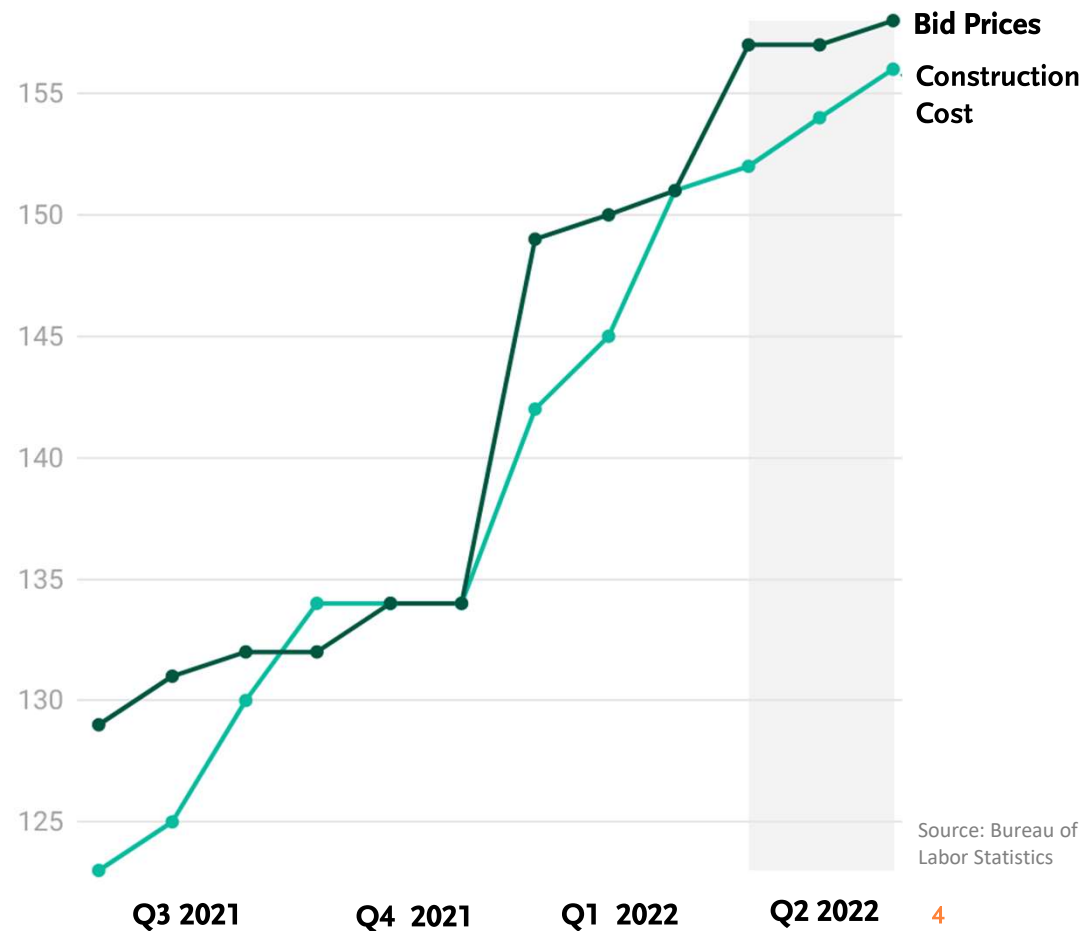


Source: Bureau of Labor Statistics

CONSTRUCTION COSTS & BID PRICES CONTINUE TO RISE

- Increases over the past 6 months:
 - **10%** in construction costs
 - **6%** in bid prices
- Increases over the past 12 months:
 - **16%** in construction costs
 - **18%** in bid prices
- Bid prices have jumped to compensate for volatility in material prices over the past year
- Bid prices likely to remain high due to competitive worker compensation to attract and retain skilled labor

Construction Costs vs Bid Prices



Source: Bureau of Labor Statistics

EMPLOYMENT DEMAND STILL GREATER THAN SUPPLY

- 2021: **7.5%** construction unemployment rate
- 2022: **3.7%** construction unemployment rate
- Demand for projects is outpacing the supply of workers
 - **466,000** construction-industry job openings at the end of May (largest May total since 2000)
 - Number of unemployed construction workers is down **47%** from last year, suggesting there are very few experienced jobseekers looking for work
- Average salary increases for construction workers are on pace to exceed **5%** this year



BY THE NUMBERS

50% drop in construction unemployment over the past 12 months

39% increase in construction job openings in the past month

64% of contractors say the labor shortage is worse than a year ago

23 year low in construction unemployment

MID-YEAR CONSTRUCTION MARKET SUMMARY

- **Industry Market Outlook:** Construction market at a crossroads
 - Construction starts up by 6% compared to last year
 - Bellwether indicators forecast strong future construction demand
 - May be tempered by interest rates and potential recession
 - Contractors see declining market through the end of 2023
- **Material Price Trends:** Tightening financial markets, slower growth, and continued improvement of supply chain may cool material prices
- **Labor Trends:** Skilled labor shortages will continue to plague productivity causing project delays
- **Local Construction Indicator:** Los Angeles currently has 51 cranes, most in North America (Seattle is next with 37)