

The Construction Market Outlook for 2010 and the Implications for the Design and Construction Professions

Kermit Baker, Chief Economist

The American Institute of Architects

AGC of Mass., BSA, and CFMA
December 3, 2009



Agenda

- Emerging recovery in the broader economy still looking for traction;
- Architecture firms still reporting very weak business conditions;
- Nonresidential construction outlook: weakness continues in 2010;
- Economic trends point to emerging issues for the design and construction professionals;

U.S. Economy – Beginning to Dig Out From Under

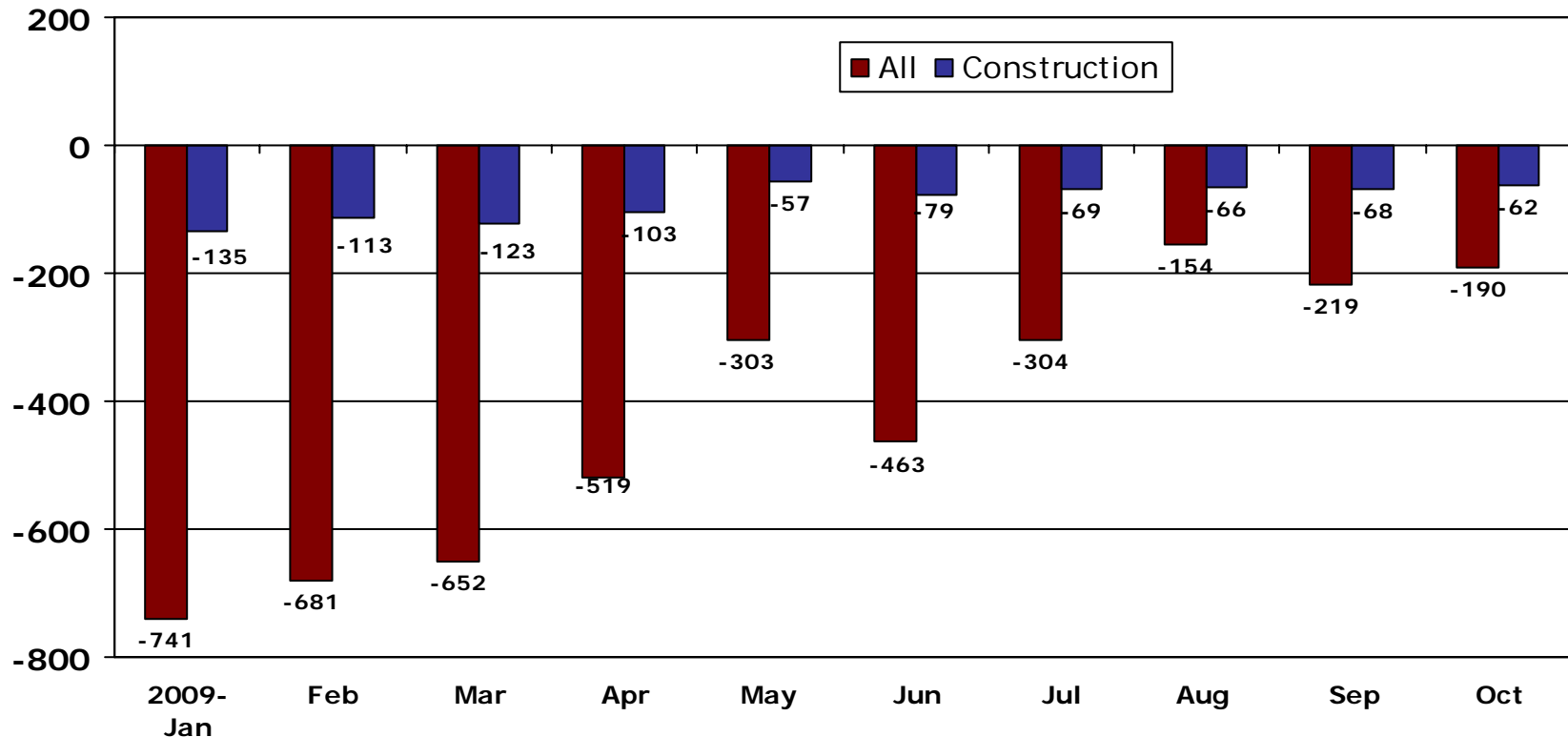
- Traditional economic leading indicators (e.g. stock market valuations; interest rates; money supply) have been very favorable in recent months;
- Much of federal stimulus funds yet to be spent, so boost to economy will come later this year and into 2010 and 2011;
- Low inflation and favorable interest rates have helped turnaround financial markets and credit conditions;
- Low value of U.S. dollar has helped exports, which has improved manufacturing activity;

But We're Not Nearly Out of the Woods Yet

- U.S. recession was the longest since the Great Depression; some sectors (such as nonresidential construction) have not yet recovered; ensuing upturn likely to be weak;
- Payroll losses still mounting; unemployment high;
- Wealth losses (stock market, home equity) substantial and limit consumer spending;
- Massive federal deficit will take years to resolve; extraordinary monetary stimulus may generate bout of inflation in the years ahead;

U.S. Business Payroll Declines are Significant, But Construction Accounts for Growing Share of the Total

Monthly declines in business payrolls (000s)



