Texas Construction Industry Outlook for 2006: It Looks Good, But . . .

By Rodney A. Carver

Expect the construction industry in Texas to grow by roughly six percent overall, and at least five percent in all but a few sectors in 2006, unadjusted for inflation. According to the forecast by the Econometrics Group at Decision Analyst in Arlington, only electric power-related and religious sector construction will experience less than five percent growth.

Education, healthcare, transportation, retail, and warehouse construction are among the strongest sectors in the forecast, with projected growth rates in the six percent to 10 percent range. Hospitality and recreation construction should also see strong growth with up to a seven-percent increase for the year.

Recent passage of the state appropriations bill makes the outlook for public projects better than it's been in years. In fact, the 2006-07 budget is almost 20 percent larger than the previous one. Private sector construction also looks favorable. Retail construction, warehouses, hospitality and recreation will be propelled by strong population growth and the fact the Texas economy has begun to outpace national growth. Meanwhile, housing construction should see about 6 percent growth overall, with even more in Houston and Dallas as those cities continue to emerge as secondary immigration gateways. Since Texas hasn't experienced a "housing bubble," the industry here won't be appreciably softened by a general housing slowdown.

Regionally, healthcare construction should be strong in Dallas-Fort Worth (DFW). Fort Worth's very tight office space market should spur construction in Tarrant County, and Alliance Airport continues to attract tech firms. However, DFW's power needs are fast running up against supply, but new power-plant construction is constrained by the area's noncompliance with the Federal Clean Air Act. That presents a huge opportunity for West Texas, however, where a new $200 million gas-fired plant is planned for Odessa, specifically to transmit power to DFW.

Contrary to the overall trend, religious construction has been heating up in Houston. Austin's economy is beginning to rebound after the tech collapse, and apartment construction is especially likely to pick up

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there. Healthcare and bioscience projects will continue to be strong in San Antonio, but the recent glut of industrial space there will take some time to absorb.

The South Texas regional economy will face challenges from the planned closure of Naval Station Ingleside and reductions at NAS Corpus Christi. However, NAS Kingsville is slated to receive $16 million for new construction.

Perhaps the biggest impediment to growth over the next year is the cost of materials. Double-digit increases over the last two years are unlikely to ebb, so costs will be higher in '06, eating away at real growth. Just how much will depend on what combination of prevailing and countervailing forces dominate. For example, plywood is already in short supply in many areas, but Katrina and Rita downed a lot of trees. That stock could increase supply if it is harvested before it deteriorates. Steel prices are high, but Katrina created a supply of steel scrap. Unlike gasoline prices, diesel fuel prices have not retreated since the 2005 hurricane season. Those costs add to the price of materials, but as refineries get back to full production, upward pressure on fuel prices will diminish.

As for concrete, prices already are being affected by damage to Gulf ports, where the nation imports more than a quarter of its cement. However, if the call to reduce or eliminate the huge tariff on Mexican cement is successful, upward price pressure there would be reduced substantially.

So, how much real growth will the industry see in 2006? It depends greatly on growth in the cost of materials, and there are too many uncertainties right now to formulate a confident answer. In the mean time, one of the most frustrating effects for those in the industry is likely to be a wider variance in bid prices due to cost uncertainty and the inability to lock in materials pricing for more than a month or two.

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