

Construction Industry Market Report

Fourth Quarter Update 2009

CONSTRUCTION INDUSTRY MARKET REPORT 2009 - FOURTH QUARTER UPDATE

Overview of the Current Construction Market

While much of the economy started to show signs of improvement, the construction sector continued to struggle in the fourth quarter of 2009. At best, it appears that the rate of decline is decreasing in most markets, particularly in the hardest hit states. Only one state, North Dakota, is showing any growth, and that is a weak 1.7% annualized. Arizona and Nevada continue to be the most severely impacted markets, with declines of around 25% annualized, both having shed over 40% of their peak construction work force of 2006.

Altogether a total of nearly 1.9 million construction jobs have been lost since the peak monthly employment in the summer of 2006, and over 1.7 million on a seasonally adjusted basis. Total construction spending for 2009 is down sharply, with an annualized estimate of roughly \$948bn, some \$124bn below 2008. Year to date spending through November 2009 is \$126bn less than year to date in November 2008¹. While the structural economic fears that were present in the fourth quarter of 2008 have now largely abated, it is clear that the construction markets remain extremely weak, and there is little prospect of a return to growth in any region or sector for some time to come.

The rapid reduction in activity has created a large negative output gap in construction. The output gap is the difference between actual activity and potential activity. Following an unprecedented twenty year period of stability in construction and core inflation, in the past five years, the construction market has experienced very large shifts in the output gap, with a significant positive gap (excess demand) in the years 2004 to 2007, followed by a significant negative gap (excess capacity) in the years 2008 and 2009.

Percentage Change in Construction Employment
from December 2008 to 2009



¹ US Census Bureau

The output gap for construction is significantly larger than that for the broader economy. The Congressional Budget Office estimates the broader economic output gap in the United States at 7%². While output gap figures are not published for the construction sectors, current data shows activity is currently running 14% below this time last year, and almost 25% below the peak of 2006³. Even though some of this capacity has been permanently lost to other sectors, it is reasonable to set the gap at around 15% to 20%. This contrasts with an annual growth rate of around 4% - 5% through the years 2004 to 2006, which represents an effective positive output gap of around 3% for the sector.

The large negative output gap is leading to greatly increased competition among bidders and putting pricing pressure on projects. In most areas cost trends continue to be sharply negative, leading to moderate to strong construction price deflation.

The American Recovery and Reinvestment Act (ARRA) is working its way through the economy, but, while it has been successful in providing a substantial number of construction jobs, it is not sufficient to create overall growth in construction activity. As of the end of October, about \$159bn has actually been paid out from the entire package⁴.

² The Budget and Economic Outlook: An Update: Congressional Budget Office, August 2009.
<http://www.cbo.gov/ftpdocs/105xx/doc10521/08-25-BudgetUpdate.pdf>

³ Bureau of Labor Statistics

⁴ <http://recovery.gov>

MARKET OUTLOOK

As the signs of a recovery grow, the questions now turn to the nature of the recovery and the likely shape of the post-recovery economy. The broad consensus on the direction of the global economy over the next two years is that, while the recession is largely over, the recovery is likely to be very slow, particularly in the Advanced Economies (United States, Euro area, Japan, UK, Newly Industrialized Asian Economies)⁵. Published forecasts for the anticipated growth for these economies are in the range of 1.5% to 2.5% per annum⁶. Developing economies, by contrast, are expected to grow at a rate of around 6% to 8%, with the bulk of that growth being provided by China and India. Excluding those two nations, the growth is expected to be around 2.5% to 4%. While these rates appear relatively strong, they are significantly weaker than the years prior to the recession.

Throughout the world, the output gap is expected to be negative in the short term, indicating that actual economic activity will remain below the economic capacity. The gap is most pronounced in the Advanced Economies; for China and India, the gap is much smaller. Forecasts generally show the gap being eliminated in Emerging Economies by 2011, while it persists in the Advanced Economies into 2012 or 2013. In all scenarios, the median projection is for the output gap remaining very close to zero after recovery in all major economies, indicating little, if any, overheating of the global economy in the short term. There is the strong possibility of speculative asset bubbles forming, and of transient, localized positive output gaps as idled supply capacity is brought back into production.

Commodity prices are showing some recovery from the lows of 2009, and production activity is increasing. For example, US steel capacity utilization has increased from 41% to 65% in the past year⁷. China's steel capacity utilization has risen to 75%, 2% less than global capacity utilization⁸. Most other commodities have similar levels of idled capacity which is likely to return to production as demand increases. Prices have recovered from the lows of mid-2009, and returned to the price levels prevailing at the end of 2008, but prices are still roughly half of their peak in 2007/8. Despite headlines showing sharp commodity price increases, the data do not support an expectation of significant price rises in the next two years, except for possible transient spikes in prices due to inelasticity of supply re-engagement.

Overall, the weak recovery, coupled with the depth of the recession around the world, means that there should be significant residual capacity in most construction and commodity markets. Even with the attrition and elimination of capacity in these markets, it is likely that global growth in 2010 and 2011 will not put significant upward pressure on prices.