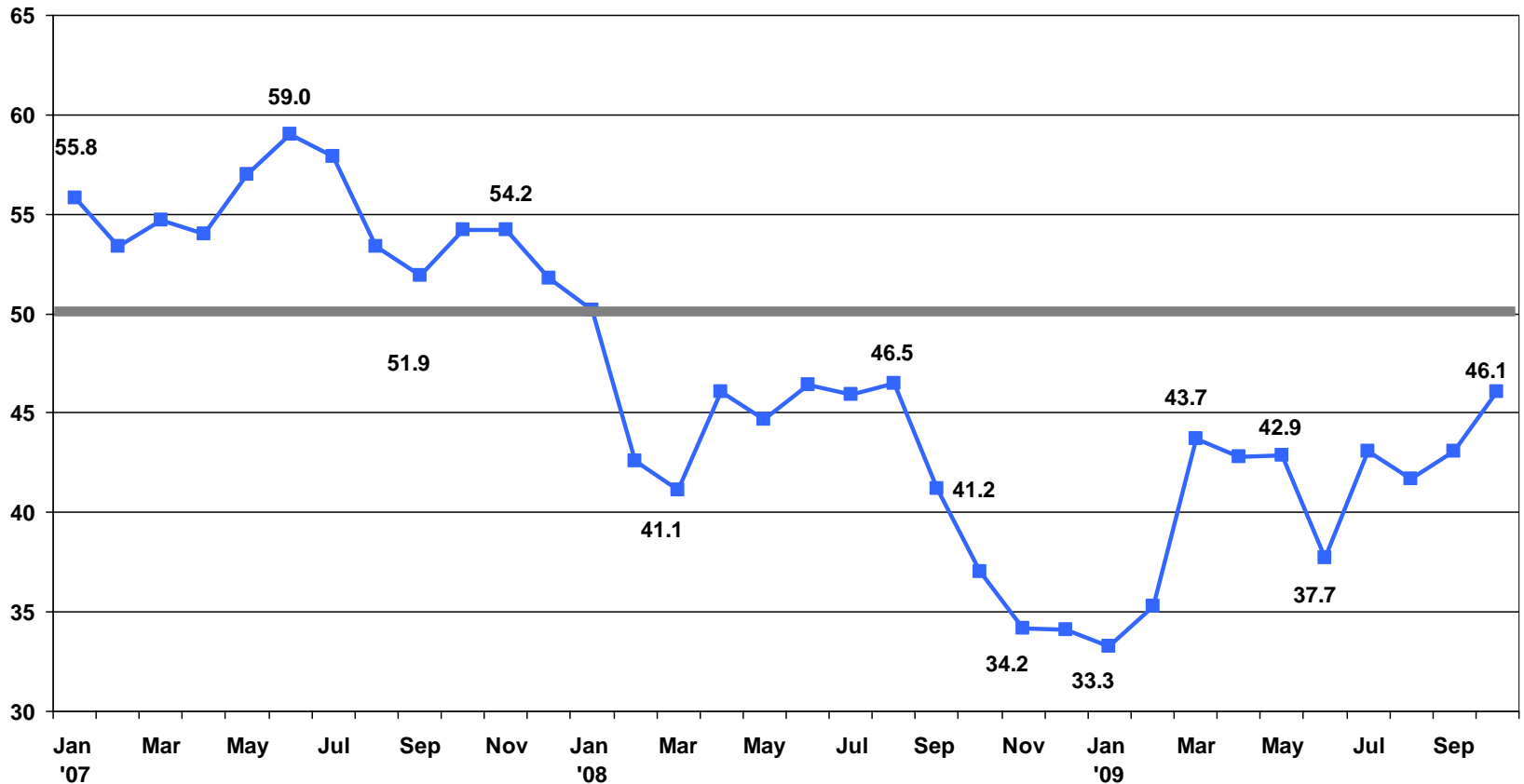
Source: US Department of Labor

Business Conditions at Design Firms: AIA Architectural Billings Index



Architecture Billings Index is Edging Up

billings scores since 2007; index: 50 = no change from previous month

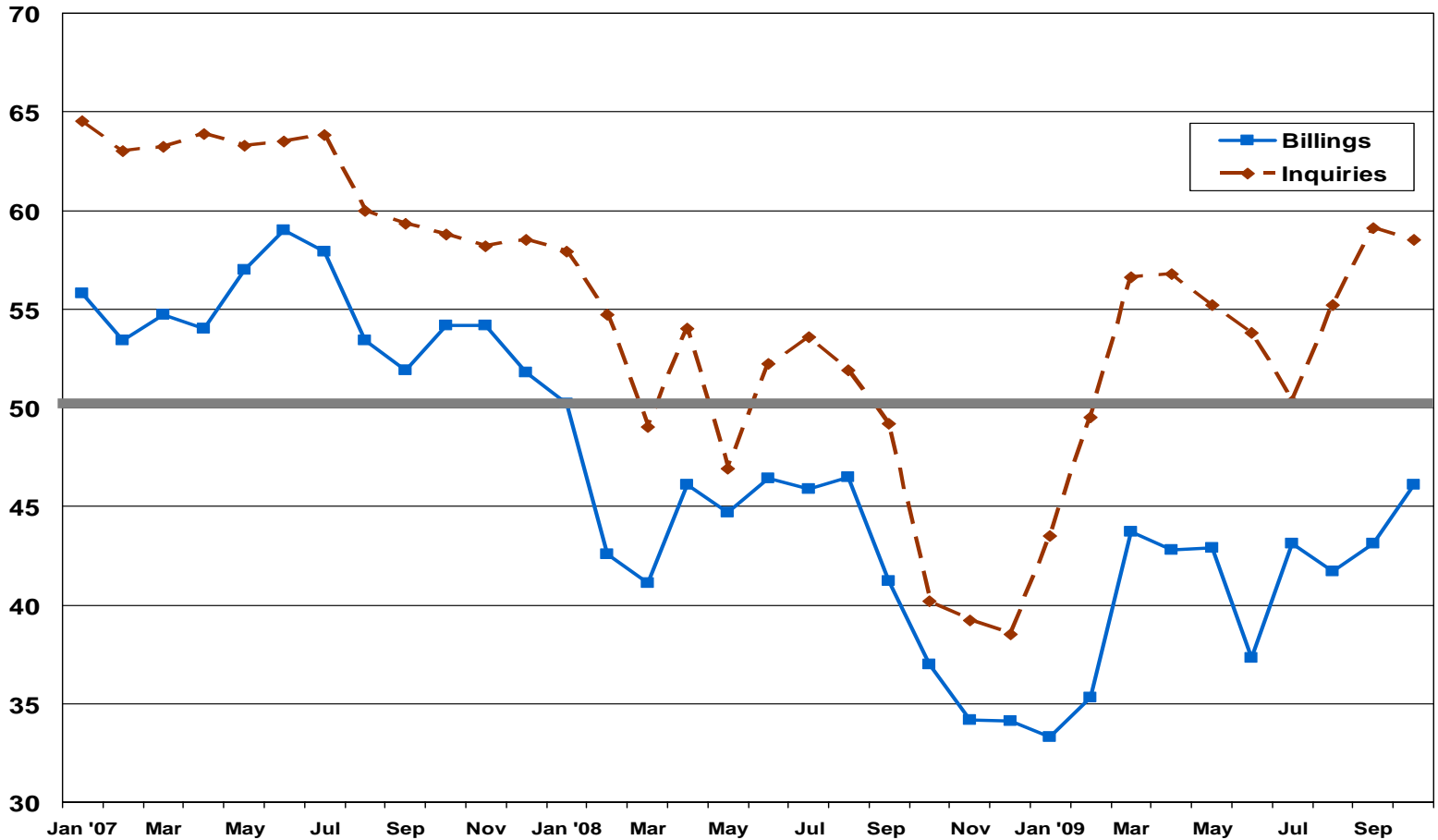


Source: AIA Architecture Billings Index



Inquiries Growth Continues to Outpace Gains in New Workloads

billings scores since 2007
index: 50 = no change from previous month

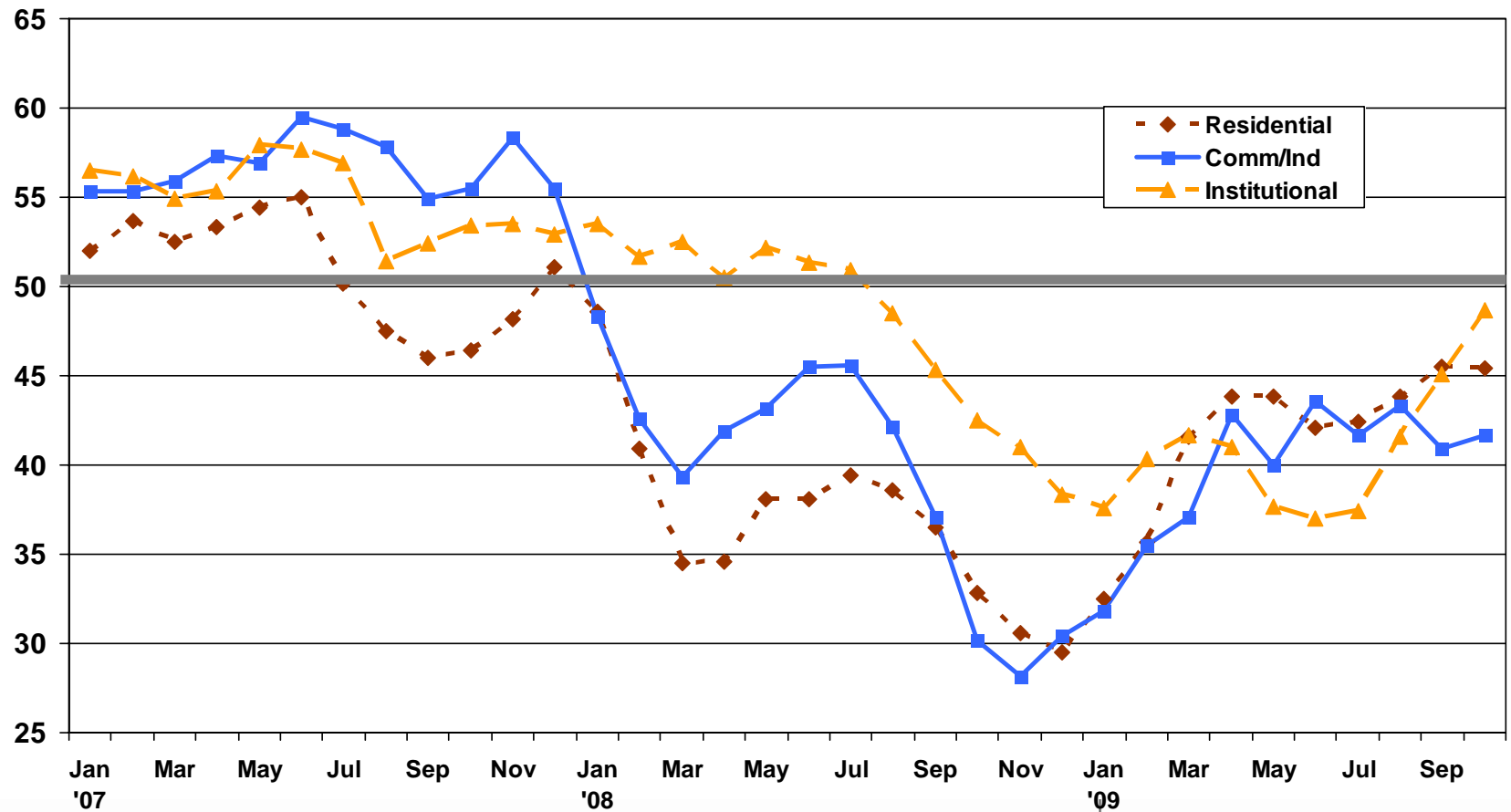


Source: AIA Architecture Billings Index



Institutional Firms Reporting Strongest Business Conditions at Present

Billings scores by firm specialization; Index: 50 = no change from previous month

