2016 Construction Hiring & Business Outlook Media Call Remarks

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Hello everyone, thank you for dialing in today. My name is Stephen Sandherr and I am the chief executive officer of the Associated General Contractors of America. With me today is our chief economist, Ken Simonson and Jon Witty, the vice president and general manager for Sage Construction and Real Estate, North America.

We also have three contractors on the call with us today, Gary Smith, the president of Seattle, Washington-based Lease Crutcher Lewis; Josh Clardy, the President of Myrtle Beach, SC-based JW Clardy Construction Company; and Mike Kaiman, the Southeast Texas Vice President for Turner Construction. They are here to talk about conditions in their local markets.

As some of you know, we survey our member firms to get their take on what labor and market conditions will be like for the coming business year. We then closely analyze those survey results and prepare our annual Construction Hiring and Business Outlook. This year we are teaming up with Sage Construction and Real Estate to prepare the Outlook and have added some new insights into how construction firms are – and will be - using technology to remain competitive.

Over 1,500 construction firms participated in our Outlook survey between mid-November and mid-December representing a broad range of firms in terms of size, business volume and geographic distribution. What is clear from the results of this year's survey is that the construction industry will continue to recover in 2016 as many firms add to their headcount amid growing demand in a range of private and public sector construction markets.

It is also clear, however, that the industry faces a number of challenges that have the potential to dampen, and possibly even undermine, the sector's recovery. Among those challenges are workforce shortages, the growth in federal, state and local regulations and health care costs. In other words, 2016 won't be easy, but should definitely be a good year for many construction firms.

Now I would like to turn things over to Ken to provide some details from this year's Outlook, Ken…

Ken Simonson

Thank you Steve. And you are correct, contractors are generally pretty optimistic about the Outlook for this year. They expect a mix of private and public sector market segments will drive demand for construction in 2016. As measured by the net positive reading – the percentage of respondents who expect a market segment to expand vs. the percentage who expect it to contract – respondents are most optimistic about the outlook for retail, warehouse and lodging with a 21 percent net positive.

Respondents were also positive about the hospital, private office, multi-family residential and higher education construction. They are also optimistic about the prospects for K-12 school and public building construction, particularly in contrast to last year when contractors were generally pessimistic about all public construction market segments.

Contractors are less optimistic about other private and public segments, including manufacturing, highway, other transportation such as rail, transit and airports; power, and direct federal construction markets.

Yet it is important to note that this year's Outlook survey was completed prior to enactment of federal legislation to increase funding for highways, transit and direct federal agency spending, and to extend the expiration date for wind, solar and other tax provisions helpful to construction.

Given their optimism about growing demand for construction, it is not surprising that 71 percent of construction firms say they will increase their headcount in 2016. In most cases, however, that hiring will only lead to modest increases in the overall size of most firms. Sixty-three percent of firms report their planned hiring will only increase their total headcount between 1 and 25 percent while only 8 percent report they will expand their headcount by more than 25 percent this year.

Yet even as firms plan to expand their headcounts, those expansion plans appear less ambitious than in 2015 when 80 percent of firms reported plans to increase the size of their workforce. One factor that appears to be affecting hiring plans is the continued shortage of qualified workers. Seventy percent of firms report they are having a hard time finding either salaried and craft professionals. And 69 percent of respondents predict that labor conditions will remain as tight, or get worse, during the next twelve months.

Firms are responding to these worker shortages by increasing pay and/or benefits. Forty-nine percent of respondents report they have increased base pay rates, 30 percent report they are providing incentives and/or bonuses and 23 percent report they have increased their contributions to employee benefits to retain or recruit workers. An additional 15 percent say they are considering increasing pay and/or benefits in the near future to cope with worker shortages.

Firms are also coping with worker shortages by investing in training and development programs. Nearly half of firms report they plan to increase their investments in training and development in 2016 compared to 2015. What is particularly striking about the findings on worker shortages is that they are consistent with the responses from last year's Outlook. In other words, after a year of raising pay and increasing benefits, contractors remain as worried about the lack of qualified workers as they were at the beginning of 2015.

Of particular concern is that the lack of qualified workers poses a challenge to workplace safety. Forty-seven percent of firms report that inexperienced labor and worker shortages are a "major" challenge to the safety and health of workers while another 37 percent cite worker shortages as a "minor" challenge.