For the United States, not only is the recovery likely to be weak, but also the post-recovery economy is likely to be markedly different from the one preceding it. Balancing currency value, interest rates, and economic stimulus, as well as demand for new programs such as health care, will be very challenging, and there is a strong probability that growth will be attenuated for several years as the economy reflects the new global realities.

The weakness of the recovery will have a significant impact on providers of design and construction services. Many have maintained a presence in the market due to momentum from the pre-recession period. As projects wind down, the stress on their working capital will be severe. Having capacity to grow into the recovery will demand robust working capital, and many firms may have survived the recession, only to fade in the recovery. We may be entering the period of greatest risk of failure of firms in both the design and construction sectors of the economy, which will have an impact on the later stages of the recovery. For construction firms in particular, but also to some extent for design and management firms, the barriers to entry are quite high, both due to the need for financial strength in the form of capital or bonding capacity, and due to the need for a demonstrated track record for most project types. It could be that when the recovery finally hits its stride, the capacity will simply not be there.

⁵ Definition from International Monetary Fund

⁶ The Global Outlook in Summary, 2007-2011: The World Bank: <http://web.worldbank.org/external/default/main?theSitePK=659149&pagePK=2470434&contentMDK=20370107&menuPK=659160&ipK=2470429>

World Economic Outlook, October 2009: International Monetary Fund
<http://www.imf.org/external/pubs/ft/weo/2009/02/pdf/text.pdf>

⁷ This Week's Raw Steel Production: American Iron and Steel Institute: December 2009. http://www.steel.org/AM/Template.cfm?Section=Raw_Steel_Production1&CONTENTID=29318&TEMPLATE=/CM/HTMLDisplay.cfm

⁸ China's Steel Capacity Utilization Rate Lower Than Global Average: China Mining: Dec 2009. <http://www.cnmining.org/cnmining/news?id=4980>

US CONSTRUCTION ESCALATION OUTLOOK

While the broader economy appears to be emerging from the depths of the recession, there are no signs that there is any momentum building towards a recovery in demand for construction. Demand for new construction in the commercial and residential sectors is very low; many areas remain overbuilt, and it will take quite some time for the excess to be absorbed. Institutional and governmental agencies are beginning to explore new projects, or re-open current projects, but the level of activity is still well below that of the past few years, and there is the strong likelihood of reduced public sector spending as all levels of government reduce expenditures to draw down on deficits and balance budgets. Even with the inevitable attrition as bidders and suppliers succumb to the effects of the prolonged recession, there are no indications of strong demand growth, and the negative output gap is likely to persist over the next two to three years.

Construction materials, particularly commodities and raw materials, are showing signs of cost growth. Processed materials and fabricated elements are currently more stable. Overall, the Davis Langdon materials index has increased by around 2.3% since the low of May 2009, although it is still 11% below its peak in 2008, and very close to levels seen in 2006 and 2007. Much of the cost growth is being driven by markets outside the construction sector, and to a large degree by markets outside the United States. This pressure is likely to be moderate in most cases, even though there will be appreciable fluctuation with transient highs and lows as supply and demand imbalances work their way through the markets, and as market reactivity plays out.

Even with inflationary pressure from commodities, however, weak demand may not allow bidders to recover the full impact of price variations. Many will have to absorb the risks in order to be able to compete for projects. While this can create lower cost at award, it increases the risk of higher total project costs at completion due to the potential for contractor failure, increased claims activity or correction of construction defects and quality shortcomings. Nevertheless, construction inflation is likely to remain low for the coming year, with the negative output gap being by far the dominant factor in pricing.

In addition, there is a good likelihood that any recovery will experience significant dips in confidence and demand. This means that there will be a very uneven response in the construction market, with periods of relative optimism and pessimism. Construction demand and bids for construction projects are likely to be reactive to swings in the mood of the market, leading to the potential for sharp shifts in escalation.

Overall, escalation is likely to remain low for the next two years, despite pressure from input costs. While bid prices are unlikely to fall further, there is little opportunity for growth greater than 2% to 3% per annum, and many markets will remain around 0% for 2010. The pace of increase may pick up in 2011, but the output gap will still dominate, and price rises are unlikely to exceed 3% to 4%.

In the longer term, escalation could return as the output gap is absorbed in 2012 and beyond. The range of possible scenarios is very wide, from a robust recovery leading to a return to positive output gaps, particularly in the stronger regions and sectors, to a prolonged period of stagnation.

ESCALATION RISK

Escalation in the past five years has been much more volatile than at any point in the past thirty years. Even in the high inflation period of the early 1980s, escalation trends were much more stable. The rate of change of escalation, and the variation between market sectors and regions has been far higher than in recent experience. The indications are that the coming five years will exhibit similar levels of volatility. Synchronicity in the global economy and transient imbalances in supply and demand will create marked fluctuations in cost, particularly at a global commodity level.