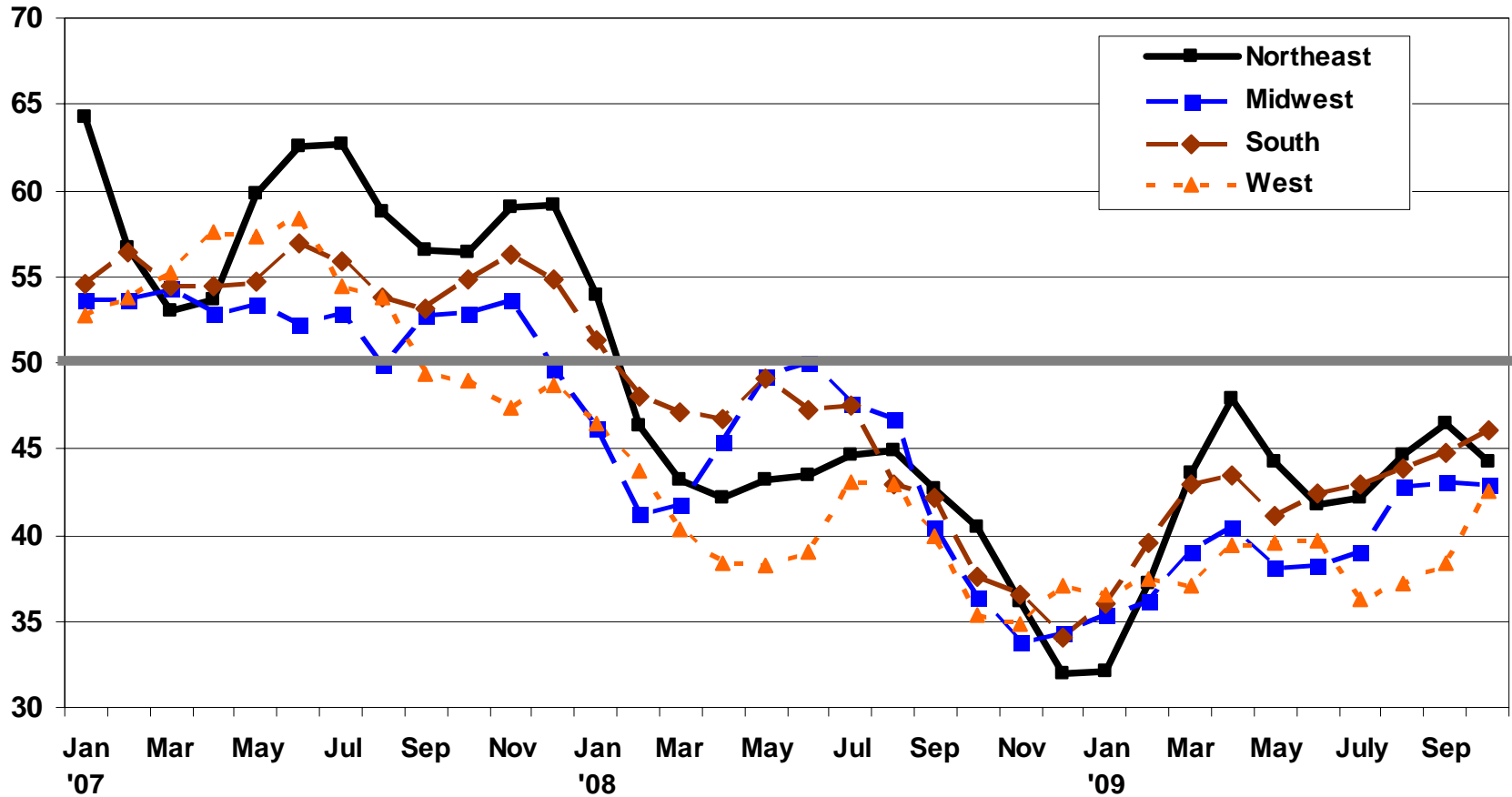


Source: AIA Architecture Billings Index



Regional Scores Trending Up, with Conditions in the South Strongest at Present

billings scores by region; Index: 50 = no change from previous month

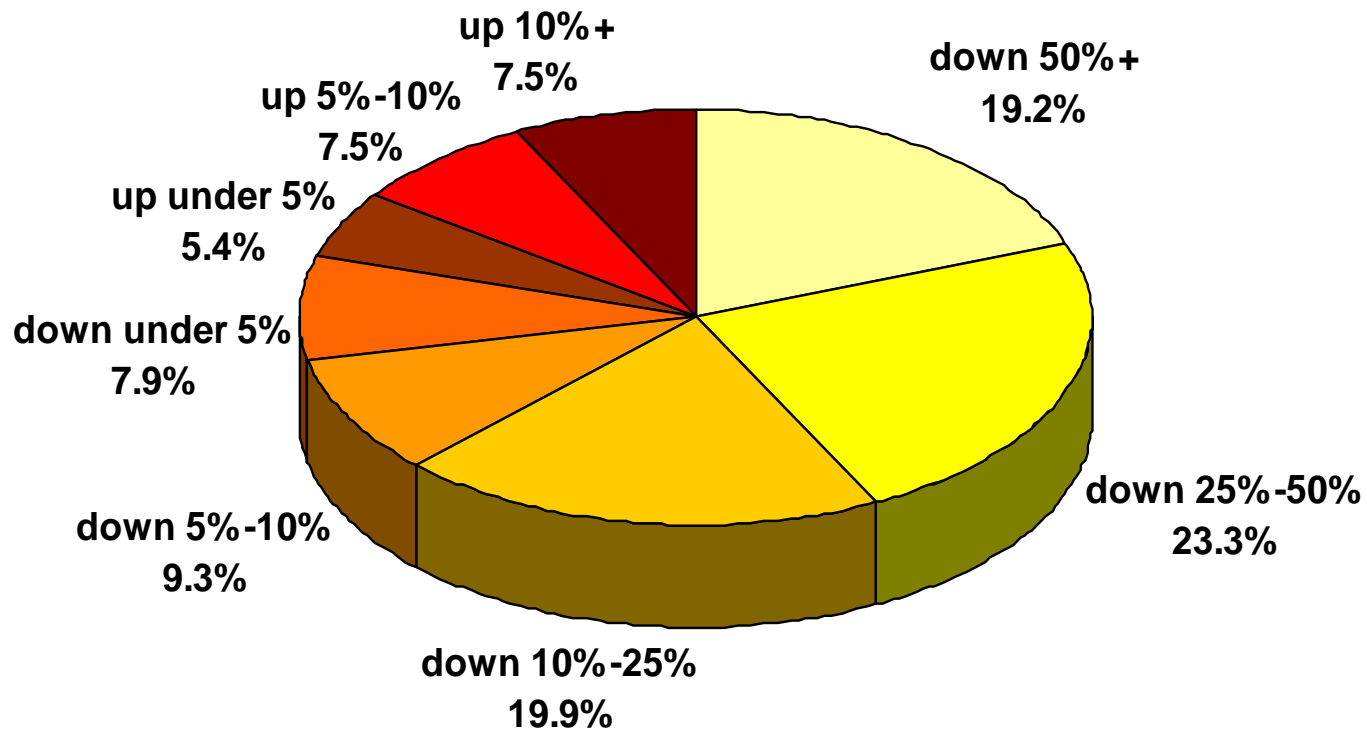


Source: AIA Architecture Billings Index



Revenue Declines in 2009 Were Sharp for Most Firms

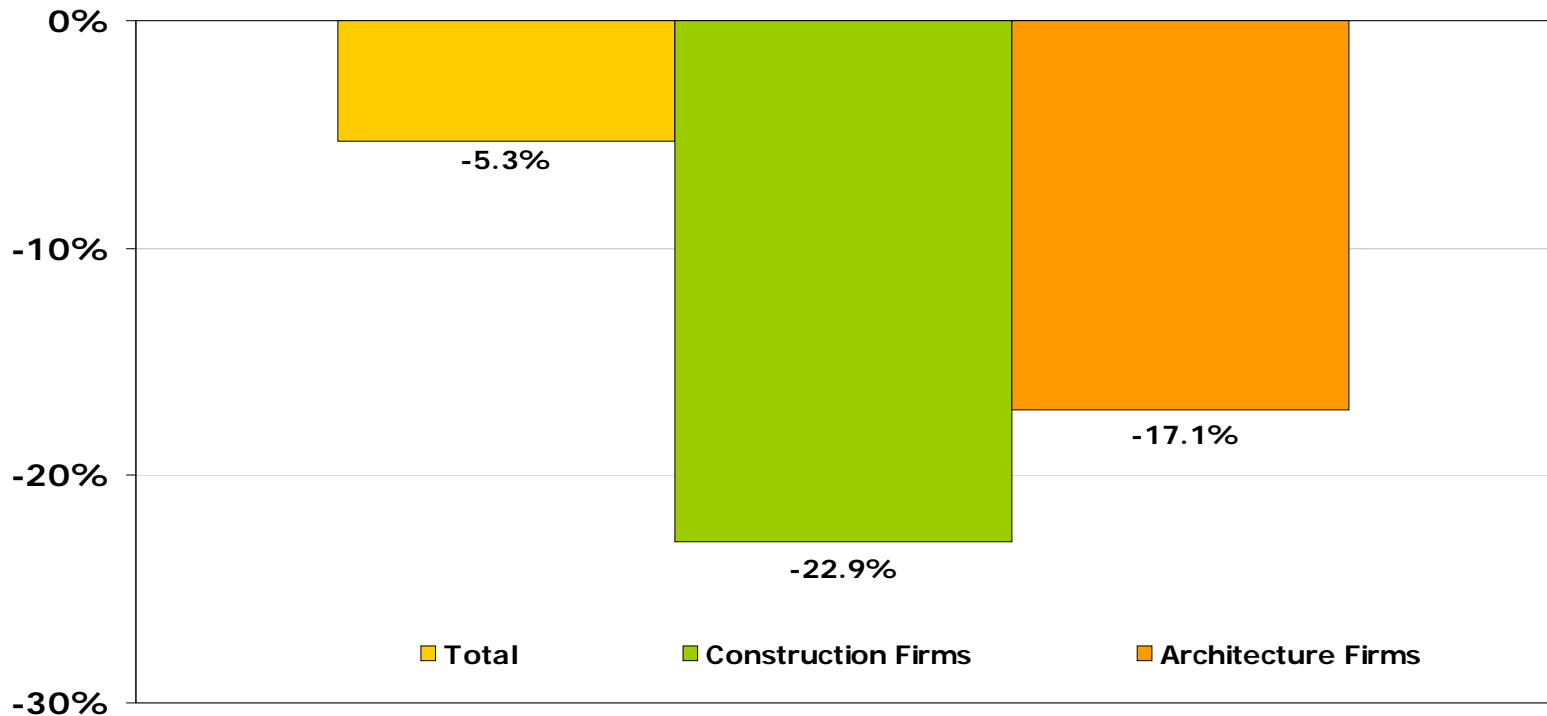
Estimate for firm revenue in 2009 compared to 2008; % of firms



