# Construction Outlook for 2010 Brings a Little Cheer

***By the Forecasting Group, McGraw-Hill Construction Research and Analytics***

The construction industry endured a particularly tough year in 2009, reflecting the weak economic climate. Moving into 2010, the improving picture for the U.S. economy should lead to renewed expansion for some parts of the construction industry, though not all.

The value of new construction starts in 2009 is estimated to have plunged 25%, lowering the level of contracting to about 40% below the current dollar peak in 2006. Single family housing led the early stages of the downturn as the housing bubble burst, but the deterioration spread to most construction categories and in 2009, multifamily housing and commercial building have suffered the largest percentage declines. Even the typically more resilient types of building, such as educational buildings and healthcare facilities, lost considerable momentum in 2009.

These declines, of course, took place in the context of the longest and steepest economic recession since the Great Depression. Moreover, while the financial markets have stabilized, lending standards remain tight. On the plus side, interest rates are at historically low levels. In addition, last February's passage of the federal stimulus act provided a lift in 2009 to several project types, such as highways, bridges and courthouses, and that support should spread to a broader range of project types in 2010.

Fortunately, the recession has likely reached its end. While the weakness at the outset of 2009 means that economic growth for the full year will be down 2.5%, real GDP in the third quarter did rise 2.2%. Coming quarters should see continued, though modest, expansion. On a cautionary note, employment will stay soft well into 2010 as firms remain reticent about hiring. This unfortunately has serious implications for commercial building in 2010, adversely affecting such market fundamentals as vacancies and rents, which will keep construction starts down for at least one additional year. Tight bank lending standards will also impede commercial development, and the rising defaults on commercial real estate mortgages make the situation more tenuous.

Furthermore, state and local finances will not be able to turn around quickly given the declines in tax receipts that accompany decreased employment. This puts downward pressure on publicly funded structure types, although the federal stimulus funding will somewhat mitigate that downward pressure. This mix of factors means that the early stages of recovery for the U.S. economy in 2010 will be reminiscent of the subdued recoveries in 2002-2003 and the early 1990s. For 2010, real GDP is expected to advance 2%.

In similar fashion, overall construction activity is anticipated to begin to recover in 2010, at least in terms of construction starts. In current dollars, construction starts in 2010 should rise about 10%. (The construction *spending* statistics, which lag construction starts, are likely to see another year of decline in 2010.) One positive is that low interest rates and the extension of the homebuyer tax credit will spur demand for single family housing and, in turn, construction. Another positive is that funding from the stimulus act and federal appropriations will support more public works construction, as well as more work on government buildings. However, the year 2010 will still carry some of the negatives that were present in 2009 – weak market fundamentals for commercial building, restrictive financing and the diminished fiscal health for states and localities. The road back up will be slow and winding – but from the vantage point of late 2009, it seems to be moving on balance in the right direction.