

A photograph of a large-scale construction project. The image shows the interior of a building under construction, with a complex network of steel trusses and beams forming the roof structure. The walls are made of concrete, and the floor is a flat concrete slab. Three construction workers wearing hard hats and high-visibility vests are standing in the foreground, looking towards the structure. The lighting is bright, suggesting a sunny day. The overall scene is one of active construction.

# Construction Delivery Outlook

Q3 2023

**LGE** | DESIGNBUILD

# What We're Seeing Now.

At LGE Design Build, we understand the ever-changing landscape of the commercial real estate and construction industries, and we're committed to keeping you informed about the latest developments.

In the Dallas-Fort Worth Metroplex, construction has experienced remarkable growth, particularly in sectors like healthcare, education, and immersive entertainment venues. Tenant improvement projects are on the rise, reflecting a growing demand for customized office and industrial spaces. As the Texas Triangle continues to expand, linking urban centers like Austin, Dallas Fort Worth, Houston, and San Antonio, presents both opportunities and challenges for state authorities. From Q3 2022 to Q3 2023, LGE has seen building costs decrease an average of 10%, while sitework and electrical costs have remained stagnant or presented slight increases.

In Phoenix, rising interest rates and brief unfounded concerns over water supply shortages have influenced the real estate market. Although there's a measured slowdown, Phoenix remains in the top 10% of the market, with net rent increases of 137%. The construction sector thrives, driven by multiyear manufacturing plant projects, yet a shortage of skilled workers persists, impacting construction costs.

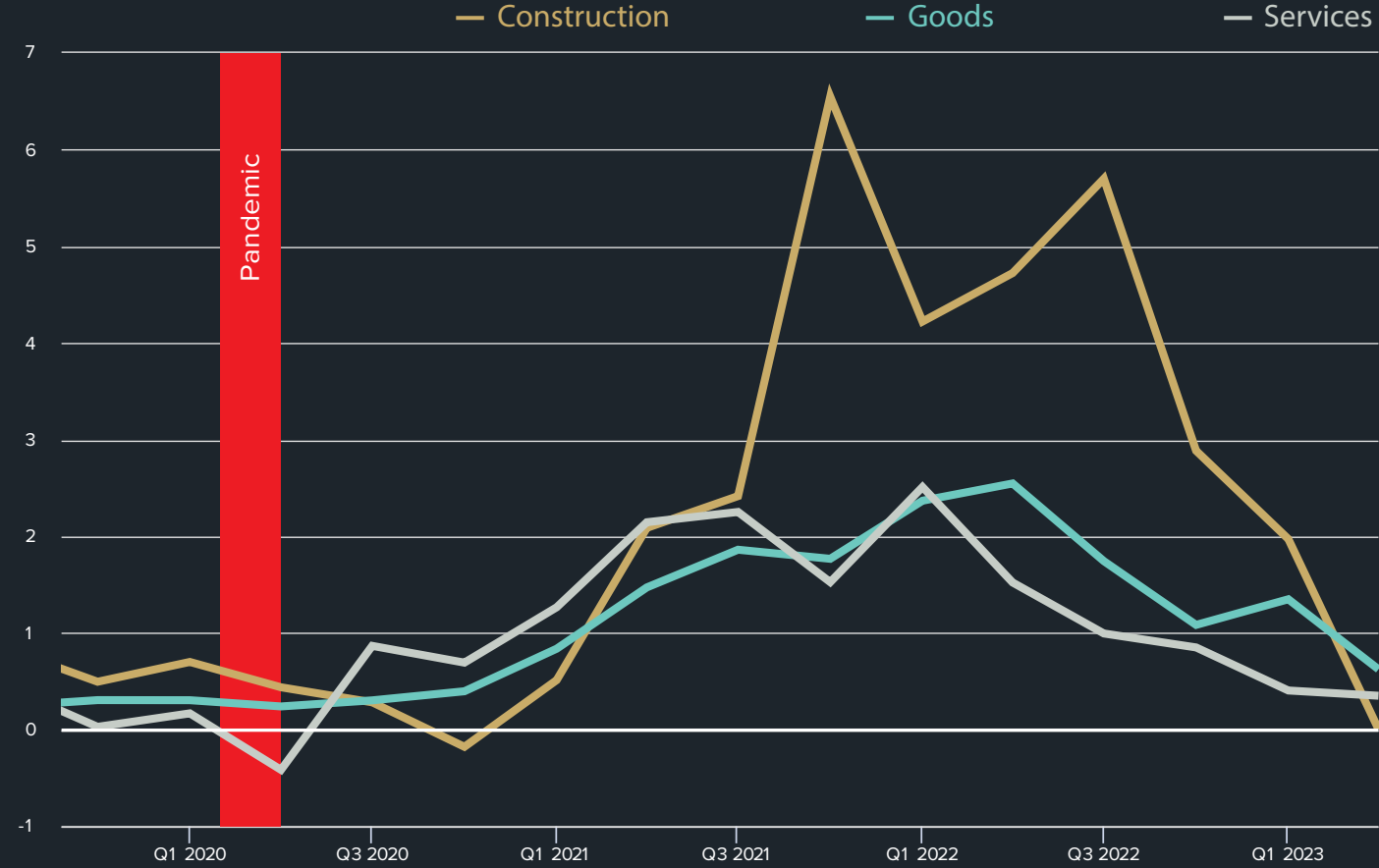
Both markets continue to face unique challenges and opportunities. We're closely monitoring economic conditions, supply chain disruptions, material pricing, and inflation, as these factors play a crucial role in shaping the commercial real estate landscape. Stay tuned for further insights from LGE Design Build as we navigate these dynamic markets together.