Source: AIA Work-on-the-Boards Survey, November, 2009

Percentage of Job Losses in Broader Economy Have Been Exceeded by Losses in Construction and at Architecture Firms

Total percent declines in payroll employees from previous peak to date

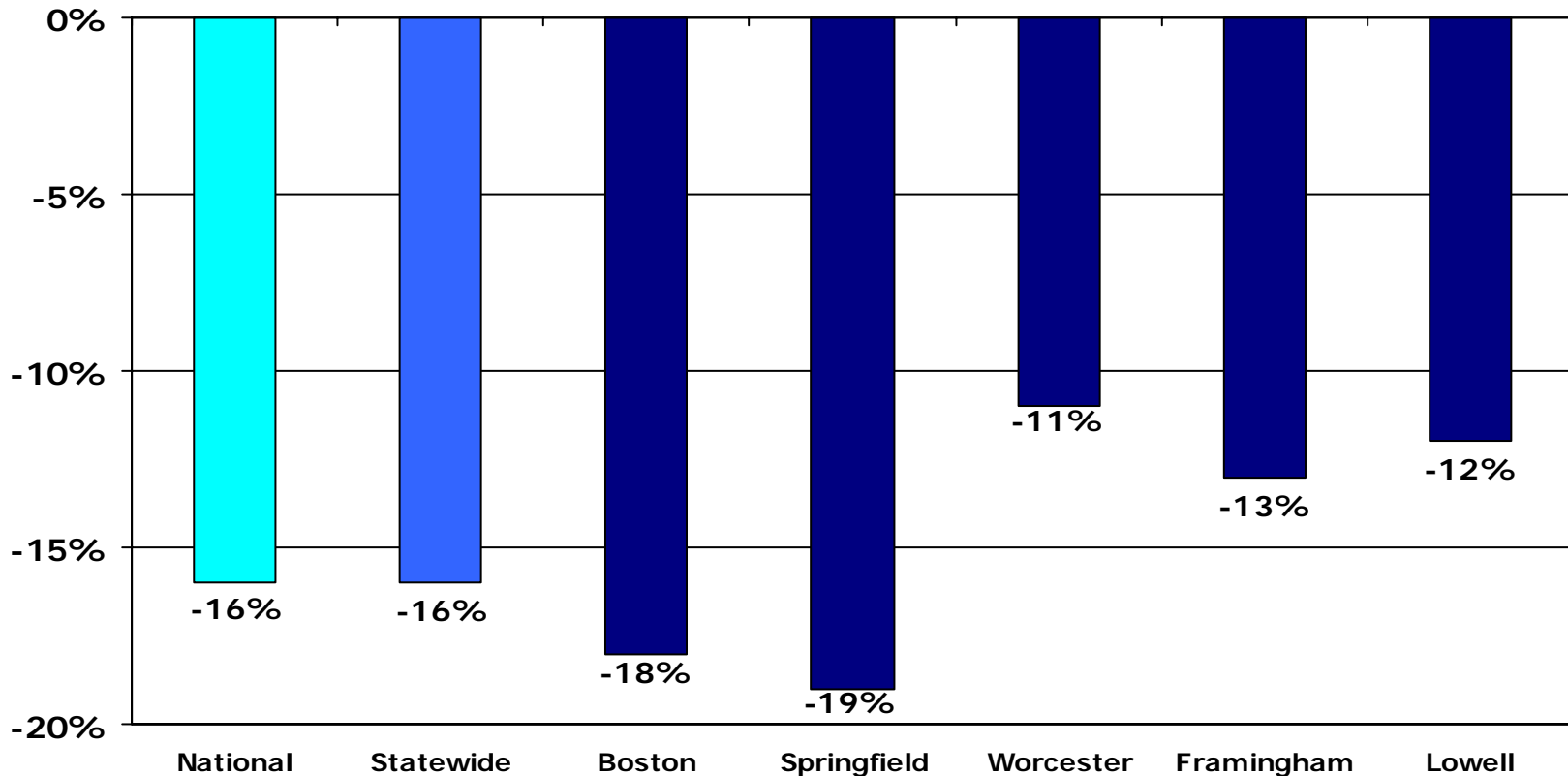


Source: U.S. Department of Labor



Construction Employment Losses Across State Over Past Year have Been Dramatic

Construction employment declines in Massachusetts from Oct. 2008 to Oct. 2009 by metro area



