

## Looking back at 2007

### Looking back at 2007 with an eye toward 2008

Now that we have closed the file on 2007 and begin a new year, I thought this would be a good time share some observations from the past year. Calendar year 2007 was an interesting year as backlogs were relatively strong, most construction firms were profitable, and the non-residential construction market continued to run strong. However, 2007 also brought with it increased competition and a trend toward lower profit margins. All-in-all it appears to have been a successful year for the non-residential construction market but some darker clouds began to form during the second half of the year.

Below are some of the most common observations from 2007:

- Competition &ndash; A trend in the second half of 2007 was clearly longer bid lists on public work construction projects. Along with this increase in competitors came a general trend toward lower profits being built into projects. With a slowing in the residential market resulting in more firms bidding public work projects it became a challenge to maintain desired profit margins and still secure enough work to maintain a healthy backlog.
- Cash Flow &ndash; In general, maintaining healthy cash balances and staying out of interest bearing debt was a little challenging in 2007. This however was a result of both some positive and negative trends. On the positive side some firms have been able to build up strong backlogs via negotiated work and/or success in the low bid market. This increase in backlog and ultimately revenue put some stress on cash flow as money was tied up in both receivables and retainages. On the negative side, some contractors have seen days receivables outstanding become significantly longer. Many firms that have been involved in residential construction have experienced this difficulty. The non-residential side has not been immune to this problem but not as significant.
- Personnel &ndash; The ability to hire and retain quality personnel continues to be a challenge. Firms have been getting a little more creative in structuring compensation and benefit plans to keep key personnel. The ability to find and hire qualified people, both administration and field personnel, continues to be a challenge in our industry.
- Project delays &ndash; In certain sectors of the construction industry project delays have become an increasingly significant issue. This had a negative effect as overheads have been built up to support a certain level of revenue but due to delays these levels were not recognized.
- Plans and Specifications &ndash; This is really nothing new but the quality of plans at time of bid have been leaving something to be desired. This has resulted in bid postponements. In addition, these plans have resulted in some unusual bid results as firms are not always bidding apples-to-apples. Some will bid the plans as they are and anticipate change orders while others have been bidding work anticipating the changes on the front side to cover the plan deficiencies.
- Growth &ndash; While competition is up, profits are tighter, and the residential market has slowed, sectors of the construction market have grown significantly. For the most part 2007 was a year of increased revenues with firms have a generally optimistic view toward 2008.

With that quick wrap up of some 2007 observations, below are some quick thoughts about what we expect to see entering 2008.

- Competition &ndash; This will remain fierce in the low bid market. We anticipate this being especially true in the first part of 2008 as people try to build backlogs. If you have a healthy backlog entering 2008 you may be able to let the hungrier firms fill up on the cheaper work and hopefully see competition reduce and margins to increase.
- Delays &ndash; We think construction delays will continue. The work will be released and built but more diligence is going into the construction loan process. In addition, getting a project from design to construction will also continue to be slow as the quality of plans and specifications will continue to be below desired standards and result in questions.
- Growth &ndash; Calendar year 2008 will likely be another year of growth. State and Federal budgets have earmarked substantial money for construction. The commercial sector, while more diligent, is moving forward with large construction projects. Residential will likely continue to be slow through 2008 but some believe by early 2009 this market will again be building.
- Bond Forms &ndash; In the later stages of 2007 onerous bond forms began to increase in frequency. Unfortunately this trend is likely going to continue and something the construction industry, bond brokers, and surety underwriters need to monitor. Some of the terms and conditions that the obligee's are asking the contractor and surety to accept have been difficult, and sometimes impossible, to consider.

Overall 2007 was a good year for the construction community at large and all indications seem to point to 2008 being a good year as well. However, challenges will present themselves and it will take a strong management team to monitor the horizon and react accordingly to the challenges that will undoubtedly present themselves. Good luck to everyone in 2008!