WHAT'S IT COST?

The April 13 report from the Bureau of Labor Statistics (BLS) on inflation in March drew headlines for its surprising decline in the Consumer Price Index (CPI), which declined 0.3 percent instead of the expected slight rise. That same surprise did not materialize for the Producer Price Index (PPI), nor for the PPI specific to construction.

A 6.2 percent drop in gasoline prices was the biggest factor in the monthly decline in the CPI, which was also weighed down by a record 7.0 percent plunge in the cost of wireless telephone services. The decline in gas prices was mirrored in the price of #2 diesel fuel, which dropped one percent from February; however, the long-term trend in fuel prices is significantly higher and a one-month dip in fuel costs hardly offset the significant year-over-year moves in basic metals, cement, lumber, and gypsum board.

Kenneth Simonson, chief economist for the Associated General Contractors of America (AGC) noted the long-term trends in several key materials for the construction industry in his analysis of the April 13 data. Simonson wrote;

> "Among the most widely used materials in construction, there were price increases over the past 12 months totaling 19 percent for steel mill products, 17 percent for copper and brass mill shapes, 8.8 percent for aluminum mill shapes, 7.6 percent for gypsum products such as wallboard and plaster, and 7.3 percent for lumber and plywood. In addition, the price index for diesel fuel, which contractors use directly and also pay for through surcharges on the thousands of deliveries to construction sites, soared 35 percent."

According to the BLS report, PPI for final demand in March increased 0.2 percent from February and 2.3 percent year-over-year from March 2016. The PPI for final demand construction rose 0.2 percent for the month and 1.5 percent. Thus far, competitive pressures and timing have prevented contractors from passing along the higher costs of tight labor and materials. In markets where business conditions are strong or labor is especially tight, prices are moving higher at a faster pace. Those dynamics are worth noting in Western PA, as a handful of major projects get underway later in 2017.

Other noteworthy data from the April report included a higher PPI for residential construction - PPIs for inputs to new residential structures rose 3.5 percent for single-family and 3.9 percent for multifamily housing over the previous year – and an increase in inputs to nonresidential construction of 3.5 percent, which more than doubled the rate of inflation for nonresidential construction put in place. That suggests a squeeze on contractors' profits and a coming increase in price for construction. Also pointing to future increases in cost were some large increases in major raw materials. Iron and steel scrap prices were up 63 percent year-over-year; liquid asphalt jumped 54 percent; and copper base scrap rose 15 percent.

A glance at the chart comparing prices over the past 12 months reveals few red numbers, a change following years of price deflation in construction materials and building products. Most of the black numbers, however, are small ones. Except for the short-term bump in gasoline and diesel, and the basic metals category, increases in construction material prices are a product of pent-up opportunities to hike prices again. Absent the increased consumption from global markets, like China's, in 2017, construction price increases will be impacted more by short labor supply and contractor selectivity. The fly in the ointment for this forecast is the potential for supply disruption due to an unexpected trade war or political reprisal.