Note: losses for construction, logging and mining except for statewide and Boston
Source: U.S. Department of Labor; compiled by Ken Simonson, Chief Economist, AGC



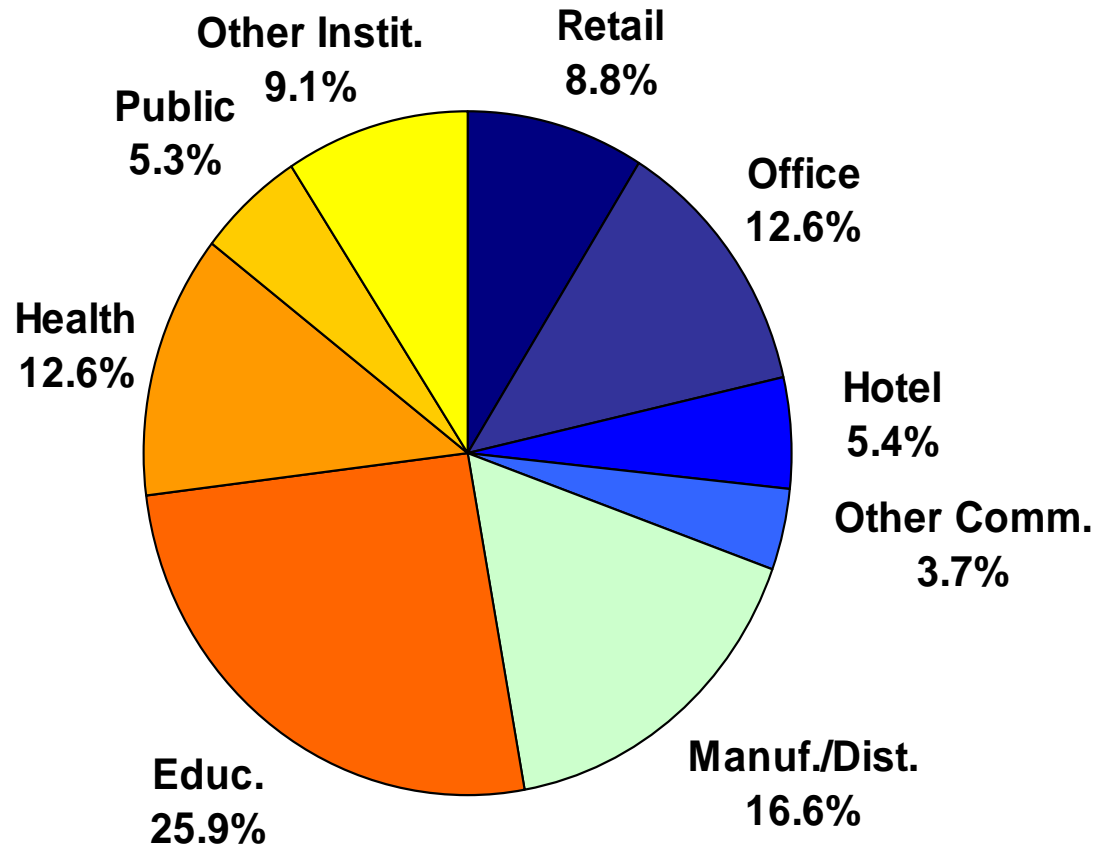
Nonresidential Construction Outlook:

2010-2011



Institutional Activity Accounts for Over Half of Nonresidential Market

Distribution of construction starts activity by sector, 2008 (\$ of construction value)

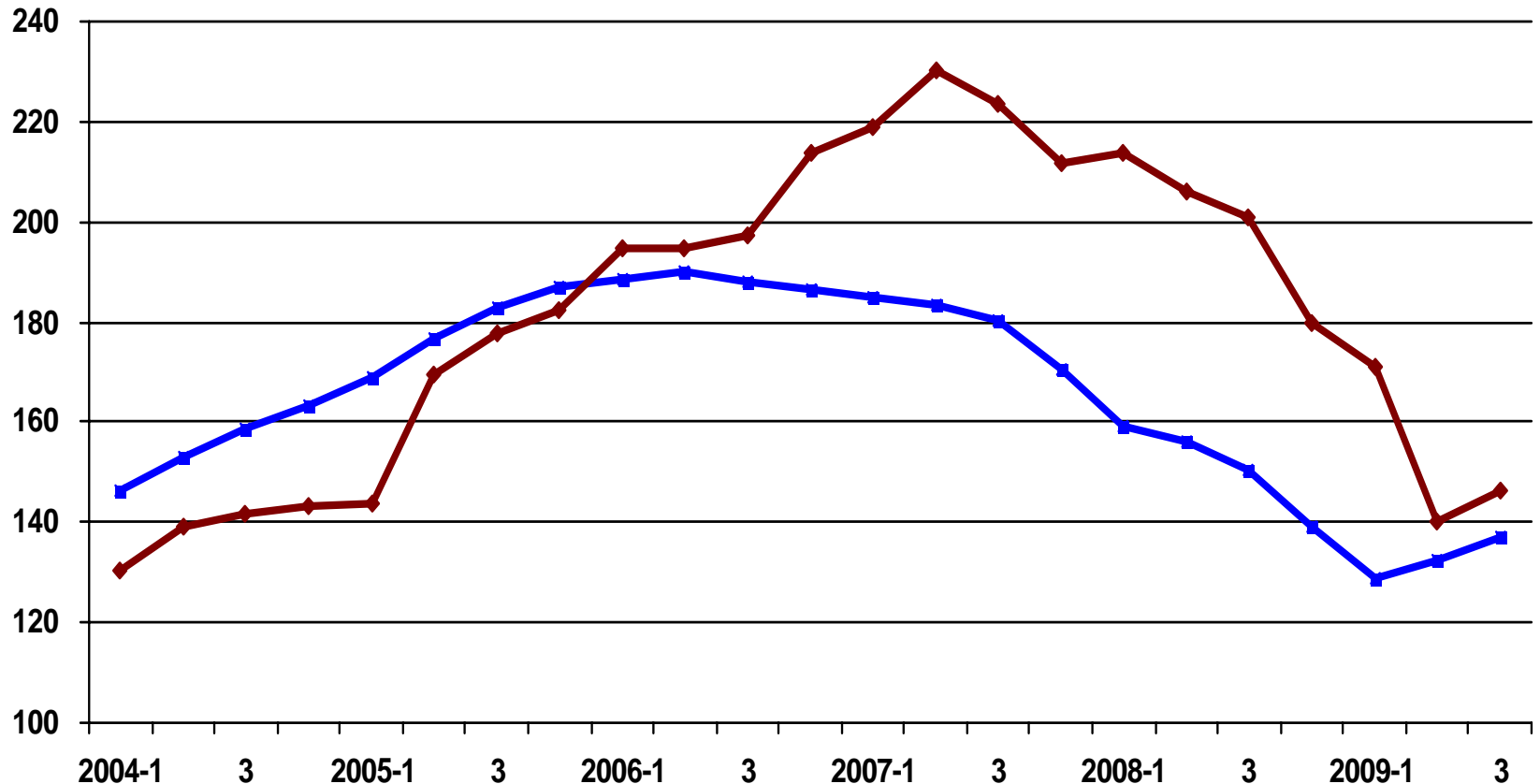


Source: McGraw-Hill Construction



Commercial Property Values Have Fallen Further Than House Prices Nationally, and May Have Not Yet Hit Bottom

Index: January, 2000=100 for house prices; December 2000=100 for commercial property values