– Blake Wells  
Vice President of Preconstruction

# The 'Why' Behind Cost and Duration

Our mission is to provide you with the latest insights into market trends and conditions. This report is a valuable resource, offering comprehensive data that not only answers the 'Why' behind current market conditions but also outlines their impact and proactive strategies to prepare for the future. With a particular focus on the design and construction sectors, this report equips us with the knowledge needed to enter the market with confidence and readiness in Dallas and Phoenix.

## PRODUCER PRICE INDEX FINAL DEMAND CONSTRUCTION



Percent change in Producer Price Indexes for final demand, January 2020 to August 2023.

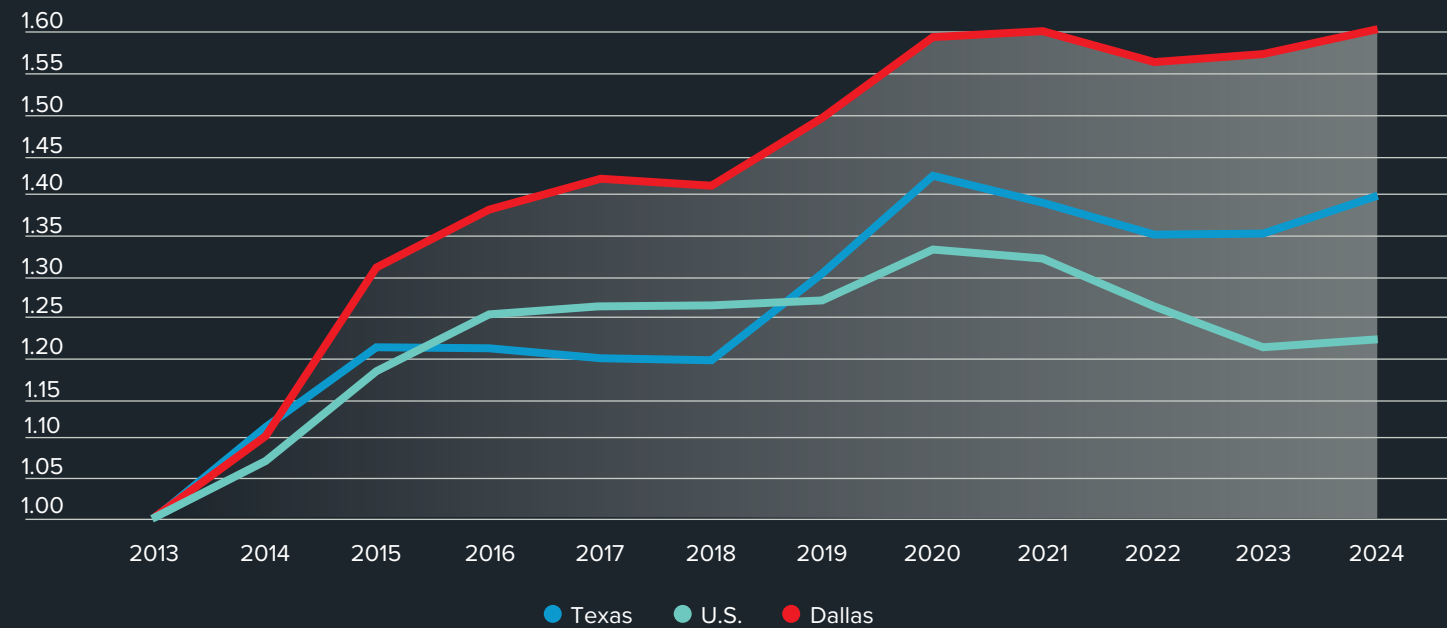
We realize the market is always changing unpredictably. The information contained in this report is using the most up-to-date data available as of August 2023.