The period of greatest uncertainty in inflation is 2012 to 2014, where much depends on the speed and strength of the recovery, both locally and globally. The range of possible escalation scenarios is significantly greater than has been experienced in recent markets, both in the escalation rate and the speed of change in escalation. For this reason, planning for uncertainty is more important than planning to a specific escalation target. This involves developing strategies for accommodating both lower and higher than expected rates of escalation. These could include alternates and set based design, owner managed contingencies, active monitoring of market changes, and open communication among project and user team members.

It is also important to manage escalation through the construction period, as well as through the design period, particularly for large or long term projects. If bidders are concerned about the possibility of cost increases, or even cost fluctuations, during construction, they are likely to increase their bids to cover the risk. This is particularly noticeable in fixed price contracts. As the global economy resolves the current recession over the next five to ten years, there is a significant probability of a return to the very volatile markets in commodities and raw materials seen in recent years. There is also the possibility of strong localized demand for construction work as investment returns to real estate and market capacity seeks to respond. This means that bidders on long term projects face significant price risks during construction.

In the current market, the lowest first cost will be obtained by some form of competitive bidding. This approach, however, carries with it appreciable risks related to quality of construction and costs associated with change orders, and, increasingly, contractor/subcontractor insolvency. These risks are often greater in highly competitive markets, where bidders may have reduced margins sharply in order to secure the work, and are in a weaker position as a result. Change orders are also more likely on remodel work, where the complexity and site conditions are more difficult to capture in the final bid documents. In competitive bidding there is less opportunity for bidders to explore and understand these conditions, and hence more likelihood of post-award changes. If the scope can be adequately defined, however, the cost risk on competitive bidding is likely to be less than the benefit accruing from the lower initial price. For highly specialized trades, or ones with limited market capacity, sole source or negotiated bid will still have an overall price advantage.

Going forward, it would be more cost efficient to introduce some form of inflation management to bid projects, either through fluctuation clauses or cost reimbursement. It would also be desirable to use integrated forms of design and procurement, such that project teams can respond quickly to changing market conditions, and can incorporate alternate materials, methods or design approaches seamlessly into the project.

DIRECT COSTS

Input costs include the direct costs of materials and labor, together with the contractor overhead costs. Materials and labor make up the majority of the cost, contributing between 80% and 90% of the construction inputs. Overhead costs vary, depending on the procurement method and the contract requirements for site establishment. In the current market, input costs are not the key driver of construction cost escalation, although they do influence it. In many instances, direct costs are used as a rationalization for cost rises that are truly attributable to market factors. This was particularly the case in the escalation experienced from 2004 to 2007, where overall escalation was significantly higher than the escalation in direct costs.

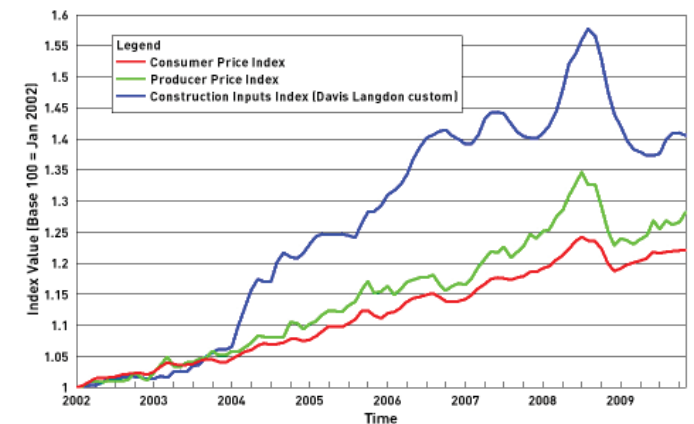
Direct costs can influence escalation in three main ways:

- *Direct impact.* When costs change, bidders will seek to recover the change in cost. This is only possible to the extent that the market will allow it. In weak markets, bidders may not be able to recover the full effect of price increases; in strong markets they may well be able to go beyond the price increase.
- *Perception impact.* In many cases, the news of a price change, or even the news of a potential price change, can alter the market willingness to pay for construction inputs. This was most noticeable after Hurricane Katrina, where there were high profile news stories of impending material and labor shortages and price increases. Most of these did not materialize, but in many respects the news alone served to act as an economic lubricant to escalation.
- *Risk impact.* Since most construction procurement leaves construction period cost risk with the contractor, bidders are vulnerable to input cost changes. During the past five years, input cost changes have been both rapid and large, leading, in some cases, to contractor failure. This volatility creates asymmetrical risk for bidders. Rapid increases in cost will lead to failure, whereas rapid falls in cost will simply create excess profit. Bidders are therefore more likely to hedge to the higher end of the range of potential costs, rather than to the most likely. This is particularly true for larger or longer term contracts, or for those more heavily concentrated in one or two key inputs.

