

WHAT'S IT COST?



The Producer Price Index (PPI) for November revealed what most consumers and businesses were feeling at the cash register. Muted global demand and plunging oil prices are helping to keep the costs of building products and materials well in check while pressures from tighter labor supply continue to push wages higher. The opposing market forces are offsetting each other to create an environment that is mostly flat in the short term and slightly ahead over the pace of inflation overall.

What bears watching are how those dynamics will change as demand picks up for materials and labor costs continue to rise. A quick glance at the chart below reveals more red than black numbers but it's worth a closer look to see that most of the red numbers are in the columns reflecting the pricing in the last 90 days, during which oil prices tumbled almost 25 percent. That means lower fuel costs, lower prices for asphalt and other oil-derived products, and lower energy costs for manufacturing building products. Likewise, prices for steel and other metals saw another leg down in pricing since Labor Day. While there was another five-dollar decline in oil prices since December 1, the November PPI report reflects prices that likely have seen bottom. Whether those pricing levels hold for an extended period is a concern the construction industry must have.

Tight labor supply in the U.S. construction market and rising construction volumes have and will continue to push prices upward as wages and profits increase. During 2016, the likelihood is that there will be more market forces that press material prices upward than down. How fast and how far those pressures work will determine the trend in construction inflation.

IHS PEG Engineering and Construction Cost Index (ECCI) showed in November that the pace of change was faster than earlier in 2015. The overall index registered 43.7, up from 40.9 in October. (A reading greater than 50 represents upward pricing strength and a reading below 50 represents downward pricing strength.) The subcontractor labor index increased by six points to 51.1 in November, indicating that labor costs are rising. HIS economist see materials staying at the current levels in 2016 but see improving demand and tight labor supply pushing subcontractor pricing higher still. That ECCI sub-index is forecast to be 57.3 by May 2016.

One segment of the market that seems to be experiencing higher costs faster is the heavy and highway segment. Infrastructure costs have benefitted from lower diesel and asphalt prices but the supply chain for the highway segment cut capacity when construction fell off after the stimulus of 2009-2010, meaning that increases in volume will lift prices more quickly.

The National Highway Construction Cost Index, a measure of the cost of all projects awarded by states, increased 3.9 percent over the previous 12 months, according to data the Federal Highway Administration posted. The 12-month change was the steepest since September 2011. Passage of the Fixing America's Surface



Transportation (FAST) Act of 2015 is expected to begin pushing costs higher, especially as FAST plays out over five years. The Portland Cement Association forecasts that FAST will add 375,000 metric tons to cement consumption in 2016, with the impact of FAST adding 1.4 million tons in 2020.

PERCENTAGE CHANGES IN COSTS	Nov 2015 compared to		
	1 mo.	3 mo.	1 yr.
Consumer, Producer & Construction Prices			
Consumer price index (CPI-U)	0.0	(0.3)	0.2
Producer price index (PPI) for finished goods	0.0	(1.0)	(1.1)
PPI for final demand construction	(0.3)	0.7	2.1
Costs by Construction Types/Subcontractors			
New warehouse construction	(0.1)	0.9	2.2
New school construction	0.0	0.9	2.2
New office construction	(0.6)	0.5	2.3
New industrial building construction	0.1	0.4	1.9
New health care building construction	(0.5)	1.0	1.0
Concrete contractors, nonresidential	0.1	1.8	4.0
Roofing contractors, nonresidential	0.2	0.8	1.7
Electrical contractors, nonresidential	0.1	2.4	5.8
Plumbing contractors, nonresidential	(0.2)	(0.7)	(1.1)
Construction wages and benefits	N/A	1.0	2.4
Architectural services	0.1	0.2	1.6
Costs for Specific Construction Inputs			
#2 diesel fuel	(3.5)	(11.6)	(38.2)
Asphalt paving mixtures and blocks	(0.2)	(1.5)	(5.9)
Cement	(0.1)	(0.5)	6.2
Concrete products	0.5	0.9	2.8
Brick and structural clay tile	(0.4)	(0.4)	1.5
Plastic construction products	(0.3)	(0.4)	(0.2)
Gypsum products	(1.7)	0.5	(1.1)
Lumber and plywood	1.0	(0.4)	(7.4)
Architectural coatings	0.0	(0.2)	(2.6)
Steel mill products	(3.3)	(5.7)	(18.4)
Copper and brass mill shapes	(3.0)	(4.6)	(15.6)
Aluminum mill shapes	(1.4)	(2.5)	(13.0)
Fabricated structural metal	(0.6)	(2.5)	(1.2)
Prefabricated metal buildings	(0.1)	0.4	(0.2)
Iron and steel scrap	(11.5)	(31.7)	(52.7)
<i>Source Bureau of Labor Statistics, Updated December 11, 2015 Compiled by Ken Simonson, AGC Chief Economist</i>			