# Demand for our Core Markets

## DALLAS:

In the Dallas-Fort Worth Metroplex, construction has flourished in recent years, driven by sectors like healthcare, education, and entertainment. Noteworthy is the escalating popularity of the tenant improvement market, indicative of the growing desire for personalized renovations in office and industrial spaces. As the Texas Triangle (formed by the states four main urban centers, Austin, Dallas Fort Worth, Houston and San Antonio) experiences rapid expansion, characterized by outward growth due to the region's flat landscape, the task of interlinking these communities poses a significant undertaking for state authorities but boasts high probability for new projects on the horizon. As of July 2023 construction spending for Dallas Fort Worth remains at 1.57 well above the national level of 1.22.

CONSTRUCTION SPENDING INDEX 2013-2023

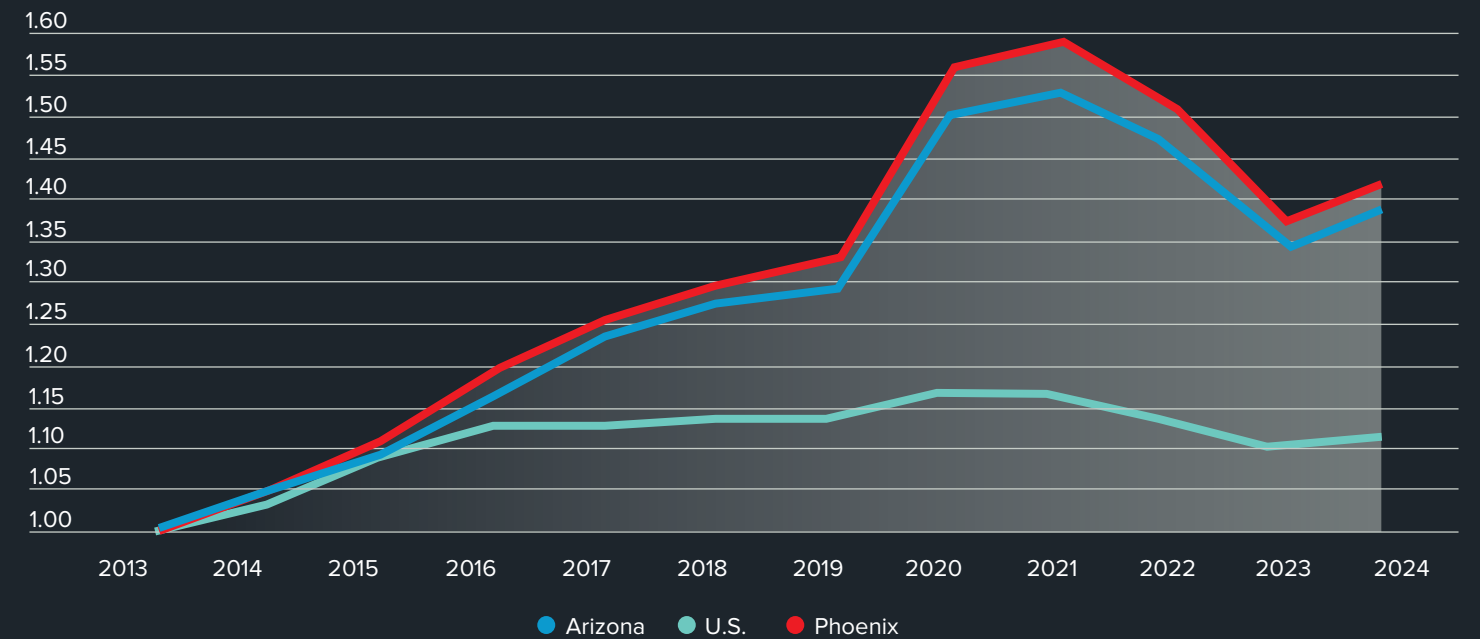


## PHOENIX:

The recent increase in interest rates has had a moderating effect on the Phoenix real estate market. Concerns about water supply shortages have led to some restrictions on residential and commercial properties, which could further dampen the market in the short to medium term. The business is moderating at a slow pace but is still in the top 10% of the market with net rent change up 137% in Phoenix.

The construction market in Phoenix is being driven by the establishment of several large, multiyear manufacturing plants. This growth has also contributed to an expanding labor market, but there is a shortage of qualified skilled workers, both in blue-collar and white-collar positions, which is keeping construction costs high. Despite this, the economic outlook has improved since late 2023. Construction spending seems to be on the rise in Phoenix and is currently at 1.74 and is projected to rise to 1.85 by end of the year.