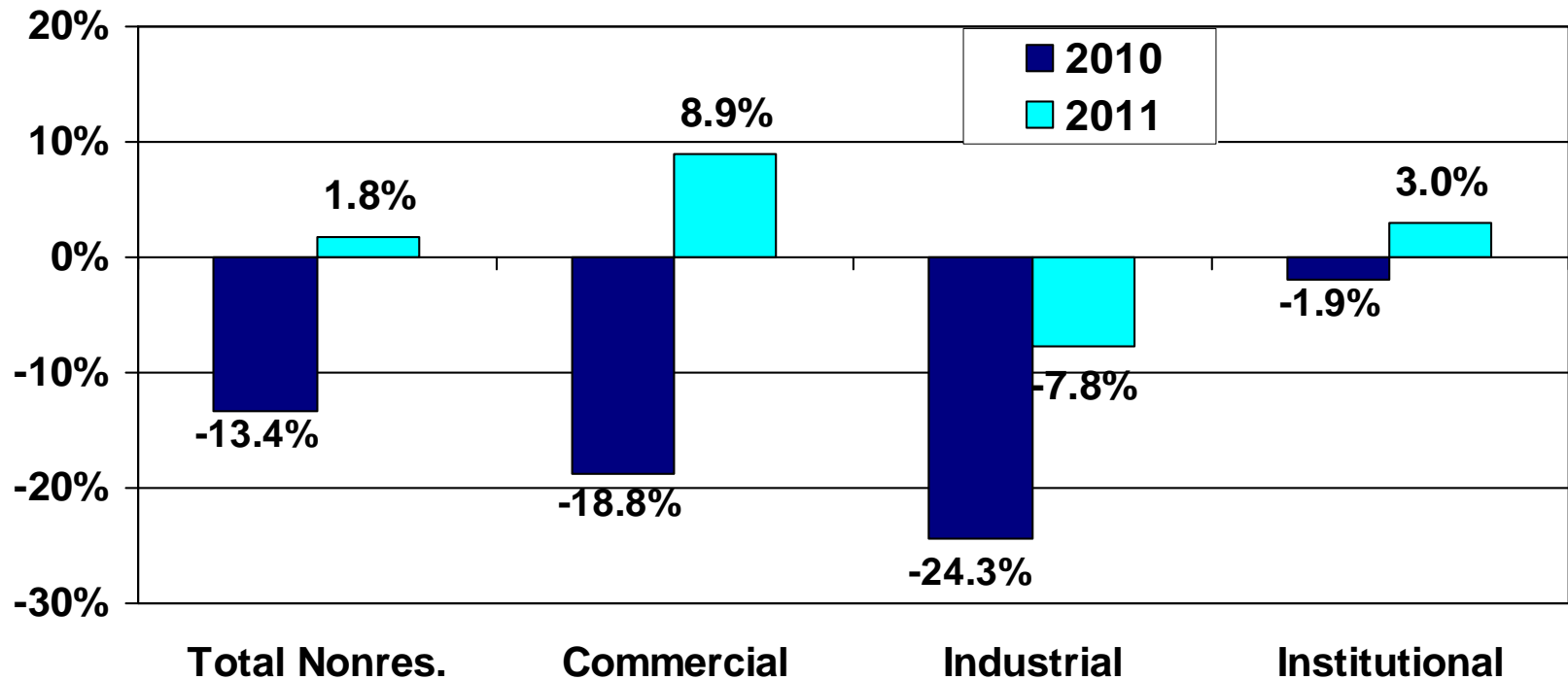


Sources: S&P Case-Shiller National Home Price Index; MIT Commercial Property Price Index



Another Weak Year for Nonresidential Construction Before Recovery Begins in 2011

annual % change; inflation-adjusted \$



Source: AIA Consensus Construction Forecast Survey for 2010 and 2011 conducted in Nov., 2009.



Office Vacancy Rates Lowest in East Coast Markets

(Third Quarter 2009)

Lowest Metropolitan Vacancy Rates

- Manhattan 9.1%
- Honolulu 10.3%
- Washington, D.C. 11.2%
- Cambridge 12.8%
- Nashville 13.3%
- **Boston 14.2%**

Highest Metropolitan Vacancy Rates

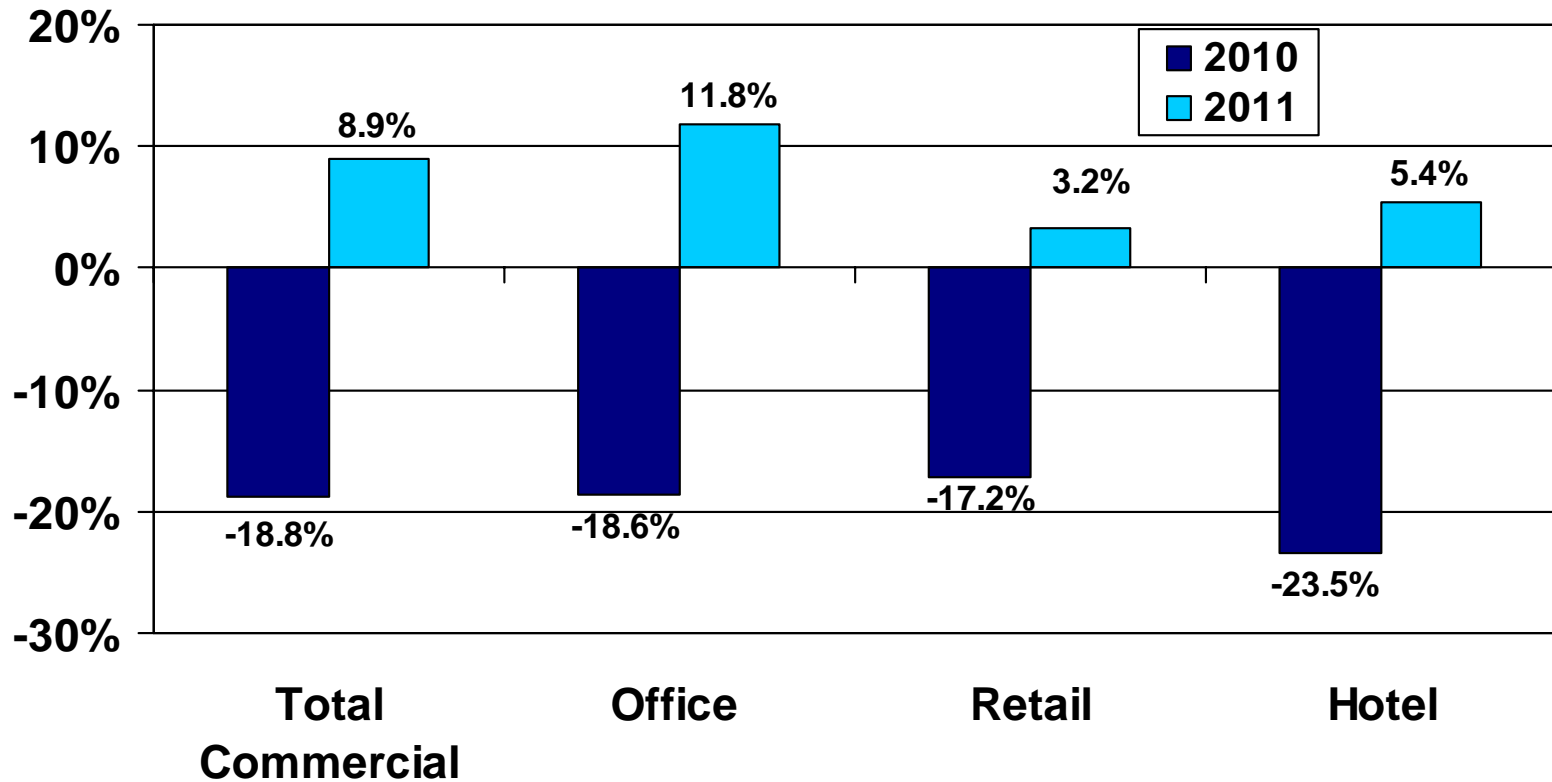
- Detroit 28.5%
- Austin 24.9%
- Inland Empire (Ca) 24.7%
- Palm Beach Co. 24.7%
- Ventura Co. 24.3%

