

May 20, 2004

## **MEMORANDUM**

**Re: Current Bid Climate**

**To Our Valued Clients and Friends**

As most of us realize, construction costs are rising at an alarming rate. It is similar to the escalation we saw in 1995-96 when the San Francisco Airport Project and the Port of Oakland jump-started a major construction growth in California, right after the recession of the early 1990's.

### **Escalation:**

In an effort to help you understand what is happening; we have identified the following factors which have impacted the current bid climate, i.e. construction costs. We can understand the normal amount of escalation related to construction materials and labor. However, the escalation we are seeing is beyond that and is prompted by several factors.

One of the predominant issues in the rise in construction costs is the amount of construction taking place in California right now. New construction appears to have become the "mainstay" of the California economy. There is a glut of construction projects. In the McGraw Hill database for Northern California (48 Counties) in the first quarter of 2004 shows over 600 projects over \$5,000,000 in Northern California. These projects are in pre-planning through construction. There are 125 new projects in pre-planning in the past month with construction budgets over \$5,000,000. These projects represent areas, commercial, medical, leisure, educational, retail, and industrial.

*In other words "Supply and Demand"-- there are many more projects on the books, both public and private than there are contractors to do the work, i.e. contractor's are controlling the market Some contractors have a work backlog for two years out and have to bid high to cover additional unanticipated expenses for a project.*

### **Additional factors:**

- Labor costs have increased over 6.4% since January 2003. Over 1,500,000 new construction jobs have been created in the State within the past three years. Most of the jobs created are unskilled labor jobs, the trades requiring skilled journeymen are still short handed.
- The worker's compensation insurance has added \$.50 - \$1.00 per hour to labor costs depending on the trade.
- In addition to the worker's compensation problems, contractor's bonding and liability insurance has risen dramatically, almost doubling for some small contractors.
- Basic materials have increased from January 2003 with an overall average price increase of 4%.
- Additionally, to those increases, we have seen shortages along with price increases in several key construction materials, just since the first of the year.
  - Steel, structural steel, rebar, pipe, etc. – Up 30% - delays to 90 days

- Copper piping and copper wire – Up 10% - 15%
- Metal studs – Up 25% in March, 25% in April, plus 5% each month until December -- Delays to 6 weeks  
*Raw materials on the commodities market is high and not showing a decrease which in turn will keep the metal prices up.*
- Concrete – Up 5% in January – Up 5% in June – delays to 30 days
- Lumber – Up 15%
- Oil products, pipe, asphalt, tar, etc.-
- With diesel and gasoline hitting all time highs, the cost to transport materials has increased the price of materials about 1% to 1 ½%.

There have been some discussions on establishing some pricing indexes for steel. There may also come some indexes for petroleum products and cement also.

The inflation factor for the past several years has not been too erratic, averaging 3%+. As for projects coming in the next year or two, we anticipate an escalation factor of 6%.

This situation simply amplifies the best-known way to get the lowest bid – attract as many pre-qualified contractors to bid each project. One resource shows: the variance costs from a base cost can be:

1 bid	+15% to +40%
2 – 3 bids	+8% to +12%
4 – 5 bids	-4% to +4%
6-7 bids	-7% to -5%
8 or more bids	-12% to -8%

The more general contractors and sub-contractors bidding a project create a more competitive atmosphere and better numbers.

### **Summary**

The State just passed a \$12 Billion education bond, plus the numerous local school district and community college bonds that passed. The State has ongoing school construction from the previous school bonds.

There are ways we can be **proactive** to slow down the escalation in bidding.

- If you have a project coming out to bid, make sure the estimate is current, i.e. within the last 30 days.
- Solicit and pre-qualify contractors/sub-contractors that could bid the project and communicate with these pre-qualified firms.
- Do not just advertise - personally call, visit or somehow contact as many contractors as possible to maximize the number of bidders and sub-bidders on a project.
- Let the contractors know when the project is coming out for bid.
- Allow enough time for the contractor to bid a project – 3 weeks minimum.
- Watch for other major projects which are bidding at the same time – try not to put bid submittal dates and times close with other large projects -- the middle of the week tends to have fewer bid deadlines.

There is not going to be a quick fix, this situation may last six months or six years,. The one thing we are sure of is that escalation will continue – and we need to plan for it.