A small step back

How the construction and real estate industries look going into 2014

INTERVIEWED BY ROGER VOZAR

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Results of the Skoda Minotti annual survey of the construction and real estate industries looked good in 2012, indicating the most positive response since the initial poll in 2007. The 2013 numbers, however, reflect that the local market hasn't completely recovered from the recession.

"Things started to look positive, but it appears we've taken a step backward," says Roger T. Gingerich, CPA/ABV, CVA, CCA, partner in charge of the Real Estate Construction Group at Skoda Minotti. "Business owners are sitting on cash and holding off on capital investments because they're uncertain whether we're in a long, slow cycle of recovery or if we're dipping back into a recession."

Smart Business spoke with Gingerich about the 2013 survey results and the status of the Cleveland-area construction and real estate marketplaces.

What is construction reform and how has it impacted contractors?

Under a 2012 Ohio law, rules for government contracts changed and there is no longer multi-prime bidding — breaking a project into different packages for mechanical, electrical, etc. Instead, the process went to single prime construction, with one general contractor responsible for hiring any subcontractors.

Reform has made it more difficult for smaller contractors to bid for work because they don't have the bonding capacity; they don't have the net worth or capital that a bonding company prefers. They may be able to get a bond for a $3 million project, but not for a larger project, even if they have subcontractors doing the majority of the work.

The concern is that subcontractors have another company — the general contractor — between them and the customer and it takes two or three weeks longer to get paid. There also could be more out-of-state competition because larger contractors see opportunity when there are only so many companies that can bid.

Despite problems, construction companies surveyed were positive about opportunities in the next three years — 43 percent expect more opportunities, 41 percent said the same amount and 16 expect to have less business. Although that's the second best result since the survey started, it is somewhat discouraging that 49 percent of respondents in the 2012 survey saw more opportunities. So we took a small step backward.

Why is securing credit continuing to be a problem with commercial real estate?

When asked about which obstacles prevent closing a deal, credit was the top response and is tied to property valuations. Banks tightened up in 2007 and 2008 and exited the real estate market. As a result, there was more supply than demand for real estate. Properties that were worth $1 million, for example, might now be valued at $750,000, and the owner still owes $800,000.

Loans are still available for businesses that operate out of their buildings; it's the investment real estate that is not being financed. Retail businesses have struggled and companies were going out of business or couldn't pay rent and, if leases were up, wanted to renegotiate for significantly less than what had been paid. As a result, developers are having problems securing loans to get projects off the ground. We've seen some improvement, but there still are challenges when it comes to credit.

Overall, what do the survey results suggest for 2014?

The results weren't surprising. Respondents said healthcare reform would have a negative impact; however, healthcare is going to be a challenge for everyone. The survey also indicated that while everyone seems concerned about green construction and sustainability, it's not changing many developers' minds about how they build.

The fact that we took a step back from 2012 in terms of optimism shows that it's still an uncertain market. That wasn't surprising, although lending restrictions appeared to be lessening.

However, interest rates remain low and it's a great market for business owners with cash. Those people will see opportunities. If you don't have access to capital, you will continue to face challenges and that will slow the area's recovery. ●

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