Source: CB Richard Ellis



Commercial Outlook: Steep Declines Projected to Continue Through 2010 for All Major Sectors

annual % change; inflation-adjusted \$

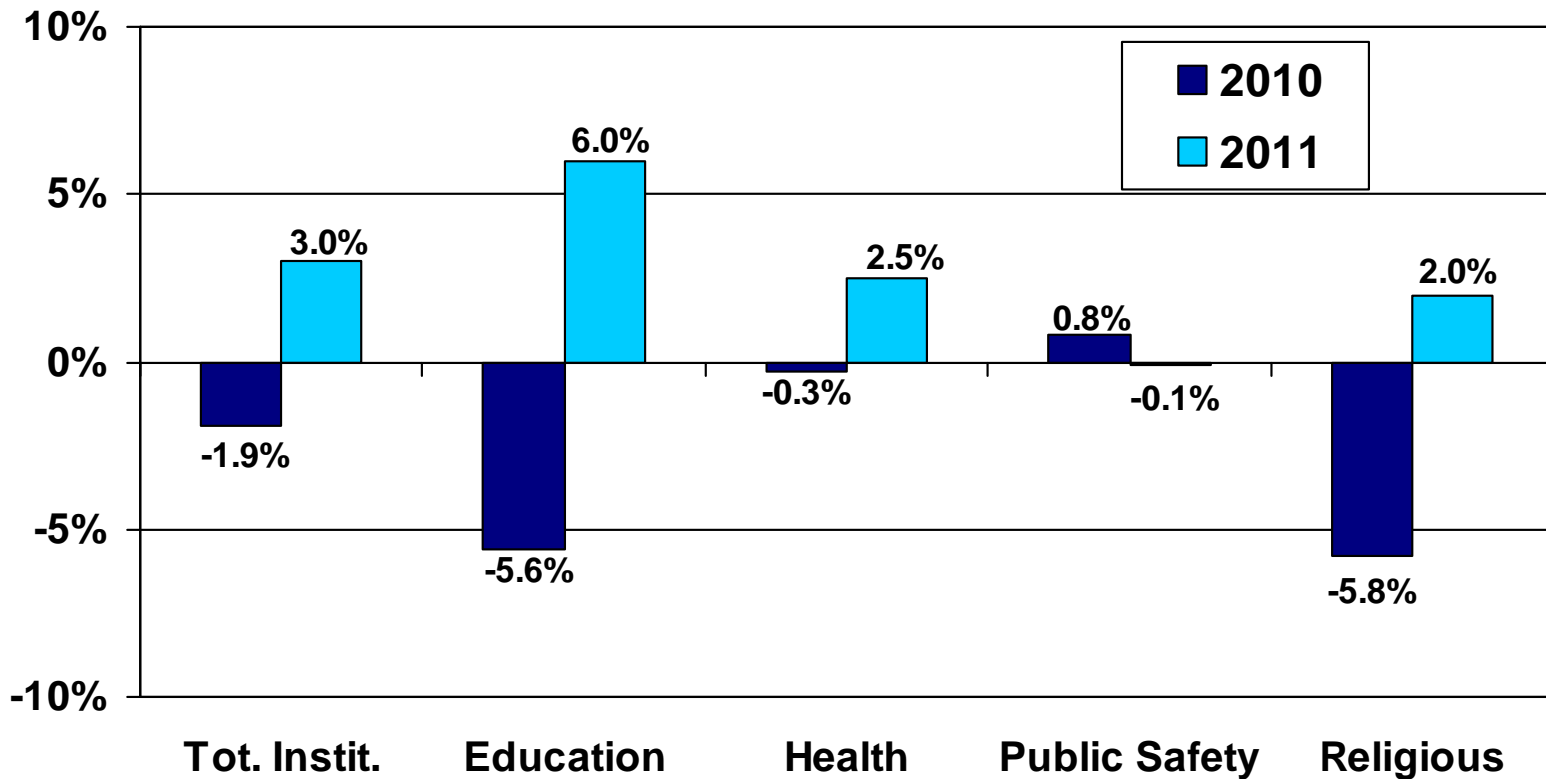


Source: AIA Consensus Construction Forecast Survey for 2010 and 2011 conducted in Nov., 2009



Most Major Institutional Categories Expected to See More Modest Downturns in 2010

annual % change; 2000\$

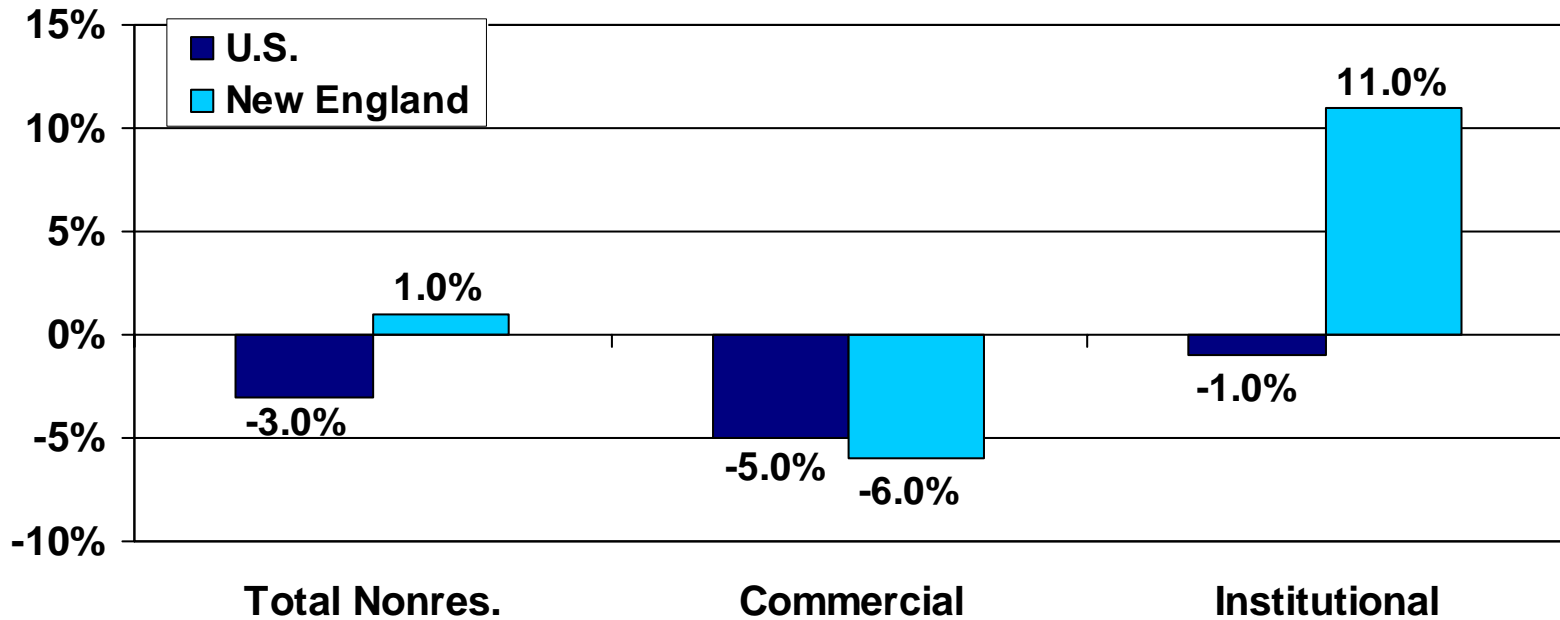


Source: AIA Consensus Construction Forecast Survey for 2010 and 2011 conducted in Nov., 2009



Construction Starts Expected to Rebound Stronger in This Region Than Nationally

annual % change; square footage of construction, 2010



Source: McGraw-Hill Construction.



All Business Cycles are Different, But Typically Unfold in a Similar Manner

Timing of beginning of recovery for selected economic indicator

| Recession Period | Stock Market | GDP | Payroll Employ. | Nonres. Const. Starts |
|--|---------------------|------------|------------------------|------------------------------|
| 1981-1982 | 1982-Q2 | 1982-Q4 | 1982-Q4 | 1982-Q4 |
| 1990-1991 | 1990-Q4 | 1991-Q1 | 1991-Q3 | 1993-Q1 |
| 2001 | 2001-Q4 | 2001-Q4 | 2003-Q2 | 2003-Q3 |
| 2008-2009 | 2009-Q1 | 2009-Q3(?) | ? | ? |
| Average Duration from Prior Benchmark | | 2 Quarters | 3 Quarters | 2 Quarters |

Sources: Dow Jones, U.S. Dept. of Commerce, U.S. Dept. of Labor, McGraw-Hill Construction.