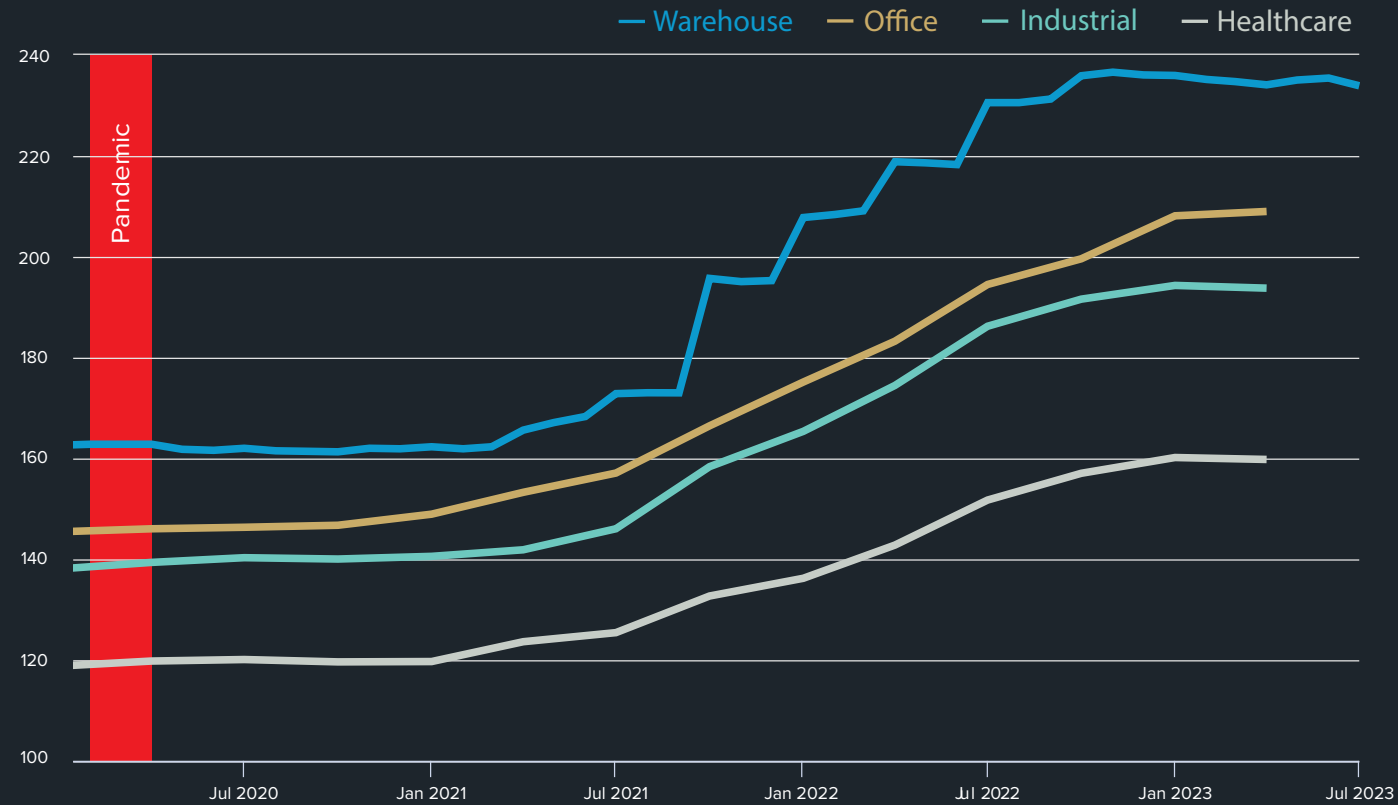
CONSTRUCTION SPENDING INDEX 2013-2023



# Demand by Product Type

## NEW BUILDING CONSTRUCTION

PERCENT CHANGE. QUARTERLY



Despite a nationwide slowdown in mega warehouse deals for e-commerce and logistics companies due to the Covid-19 pandemic, Phoenix's industrial market continues to be driven by those same sectors. The region has surged to the top of the industrial ranks, fueled by the current manufacturing boom and companies relocating from California. In June 2023, the Phoenix metro had an impressive 58 million square feet of industrial space under construction, accounting for about 16.6% of the existing inventory and surpassing supply pipelines in other major regions like Dallas-Fort Worth and the Inland Empire.

Despite a peak in the pipeline in Dallas last quarter, the Dallas-Fort Worth industrial market remains at the forefront of national development activity, with occupier demand for the first half of 2023 surpassing pre-pandemic levels after consecutive record-breaking years.



Positive absorption in CBD (Central Business District) submarkets hit hard during the pandemic suggests a potential urban core recovery. The prime South Scottsdale submarket showed significant occupancy growth, with 198,509 s.f. net absorption, favored for its location and workforce. Although average direct rents are stable quarter-to-quarter, they have increased by 3.5% YoY across the valley. While return-to-office trends are emerging nationally, the future of office spaces remains uncertain due to elevated interest rates, impacting landlords and occupiers. Amid economic challenges, the Phoenix market remains resilient.

Dallas' direct asking rents surged to \$34.14 p.s.f. in Q2, reflecting a 3.2% YoY growth. Far North Dallas and Las Colinas are grappling with high sublease availability, while Class A properties saw a 1.2% overall YoY decline to 8.3 million s.f. Despite rising national and local office vacancy rates, the disparity in performance since 2020 has led older assets to bear the brunt, with 90% of the market's vacancy concentrated in just 35% of existing buildings. Leasing activity dropped by 27.6% YoY due to a delay in large-scale deals, but Dallas still ranked among the top five markets nationally.

