




CONTRACTORS UPDATE

A look at the issues challenging Midwest's general contractors

Compiled by Kevin Jeselnik

<h3>HREB CONTRACTOR SURVEY</h3>	 <p>Jeff Raday is founder and president of Rosemont, Illinois-based McShane Construction Corporation.</p>	 <p>Kirk Warden is senior vice president and partner at St. Louis-based Clayco.</p>	 <p>Paul Chuma is president of Deerfield, Illinois-based Meridian Design Build.</p>
<p>1) Where is your company's work most concentrated in the Midwest?</p>	<p>McShane Construction's work within the Midwest is primarily concentrated on projects in a variety of suburban communities and within the city of Chicago.</p>	<p>Clayco is a national real estate, design and construction company with many Midwest projects, especially in St. Louis and the Chicagoland.</p>	<p>The majority of Meridian's work is in Chicago and its collar counties. We perform work regionally throughout the Midwest.</p>
<p>2) Which sector do you see most of your business coming from this year?</p>	<p>McShane's current construction workload represents a balanced mix of projects allowing us to manage economic and cyclical changes within the economy, capital markets and specialized markets.</p>	<p>Industrial, Institutional and Corporate</p>	<p>Speculative and build-to-suit industrial construction is the core of Meridian's business. We have also seen an increase in the number of opportunities to work directly with several manufacturers and food processors.</p>
<p>3) What's the latest construction buzzword in the Midwest?</p>	<p>Green technology and Building Information Modeling (BIM) are two of the latest buzzwords that have gained significant coverage and implementation over the past year throughout the Midwest.</p>	<p>Sustainability and escalation costs</p>	<p>"Green", "LEED" or "Sustainable" are definitely the current buzzwords at industry events.</p>
<p>4) What new services/amenities are your clients asking you to provide?</p>	<p>McShane Construction's project teams are committed to providing input to allow the project to be "designed to budget." Our professionals are often asked to provide input on methods that can be evaluated to maintain the cost of the project within the budget that was initially established.</p>	<p>USGBC LEED Certifications and Real Estate Development with a variety of economic solutions</p>	<p>Most clients now want to at least investigate LEED Certification for their project whether it's new construction, shell & core, or tenant improvements. To be on the forefront of the LEED movement, we have successfully encouraged our project management staff to become LEED Accredited Professionals.</p>
<p>5) What is the biggest trend you're seeing within the green building movement?</p>	<p>Our prospects and clients are frequently requesting that we examine the costs associated with utilizing green technology or green building techniques throughout their project. We are also asked to provide cost evaluations and comparisons to accommodate a LEED-certified facility.</p>	<p>Practicality and visible LEED features</p>	<p>There is a trend towards fast-track priority of projects through municipal entitlement/permitting processes. AIA reported in 2007 that over 90 cities have adopted green building ordinances that mandate green building. This would level the playing field, from a cost standpoint, between owners/developers committed to the concept and those who have not yet embraced it.</p>
<p>6) Does a certain property type lead the way in terms of green building business?</p>	<p>The green movement initially found its greatest usage in the office market. The U.S. Government and municipalities have also adopted green or LEED requirements for new construction projects. With the new LEED-CS (Core and Shell) classification, more industrial projects are able to meet LEED certification.</p>	<p>Not necessarily, but large lab buildings provide the biggest challenges</p>	<p>Government buildings lead the way; in my opinion, the use of public funds, not having the need to generate investor returns and heightened demand for green building by the public, makes LEED implementation easier. Office buildings comprise the largest component of green building type. With the issuance of LEED for Schools, we'll see growth there for the same reasons that make government buildings strong candidates for LEED.</p>
<p>7) What's the latest on construction costs? Is a certain product type more affected than others?</p>	<p>Over the past 4 years, prices for construction materials have risen faster than the consumer price index. From December 2003 to January 2008, construction prices have increased 30.2% compared to a 14.5% increase in the consumer price index. Each construction type relies upon a different mix of materials; such diverse mixes have explained why costs for different construction sectors have diverged in recent years.</p>	<p>All, it has more to do with the specific design and use of materials than property type</p>	<p>Besides the interest in being green, there is a rigorous focus on cost control and long-term value, particularly with build-to-suit clients. On the industrial side, the real estate professionals have advised us that, while costs of land and construction continue to increase, rents are not tightening the ROI, which is continually putting pressure on project viability.</p>
<p>8) What have been the most common measures taken by developers when negotiating rising construction costs?</p>	<p>Following the initial 'sticker shock' if the owner/client has not been involved in a new construction project over the past 4 years, our clients have requested that an aggressive value engineering evaluation be applied to the project to discover ways that costs can be reduced or eliminated.</p>	<p>Try to utilize materials that are more stable like concrete structures over steel. Plan in the budget for escalation. Decrease the construction duration with design/build delivery methods.</p>	<p>Meridian suggests a greater effort towards upfront coordination and planning to minimize the effect of rising construction costs. Commit to long lead items early to lock in pricing and delivery. The prices for steel products are being adjusted approximately every 15 days and the trend is not down. Carefully sequenced construction schedules will result in minimizing the time from commencement to completion.</p>
<p>9) What new industry issue or trend will be a large factor during the rest of 2008?</p>	<p>Green building technology will continue to remain in the spotlight, garnering more and more attention as fuel costs and material costs continue to rise. The high cost of energy will force continued research and development of more energy-efficient materials and supplies.</p>	<p>Third party developer led deals. Concrete structures, "Green" buildings without the official USGBC LEED program but rather independent criteria.</p>	<p>The modified LEED rating systems will be effective January 2009, which may have a substantial impact, as the new system will weight the credits. If there is a cost-benefit distribution to the rating system, it may disrupt the creative, "low cost" model that has been incorporated by several industrial developers to achieve the minimum number of points for LEED Certification.</p>

**HREB
CONTRACTOR
SURVEY**



Hank Bellina is a project manager for St. Louis-based ARCO Construction.