In addition to coping with worker shortages, contractors are also worried about the continued increase in health care costs. Seventy-nine percent of firms report the cost of providing healthcare for their employees increased in 2015 while 81 percent expect their healthcare costs will increase in 2016.

Even as contractors are being forced to spend more to provide healthcare coverage for their employees, many firms report they are prepared to increase their investments in information technology. We've asked Jon Witty with Sage Construction and Real Estate, to walk us through some interesting findings about how and why firms are spending on IT in 2016. Jon…

Jon Witty

Thank you Ken.

As Ken mentioned contractors faced with qualified labor shortages are not planning to expand their headcount as ambitiously as last year. Their alternative is to find ways to do more with their current staff. So it's not surprising that contractors are increasing their investment in IT as a way to achieve higher productivity. 42% of the firms surveyed say they are currently spending 1% or more of revenue on IT. That number is up from 32% of firms who said they spent 1% or more of revenue in studies conducted the past two years. In addition 41% of firms plan to *further* increase their IT spend in 2016. But even with a 10% increase in the firms spending 1% or more, the construction industry spends the smallest percent of revenue on IT compared to other major industries (according to Gartner).

That’s a bit about how they spend, now let’s take a look at how they consume that IT spend. 69% of contractors outsource some or all of their IT. Outsourcing is most common among smaller firms, which are more likely not to have any in-house IT staff. More than 3 out of 4 firms under $50 million in revenue report that they outsource their information technology. This confirms our experience at Sage where we are seeing more contractors moving their back-office systems to remote data centers that are managed by third-party IT service providers.

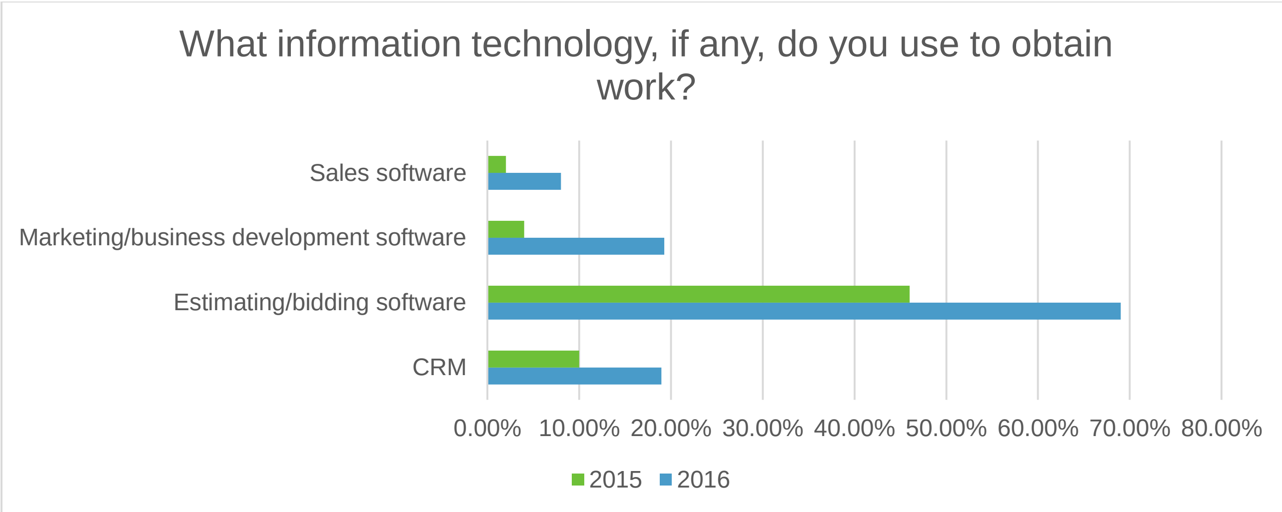
	Annual Revenue						
	All contractors	Under $10M	$10M-$30M	$30M-$50M	$50-$100M	$100M-$500M	Over $500M
No in-house IT staff	42%	55%	53%	38%	27%	11%	5%
Outsource their IT	69%	74%	86%	76%	59%	37%	26%

Along with the move to outsourcing is the adoption of cloud-based software. It is becoming more relevant for contractors, because of the speed at which issues on the job site need to be communicated, escalated and resolved. The faster the resolution, the faster everyone makes money on the project. 59% of firms currently use or plan to use cloud-based software, which is most often accessed through mobile devices. The ability to access information anytime and anywhere is the main reason 63% of firms say they are adopting cloud-based software.