Materials

Materials range from commodities to fabricated elements. Of these, commodities and raw materials (such as oil products, asphalt, concrete, steel, copper, etc.) are the most volatile, since they are generally traded in open markets, and are highly reactive to global supply and demand, currency fluctuations, and even, to some degree, speculative trading. Processed materials and fabricated elements tend to be less volatile, and thus their price changes tend to lag behind changes in commodity or raw material prices.

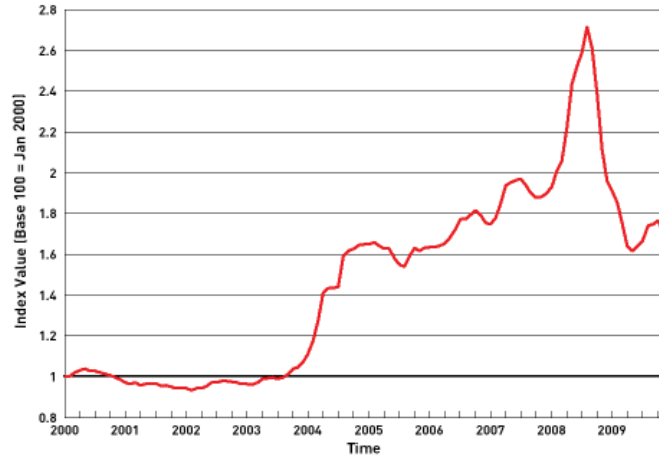
Comparison of Construction Inputs
to Published PPI and CPI



Data compiled from Bureau of Labor Statistics (<http://www.bls.gov>)

The direct cost of construction materials has seen significant fluctuation over the past two years. At the macro level, the major indexes all show a peak in 2008, followed by a sharp fall, then the start of a modest recovery. Looking at individual materials, however, there are a wide variety of profiles, from steel which has a sharp single peak, to softwood lumber which has been falling steadily from a peak in 2004, and ready-mix concrete which has continued to grow throughout the recession.

STEEL



Data compiled from Bureau of Labor Statistics (<http://www.bls.gov>)

ASPHALT



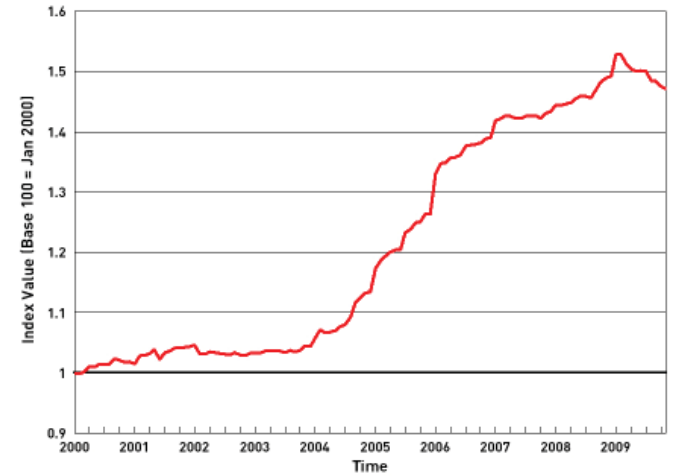
Data compiled from CA DOT
(http://www.dot.ca.gov/hq/vsc/oe/asphalt_index/astable.html)

SOFTWOOD LUMBER



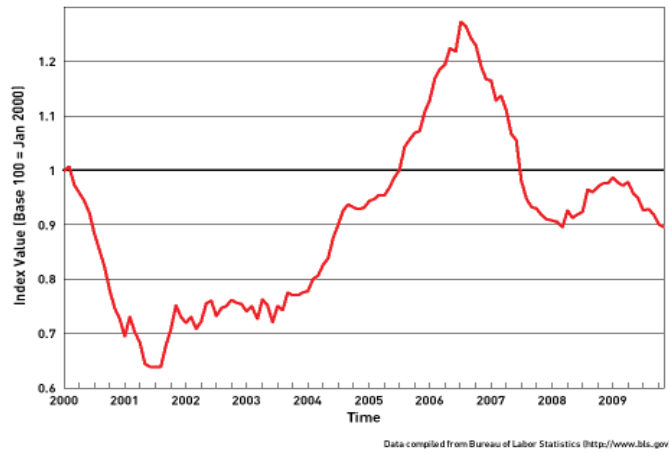
Data compiled from Bureau of Labor Statistics (<http://www.bls.gov>)

READY-MIX CONCRETE

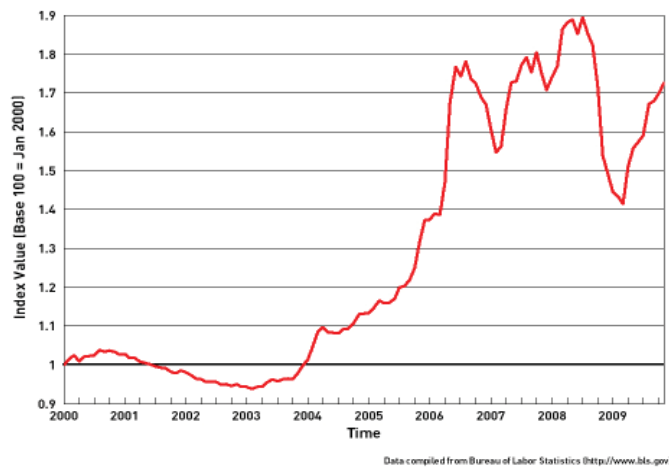


Data compiled from Bureau of Labor Statistics (<http://www.bls.gov>)