Adam Miller is president of Chicago-based Summit Design + Build.



Mike Uhrig and **Andy McDonell** are project managers for St. Louis-based Brinkmann Constructors.

1) Where is your company's work most concentrated in the Midwest?

Most of ARCO Construction Company's work is centered in St. Louis and Chicago.

Summit Design + Build has completed work in the city of Chicago and the surrounding suburbs. In the future, we are anticipating doing work in southern Wisconsin and Northwest Indiana.

Brinkmann Constructors is based in St. Louis and most of our projects are concentrated in the surrounding metro area, including Illinois.

2) Which sector do you see most of your business coming from this year?

This year, ARCO's business has largely centered on the industrial sector.

We see most of our business coming from the industrial, suburban office and healthcare sectors this year, but continue to have work in the urban condominium market.

Nearly 80 percent of our work is negotiated with repeat clients, most of whom are retail developers. We also see opportunities in the elderly, multifamily sector.

3) What's the latest construction buzzword in the Midwest?

Going green and LEED-certified building have exploded onto the scene recently. We believe design/build can adapt, as it has through the years, to ultimately deliver green projects more cost efficiently.

LEED/sustainability/green buildings are the latest buzzwords in the construction industry in the Midwest.

Cost escalation and energy conservation seem to be on everyone's minds because of rising fuel prices. More and more clients are looking for environmental solutions like LEED certification and the cost advantages of design/build.

4) What new services/amenities are your clients asking you to provide?

Our clients are very concerned with building environmentally friendly projects that are also cost effective. Repeatedly, they request LEED-certified building practices. We have numerous LEED-certified project managers and consultants we engage to meet our customer's needs.

We have not really seen a big change in service or amenities, but clients are definitely looking to have their buildings completed in a shorter timeframe and value engineered to increase efficiencies and reduce costs while utilizing higher quality subcontractors.

We've always specialized in deploying engineering proficiency to overcome development challenges. Our clients continually ask for us to find new and innovative solutions to problems and to improve their projects.

5) What is the biggest trend you're seeing within the green building movement?

Energy efficiency and resource management, both during the building process and in the finished product, have become incredibly in demand in the last few years. Clients want to take over finished buildings that offer sustainable energy usage.

We are seeing buildings designed to achieve high levels of energy efficiency, and incorporating new technologies such as green roofs, geothermal heating systems and solar panels. I also see an increase in local government incentives in the form of tax rebates and credits, and other policies such as expedited permitting and approval for green projects.

More and more owners and builders are becoming better educated as to the actual process of LEED certification for their projects. A few years ago, LEED was not a very widely known term or process. Today it is part of the discussion on almost every project. Developers and owners are now willing to make the additional investment needed to be more environmentally conscious.

6) Does a certain property type lead the way in terms of green building business?

Laboratories and office buildings are on the forefront of green innovations. These buildings are often more expensive to build due to their locations, so the extra expense isn't as much of a stretch.

We are seeing income-producing properties like office buildings lead the way in the use of green technology. Industrial is one of the newest sectors to go green, and I see the sector embracing sustainability due to reduced costs it brings.

Institutional properties (schools and larger owner-occupied office buildings) build for their personal use and see the building's green components as a public responsibility, as well as an investment in lower long-term operating expenses.

7) What's the latest on construction costs? Is a certain product type more affected than others?

It's a problem across the board — everything from material prices to transportation costs have skyrocketed. The changes in the market have really forced us to get creative about how we execute projects so we can stay on-schedule and on-budget. The bright side is, in a limited number of locations hit hardest by the lack of new construction the market has stabilized or has seen a reduction in the higher labor costs we experienced just a few years ago.

The rising price of steel has had a huge effect on the mid-rise commercial and mixed-use building, and the increased price of petroleum-based raw materials has driven up construction costs across the board. No sector is insulated from the volatility of construction costs and raw materials, which forces companies and contractors to evaluate how they conduct and manage their business.

All projects have been affected, but retail development has been struggling with the recent surge in costs. Most of the time, the owners are not the primary occupants of the new buildings, but are leasing them to commercial clients. Once the lease deal is done, it becomes extremely difficult, if not impossible, to increase revenue to offset higher initial construction costs. This reduces the profitability, and therefore, the viability of the project.

8) What have been the most common measures taken by developers when negotiating rising construction costs?

Most people understand the rise in cost because it has become a reality in their personal lives. That makes it a little easier to work with clients and encourages them to contractually commit sooner than later to lock in material pricing that optimizes cost savings rather than running the risk of prices escalating further down the line.

Value engineering is very important and is a large component of our company's client services. Avoiding winter conditions and optimizing the construction schedule also helps to offset the increase in these costs. There have also been definite compromises, in building design and finishes, on behalf of owners that has also helped to keep costs down.

Developers are continually looking for ways to minimize the risk and control rising construction costs. We are purchasing materials early in the project and offering multiple methods of construction that may be a more economical than traditional approaches.

9) What new industry issue or trend will be a large factor during the rest of 2008?

Energy efficiency and LEED® design are here to stay. Accompanying those trends, the industry is going to start seeing the use of more and more alternative materials to help achieve those ends and simultaneously lower project costs.

Green building will continue to grow — it is not a question of whether or not firms should invest in understanding how to produce sustainable buildings, it is how much and how quickly one should invest. The election will also play a huge role in the future of our industry. Construction financing is crucial — banks need to get back to lending.

The largest single issue with project development will be the status of the economy, oil prices and how they affect the retail industry.