



## **Concerning the construction COVID-19 cost squeeze...(but a squeeze from 6 feet away) - by Kenneth Wille and Lucas Giacalone**

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Kenneth Wille

Lucas Giacalone

COVID-19 has created volatility in an array of markets across the world, and the construction industry is no stranger to the economic impacts of this pandemic. Throughout the past year, overall construction material costs have increased by nearly 13% but this tells only part of the story. This is largely due to an increasing demand after the significant slowdown at the beginning of the pandemic in mid-2020. With many suppliers slowing production or completely shutting down due to being

labeled “non-essential” businesses, the rapid increase in demand as restrictions were pulled back led to bottlenecked supply chains as suppliers could not ramp up production quickly enough to meet demand. Pair this with trade restrictions, supply chain difficulties for pressure treated chemicals, increased demand due to outdoor restaurant enclosure construction and increased tariffs put on imported goods over the past year, and it is a recipe for massive price fluctuation. On top of the pandemic, in March 2021 a massive cargo ship completely blocked the Suez Canal for six days. Although six days may not seem long enough to seriously impact global supply chains, there has been a domino effect of delays that continually add to product shortages. The Bureau of Labor Statistics published a new producer price index (PPI) study in February 2021, which showed the price increase for some of the most common building materials between April 2020 and February 2021. The PPI for lumber and plywood jumped 62%, the PPI for diesel fuel increased 114% and the PPI for steel mill products rose 20%. These are just a few examples of rising costs with no signs of stopping, and many suppliers are implementing plans to further increase prices periodically.

These rising prices have had the biggest impact on contractors trying to work within a lump sum. If a contractor placed a fixed bid in January 2020, and did not start ordering materials until April 2021, they will have to spend 13% more than was anticipated in their bid. With materials 25% or greater of a contractor’s budget, a 13% increase cuts profit margins by 3.25% or greater and that has not yet even considered other increase such as labor or COVID-19 protocols and distancing. As prices continue to climb, specifically for a variety of steel, lumber, and engineered wood products, contractors are facing larger impacts on their budgets.

Oftentimes, contractors are also responsible for making up lost time and ensuring deliveries come on schedule. In a time where delivery dates are constantly being pushed back, schedule management is becoming vastly more difficult. What we consider the “critical path” is often derailed. If an order for sheetrock is delayed by two weeks, that also means painting and finishing is delayed by two weeks. When all the activities of a construction project are considered together, this leads to massive delays in a project’s overall schedule. On projects with contracts that place the responsibility on the contractor for missed deadlines, penalty costs are accruing per day, which once again pulls profits from the contractor.

While there is no clear-cut solution, it is clear changes must be made to mitigate these price increases and bring normalcy back to the construction industry. When contractors are facing potential losses on a project that typically would bring profits, they become hesitant to bid or increase their pricing drastically. This leads to a cycle of increased prices for owners, riskier loans for lenders, and an overall more difficult and stressful process for all parties involved. Prices will eventually level out, as they always do, but in the meantime, we urge contractors and owners to closely monitor costs and schedules and communicate information more frequently than ever, agree to a timeframe to lock in pricing for material delivery, and consider material increase provisions in contracts to better protect from unexpected material jumps.

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Kenneth Wille, P.E., LEED AP BD&C, is president and CEO, and Lucas Giacalone is a building consultant, with KOW Building Consultants, New York, N.Y.

New York Real Estate Journal - 17 Accord Park Drive #207, Norwell MA 02061 - (781) 878-4540