GYPSUM PRODUCTS



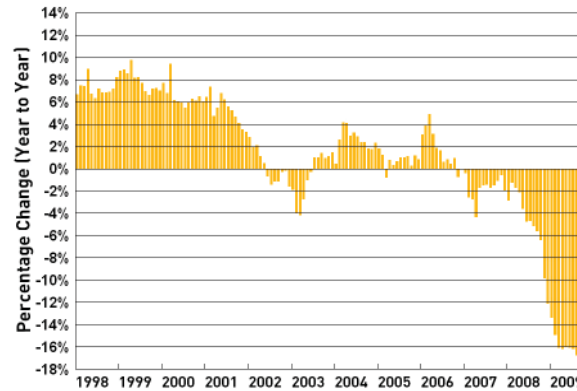
COPPER WIRING



Labor

Labor costs are showing some decreases, due mainly to informal concessions at a project level. Labor agreements are not showing a formalization of the decreases, although there have been some contract concessions in some cases. It is unlikely that new contracts will show significant labor cost reductions, but the rate of increase may well be lower than would otherwise have been expected.

Region 1. Construction Employment Percent Change



**Region 1.
Connecticut, Maine,
Massachusetts, New
Hampshire, Rhode Island,
Vermont⁹**

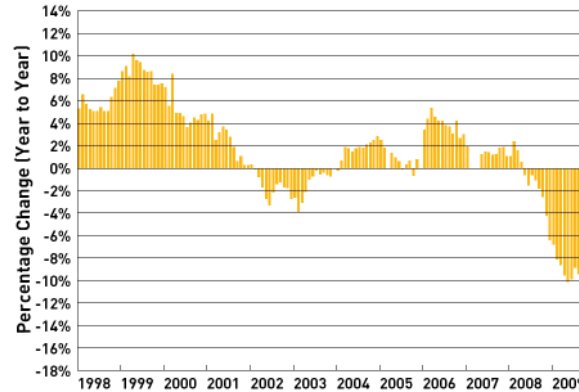
Region 1 as a whole has been severely impacted by the recession, and all states in the region continue to express double digit declines in construction employment. For most, however, this decline is less than that seen in previous months, indicating that some of the states in the region have begun to show signs of stabilization. Despite these faint signs of improvement, however, the region remains the third hardest hit in the country.

The current overall economic picture in the region is generally poor. There is weak job growth and a limited prospect for growth in demand for construction services in the short term. Connecticut is highly dependent on residential construction serving the New York region, and it is likely to be several years before this demand returns. In the longer term, however, the region does have the potential for stable market growth with strong regional economic drivers, particularly in the southern portion of the region.

For construction costs, the construction output gap is likely to be the dominant factor, at least in the short term, with inflation remaining low. As the gap narrows in the medium term, cost push will begin to be evident. It is unlikely that demand led inflation will become a significant factor within the next five years, but it is possible.

⁹ Data in all regional graphs in this report are from US Bureau of Labor Statistics (<http://www.bls.gov/>)

Region 2. Construction Employment Percent Change



Region 2.

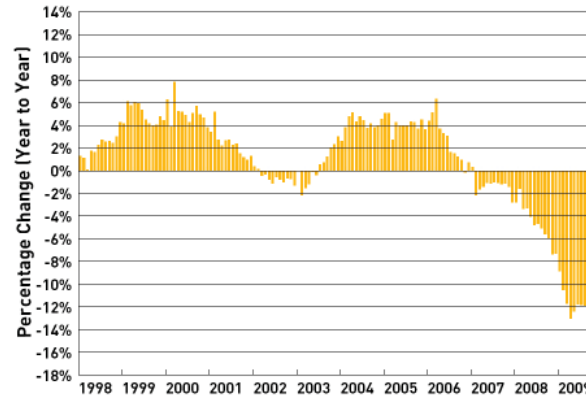
New Jersey, New York, Virgin Islands, Puerto Rico

Region 2 remains one of the least impacted regions in the country, although it is now losing jobs at a more rapid pace than before. New York, the strongest state in the region, while still declining, is one of only twelve states in the country experiencing that decline at less than 10%.

The current overall economic picture in the region is better than most regions. The New York City region entered the recession much later than most other areas, and has seen a far smaller decline in activity. This area also has the potential to recover sooner than most with the potential for stable market growth and strong regional economic drivers, particularly in the New York City portion of the region.

For construction costs, the construction output gap is likely to be a significant factor in the short term, but cost push will be evident, particularly as the recovery engages in 2011 and beyond. Demand led inflation could become a significant factor within the next five years.

