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Economics Group

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Construction Spending Edges Higher in July

Total spending rose 0.1% during the month. Residential strengthened, while nonresidential declined. Construction has shown a great deal of resiliency, but economic uncertainly continues to sideline new projects.

Residential Strength Masks Weak Commercial Activity

Construction activity appears to be holding up fairly well relative to other hard-hit industries. Total construction spending rose by 0.1% during July and is down just 0.1% compared to the same month last year. Furthermore, overall outlays through July are running 4.0% ahead of their year-to-date pace. The resiliency on display over the past few months makes sense given the strong start to the year. Moreover, many construction projects were permitted to continue while other parts of the economy were shut down.

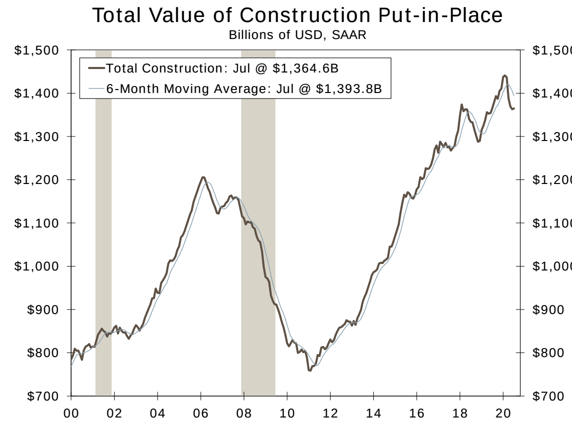
That said, the construction industry has certainly not been immune to the negative impacts of the COVID-19 crisis and total spending remains about 5.3% below February's peak. Similarly, construction employment, which has recovered about 60% of the over one million jobs lost during the lockdown period and is still 5.8% below peak levels.

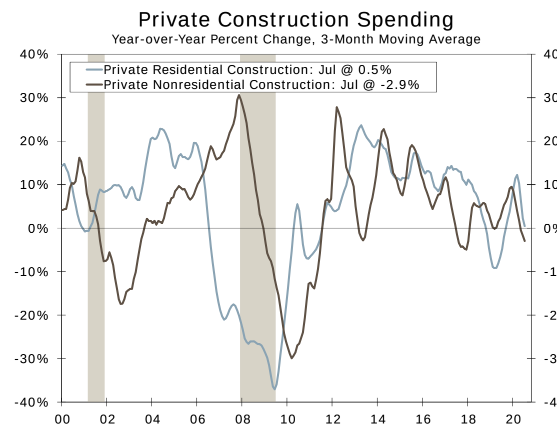
July's positive result was flattered by a 2.1% upturn in residential spending. Single-family and multifamily both gained during the month, rising 3.1% and 4.9%, respectively. We expect the strength in single-family construction to continue, as record low mortgage rates and a renewed desire for a suburban escape has sparked a surge in home buying. Although sky-rocketing lumber prices (up over 150% since April, a consequence of a COVID-19 induced reduction in sawmill capacity and unexpectedly strong builder demand), could potentially constrain single-family activity in the months ahead.

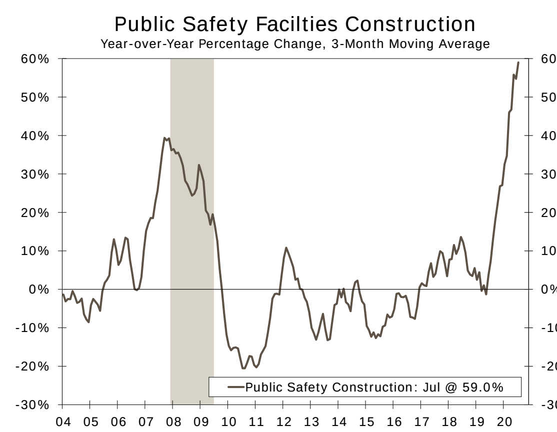
Nonresidential spending dipped 1.2% during the month, as the uncertainty surrounding when close-contact commercial activity (such as at retailers and offices) will return to normal continues to weigh heavily on construction. The declines were centered in commercial (-2.9%), healthcare (-2.8%), educational (-2.6%) and lodging (-2.0%) subcategories. Office construction fell 0.4%, while transportation outlays slipped 0.3%. Some areas have been lifted by the effects of the pandemic. The boom in online shopping has bolstered warehousing construction, which is up 20.2% over the year.

Public sector spending declined 1.3% during July, but expenditures are up 5.1% over the year. Public outlays have waned in recent months, as many summer projects were pulled forward into the spring when there was less traffic on the roads. Highway & street spending weakened 3.1% while education fell 3.0%. Public safety projects, including police stations and detention centers, have surged 57.2% over the past year. With tax revenues decimated, some further pullback in public spending is expected.

Overall, the path forward for construction looks to be forked. Residential activity will likely continue to strengthen as builders try to catch up with blistering homebuyer demand. The recent strength will add to what already looked like a mammoth Q3 rebound in residential investment and real GDP. On the other hand, heightened economic uncertainty will likely prevent many nonresidential projects from moving forward.







Source: U.S. Department of Commerce and Wells Fargo Securities

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