But with the move to cloud comes a concern about security, and this is the main reason 23% of firms are not using cloud-based software yet. This is a valid concern, but especially for companies who have homegrown systems that are exposed to the Internet. Often times we see that with some early adopters of mobile technology, there is a lack of understanding regarding all the aspects of security. Commercial cloud-based software should be certified by a third party that it meets ISO 27001 standards for securely managing sensitive company information. Contractors should always look for this certification when evaluating cloud-based solutions. Contractors are also taking notice of the very real business threat of cyber crime. 75% of firms said they have implemented an overall IT security plan to protect against hacking. Mobile device security, however, remains an open issue with only 46% of contractors indicated that they currently have a mobile security policy in place an increase of 15% over the prior year.

And one of the fastest growing categories of cloud based software adoption is with collaboration systems. Collaboration is an essential element in today’s fast paced construction environment. Whether that collaboration is about project management, estimating or any number of issues it has a huge impact on a project’s outcome; financial, quality or performance. While contractors still rely heavily on email (92%) and file sharing sites (71%), 40% have adopted some kind of online collaboration software. We expect both the adoption and sophistication of cloud-based collaborative tools to continue as project owners and general contractors have a greater expectation for collaboration among all the project team members.

In the area of winning work, contractors continue to experience increased competition for jobs, and are investing in software to help them win more business. Estimating and bidding software has seen the greatest adoption growing from 46% of firms in 2015 to 69% of firms this year, a 23% increase! Sales, marketing and CRM software are also being used by significantly more contractors, although their adoption is still under 20% of firms.



So all in all we see continued growth in the adoption of mobile technology and collaboration software and a continued move to the cloud, all done with an increasing focus on security. While the construction industry is not known for being an early adopter of IT technology, the overall adoption is increasing. I believe that we will see continued adoption of technology as a strategic competitive advantage and as a way to deliver a superior experience with higher levels of both clarity and communication to project stakeholders.

Now I would like to turn things back over to Steve Sandherr who has some additional observations about this year's Outlook. Steve…

Steve Sandherr

Thank you Jon and thank you Ken. Beyond economic and IT challenges, contractors also must cope with the impact of decisions made by federal, state and local officials. In particular, many contractors are worried about the continued, and seemingly more rapid, expansion in the number and scope of federal, state and local regulations. For example, 39 percent of contractors report they are worried about the continued expansion of federal regulations and the impacts these measures have on their businesses. Thirty-four percent of respondents also report they are worried about the growth in state and local regulations.

Contractors are also concerned by the fact the Obama administration no longer sees employers as a potential partner in helping improve workplace safety. Since the 1990s, the federal government has been incredibly successful in reducing construction fatality and injury rates by partnering with most employers to educate them on the best way to improve safety. Yet the current administration has made it clear that its preferred regulatory approach is enforcement over collaboration. That is why 19 percent of contractors cited the lack of cooperation from federal regulators as a major safety concern while another 40 percent said it was a minor concern.

Despite these challenges, contractors are expecting 2016 to be a mostly positive year. More firms expect key market segments to expand or remain stable. They plan to expand their headcount and are prepared to invest in new technologies. Yet their enthusiasm is tempered by the expectation that labor conditions will remain tight, new and relatively inexperienced workers will pose new safety challenges, the cost of complying with regulations will continue to grow, their health care costs will rise yet again and their new technology could pose security threats.

These challenges are real, but they are not insurmountable. Indeed, measures we outlined in our recently updated Workforce Development Plan are designed to re-invigorate the pipeline for recruiting and preparing new workers. The association has also helped coordinate industry-wide efforts to ensure that any final new regulatory measures are effective and minimally disruptive. We have continued to provide a host of safety training and tips to our members so they can continue to protect their workers. And IT firms like Sage are working to make sure new technologies are as safe as they are effective.

As long as local, state and federal officials are willing to act on our workforce measures, embrace a more rational approach to regulations, identify effective measures for controlling health care costs, work with employers to help them improve workplace safety and protect e-commerce, the industry should continue to expand. That is precisely why AGC of America will continue to focus its energies on ensuring the continued growth of this industry.

Before we take questions, I would like to invite Gary Smith, Josh Clardy, and Mike Kaiman to share their observations about local market conditions where they operate. After that, we will take any questions the reporters on the line may have...

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