Region 3. Construction Employment Percent Change



Region 3.

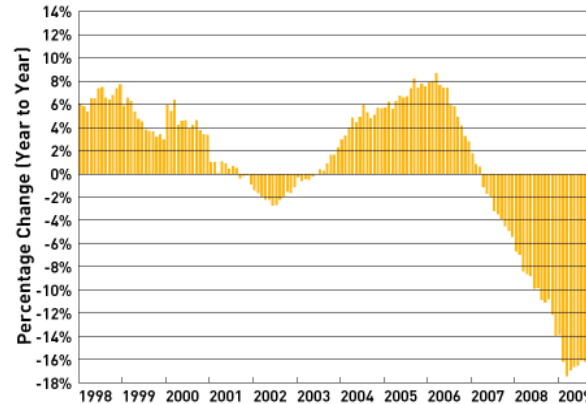
Delaware, District of Columbia, Maryland, Pennsylvania, Virginia, West Virginia

Some of the states in Region 3 are beginning to show signs of stabilization. While construction activity in the region continues to slow, like most other regions, the decline has begun to level off over the past few months. This leveling is due in large part to weak improvement in Virginia and West Virginia, as the remaining states have continued to experience incremental increases in job losses over the past several months.

The current overall economic picture in the region is better than most regions. The DC region in particular has seen a far smaller decline in activity than much of the rest of the country. This area also has the potential to recover sooner than most largely due to the strength of the economic drivers in the corridor between DC and the New York City region. The long term economic picture in the region is quite strong. The DC region is set to receive significant stimulus funding, and there is likely to be steady job growth and reasonable prospects for continued long-term demand for construction services.

For construction costs, the construction output gap is likely to be a significant factor in the short term, but cost push will be evident, particularly as the recovery engages in 2011 and beyond. Demand led inflation could become a significant factor within the next five years.

Region 4. Construction Employment Percent Change



**Region 4.
Alabama, Florida, Georgia,
Kentucky, Mississippi, North
Carolina, South Carolina,
Tennessee**

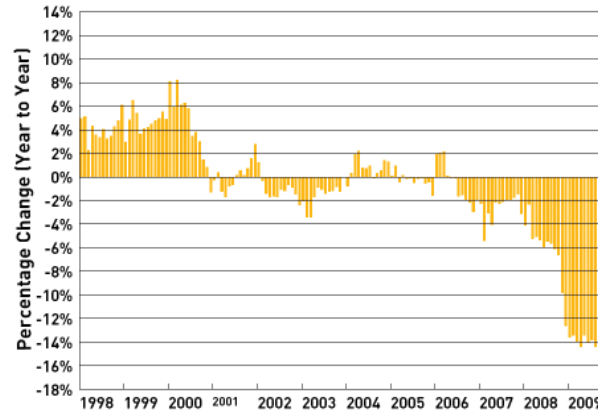
Region 4 continues to struggle, and is now second only to region 9 in its continued rate of decline. Five of the ten worst hit states in the country – Alabama, Georgia, Kentucky, North Carolina, and Tennessee – are included in this region, with Tennessee and Kentucky experiencing declines at a rate of more than 20%. The only state in the region currently experiencing declines of less than 10% is Mississippi. Since this region accounts for slightly over 19% of total national construction employment, the decline in this region is a significant part of the overall national decline.

The Atlantic states have experienced significant overbuilding, particularly in residential and hospitality construction. The backlog will take time to eliminate, and with these sectors being among the most impacted by the current recession, they are unlikely to see a rapid strengthening any time soon. The weakness is also translating into much weaker tax revenue, and so state and local government spending is likely to be constrained.

This means that this portion of the region has one of the greatest output gaps in the nation, and is likely to experience more aggressive competition for longer than other regions. The western portion of the region experienced far less excess, but it, too, is struggling to find an economic footing for growth. Recovery is likely to be some way off in this region, with recovery occurring more rapidly in the western states than in the Atlantic ones. In the long term, the region still has good economic prospects, and, while population and economic growth may not return to levels seen in 2004 to 2007, there should be stable long term growth after the recovery has stabilized.

For construction costs, the construction output gap is likely to be the dominant factor in the short term, keeping cost push limited for the next year or two. As the output gap shrinks beyond 2011, cost push will become more evident, and there is the possibility that demand led inflation will become a significant factor in the next several years.