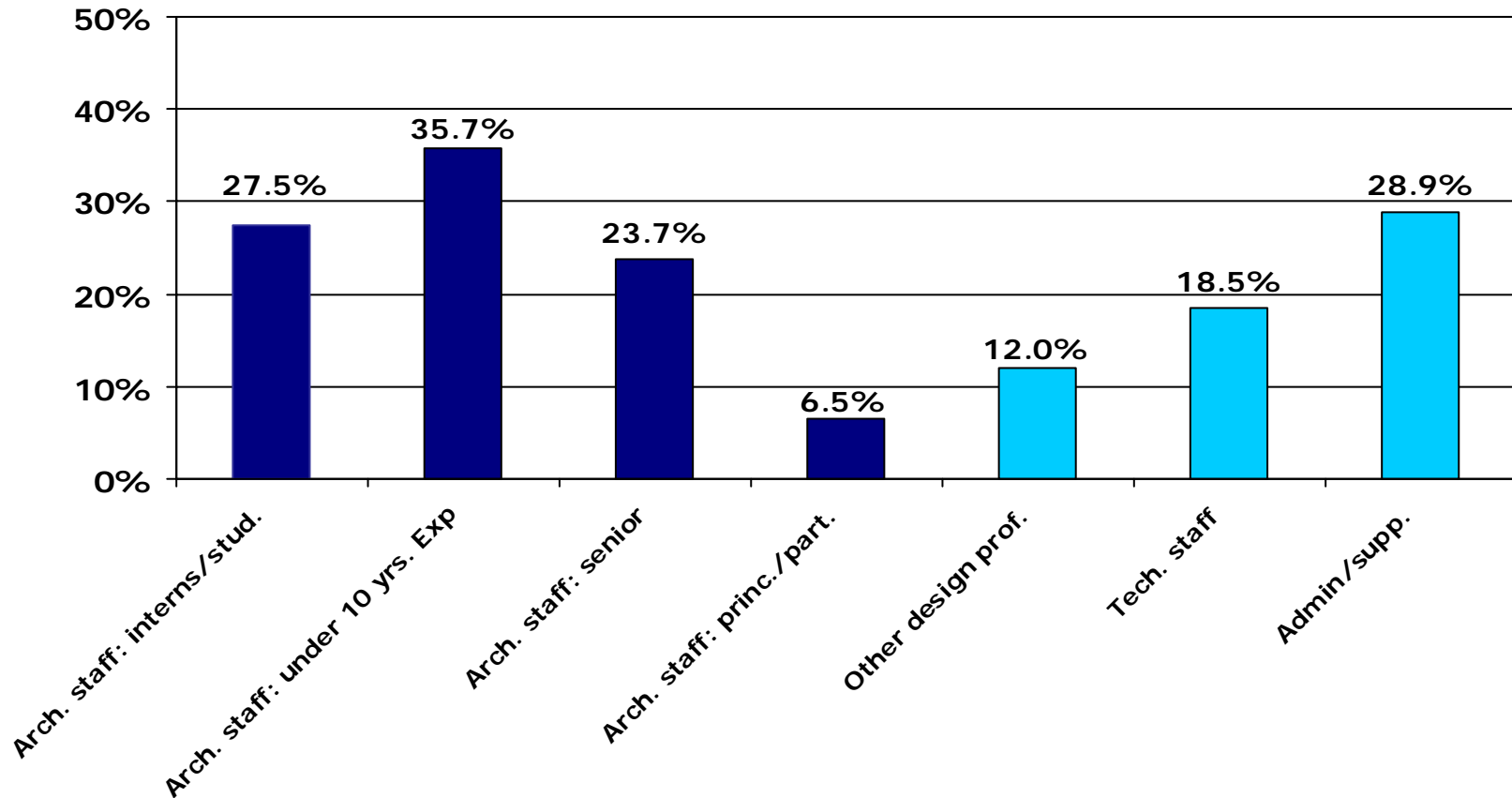


Trends influencing the Design Professions and Construction Industry

- Potential loss of future generation of architects
- Continued industry concentration and consolidation

Job Losses Widespread, but Have Hit Less-Experienced Architectural Positions the Hardest

Share of firms that have reduced staff by positions



Source: AIA Work-on-the-Boards Survey, November 2009

Larger Architecture Firms Account for Large Share of Activity in Profession

share of total staff and billings in the profession in 2008 at all firms by firm size

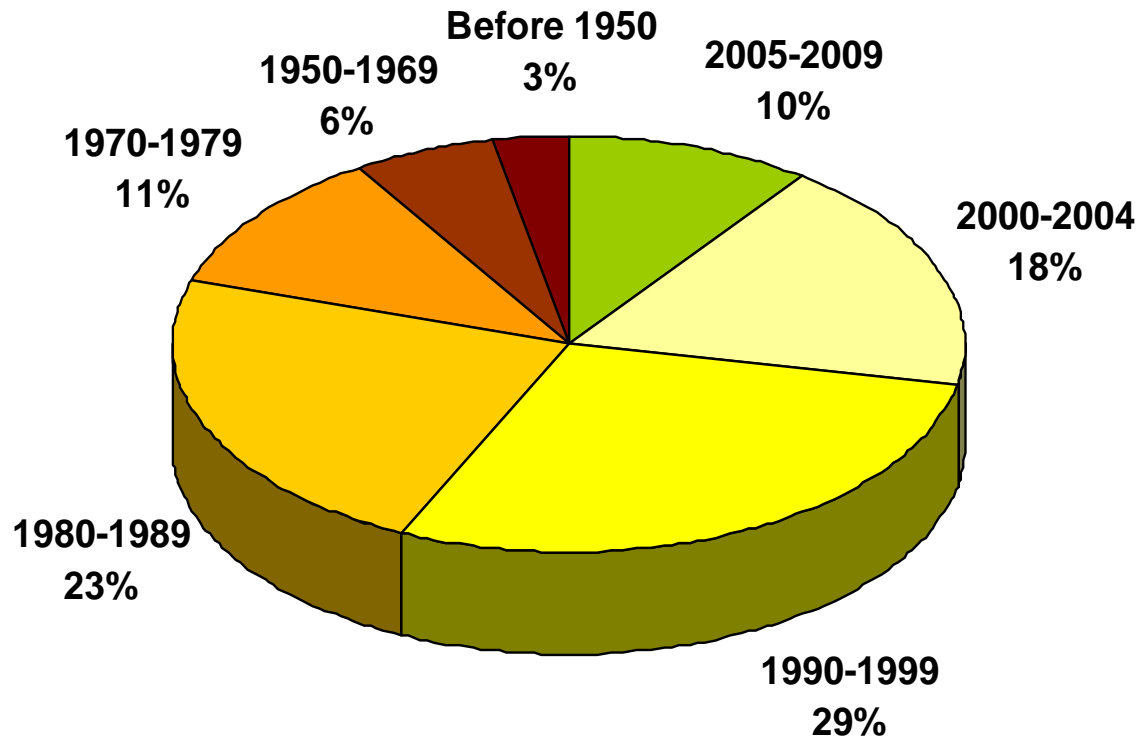
| Firm size (#emp.) | Share of Firms | Share of Staff | Share of Billings |
|----------------------|-------------------|-------------------|----------------------|
| 1 | 24% | 2% | 1% |
| 2 to 4 | 37% | 10% | 6% |
| 5 to 9 | 18% | 12% | 7% |
| 10 to 19 | 11% | 14% | 12% |
| 20 to 49 | 6% | 18% | 23% |
| 50 to 99 | 2% | 14% | 15% |
| 100 or more | 2% | 30% | 36% |

Source: The American Institute of Architects - *The Business of Architecture*, 2009.



Churning of Firms Means Majority Relatively Young, Keeping the Profession Fragmented

Year of formation, % of firms



Source: The American Institute of Architects - The Business of Architecture, 2009.

Summing Up

- Design firms approaching two years of a very sharp downturn; steepest declines in commercial/industrial categories. Current downturn shaping up to be as serious as any of the past 50 years.
- 2010 projected as another weak year for the nonresidential construction industry. Extent of weakness depends on success of federal economic stabilization measures.
- Key issues facing the profession deal with future consumer demand, creating opportunities for younger professionals, and consolidation in the profession.