Region 5. Construction Employment Percent Change



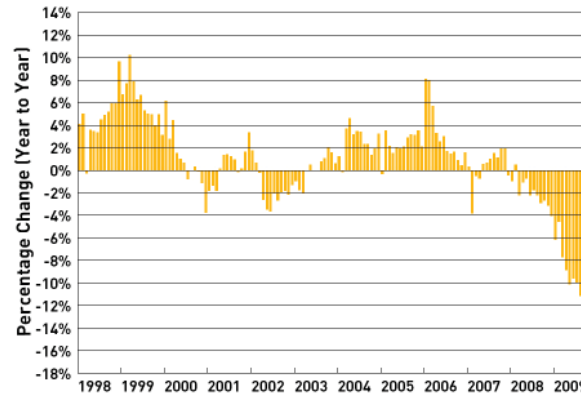
**Region 5.
Illinois, Indiana, Michigan,
Minnesota, Ohio, Wisconsin**

Despite a leveling off of the overall decline, Region 5 remains very weak. Construction activity was lower in 2009 than at any time in the past twelve years, and this is the one region that saw virtually no growth during the period of strong national growth in 2004 to 2007.

The current overall economic picture in the region is very weak, as it has been for many years. The overall economies in the region remain very vulnerable, with low prospects for employment and economic activity growth. The region has been severely impacted by the current economic conditions, and there is little sign of a pick-up in demand for construction in the region over the next two to four years.

For construction costs, the construction output gap is likely to be the dominant factor, at least in the short term, with inflation remaining low. As the gap narrows in the medium term, cost push will begin to be evident. It is unlikely that demand led inflation will become a significant factor within the next five years.

Region 6. Construction Employment Percent Change



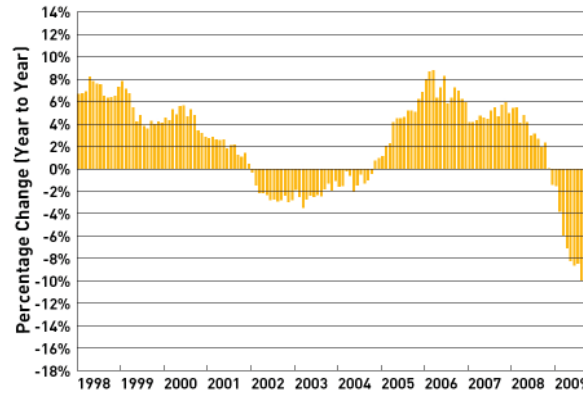
**Region 6.
Iowa, Kansas, Missouri,
Nebraska**

Region 6 is currently the least impacted region in the country, declining at only slightly more than 11% per annum. This region did not, however, experience much growth in the period of 2004 to 2007, when much of the rest of the nation saw significant growth in activity.

The current overall economic picture in the region is not particularly strong, but is relatively stable. It is not a region given to large shifts in either direction, and there are no significant economic engines in the region.

For construction costs, the construction output gap is likely to be a moderately strong factor, at least in the short term, with inflation remaining low, but because the output gap is smaller in this region, the region may be quicker to see a return to cost-push inflation. It is unlikely that demand led inflation will become a significant factor within the next five years.

Region 7. Construction Employment Percent Change



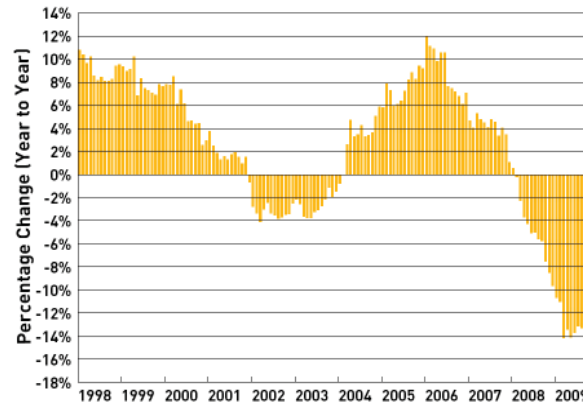
**Region 7.
Arkansas, Louisiana, New Mexico, Oklahoma, Texas**

Region 7 continues to experience mild decline. Arkansas, Louisiana, and Oklahoma are among only twelve states that are experiencing contraction at a rate of less than ten percent per annum. Texas, however, is seeing sharper declines, now at more than 16%, although this is to some degree catching up, since Texas was one of the last major states to show decline. And for the first time since early 2008, Louisiana's market has dipped into the negative. However mild it may be, however, since this region accounts for slightly over 14% of total national construction employment, the decline in this region is a significant part of the overall national decline.

The current overall economic picture in the region is relatively good. The recession has been later and less severe here than in much of the rest of the country. The region also has relatively good economic prospects, both in the short and mid-term. In general the region may experience a shorter downturn, and a quicker recovery than many other areas.

For construction costs, the construction output gap is likely to be a significant factor in the short term, but cost push will be evident, particularly as the recovery engages in 2011 and beyond. In the medium term, this region has the potential for stronger recovery in demand, particularly in the Dallas/Austin and the Gulf regions. Demand led inflation could become a significant factor within the next five years.

Region 8. Construction Employment Percent Change



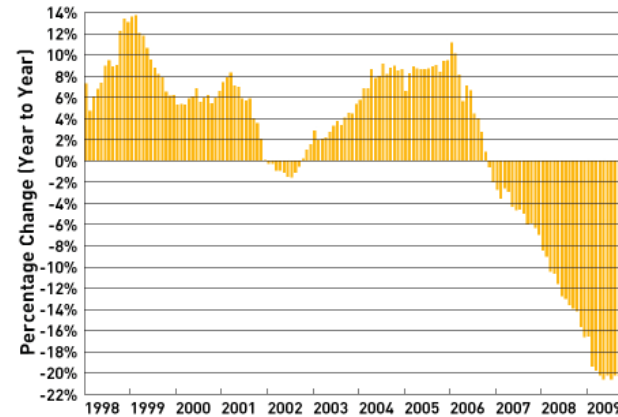
**Region 8.
Colorado, Montana, North
Dakota, South Dakota, Utah,
Wyoming**

The overall decline in Region 8 has stabilized in the past several months. However, while the region may be maintaining a steady rate, individual states have seen some significant shifts. Wyoming is now one of the ten worst hit states, declining at an annual rate of nearly 17%, and South Dakota and Colorado have continued to slip in recent months, although South Dakota, at least, remains in the ten least impacted states in the country. In addition, North Dakota remains the only state in the country to continue to experience positive growth, although this growth is fairly weak, at less than 2%.

In the short term, this region is likely to remain weak. Much of the construction growth had been driven by population movement, particularly in the two largest states of Colorado and Utah, and by speculative overbuilding. The current recession has sharply reduced migration into the region, and the weakness in the housing market is likely to keep growth low for some time to come. In the longer term, the region should return to strength, but this may be four or more years away.

For construction costs, the construction output gap is likely to be the dominant factor in the next one to two years. Cost push will become evident as the recovery becomes stronger in 2011 and beyond. The region has the potential to regain strong growth and demand led inflation could become a significant factor later within the next five years.

Region 9. Construction Employment Percent Change



**Region 9.
Arizona, California, Hawaii,
Nevada**

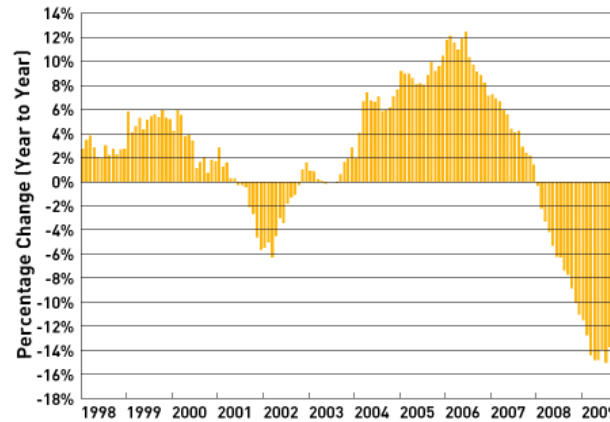
Region 9 remains the hardest hit region in the country, both in percentage terms and in total job losses. Since the peak in the summer of 2006, the region has shed more than half a million jobs, and has suffered a decline of more than 35% in total construction employment over the past three years. Arizona and Nevada remain the top two most impacted states, experiencing declines of over 26% and 23% respectively, while California remains in the top ten, at a decline of nearly 18%.

Overall the region has a very large output gap, and little opportunity to narrow the gap, since potential demand for construction services is very weak. The economic outlook for the region in both the short and mid-term is weak. The State of California has significant revenue challenges, and public sector spending is likely to be limited in most sectors. The area has experienced a large degree of overbuilding, particularly in the residential sector. Population growth due to migration has all but stopped due to the fall in the residential market.

All of these factors will take some time to correct, and it is likely that any recovery in the region will be slow. In the mid to longer term, the region has the potential to reclaim high construction demand to meet population growth and to support the expected long term economic growth.

For construction costs, the construction output gap is likely to be the dominant factor in the short term, but cost push will be evident, particularly as the recovery engages in 2011 and beyond. Demand led inflation could become a significant factor within the next five years.

Region 10. Construction Employment Percent Change



**Region 10.
Alaska, Idaho, Oregon,
Washington**

The decline in construction activity in Region 10 has begun to stabilize in recent months, to about 14%. Alaska is the only state in the region currently experiencing loss at less than 10%, but it is a relatively small market, and was not as impacted by the rapid growth of the previous years. As such, it should not experience as severe a downturn in prices. Of the three contiguous states, only Oregon has shown any signs of improvement, with decline now at slightly less than 15%, while Idaho and Washington continue to experience falling demand, at 13.5% and 14.7% per annum respectively. All three states experienced strong growth from 2005 through 2007, and all are currently experiencing challenging conditions for bidders, with moderate to strong price deflation in the range of 10% to 20% from the peaks of 18 months ago.

The current overall economic picture in the region is improving, and the region has relatively good economic prospects, both in the short and mid-term. In general the region may experience a shorter downturn, and a quicker recovery than many other areas.

For construction costs, the construction output gap is likely to be a significant factor in the short term, but cost push will be evident, particularly as the recovery engages in 2011 and beyond. Demand led inflation could become a significant factor within the next five years.

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