## U.S. OFFICE REAL ESTATE STATISTICS

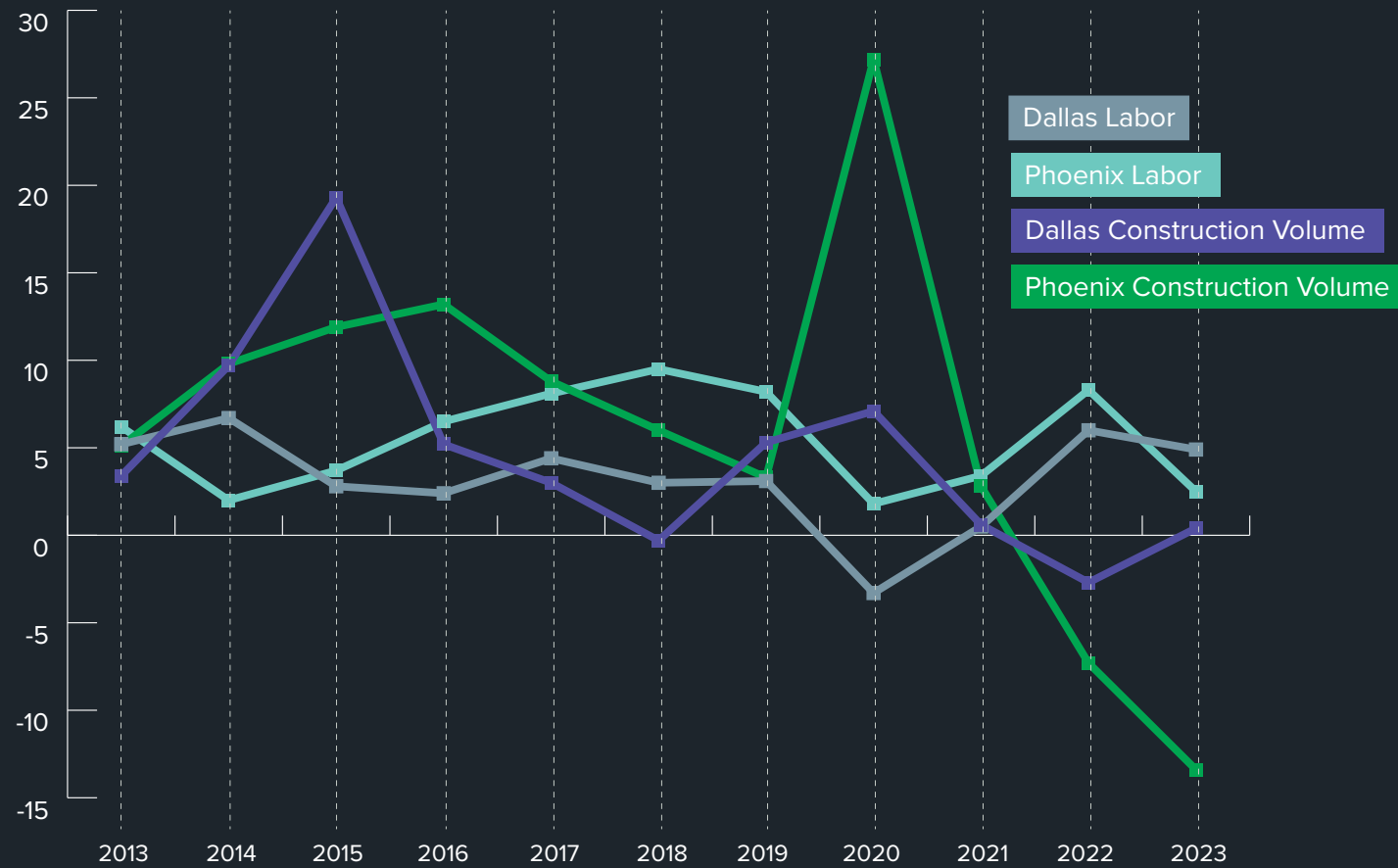
	National Average	Class A	Class B	12-Month Rent Growth	12-Month Net Absorption	12-Month Delivered Construction	Average Sales Price per SF
Vacancy	13.2%	18.4%	11.8%	0.9%	45.5M SF	\$85.7M	\$310 PSF
Rent	\$35.19	\$45.03	\$30.70				

# Construction Labor

The construction industry's persistent labor and skills shortage isn't expected to resolve itself in the near future. Contractors are grappling with substantial demand for large-scale projects like chip manufacturing plants and clean energy facilities, all while facing a scarcity of younger talent entering the skilled trades. As of Q2 2023, the situation in Phoenix shows a 2.3% increase in labor availability, but construction volume has declined by -13.4%, significantly alleviating the strain on the labor pool. In Dallas, a similar scenario is observed, with labor increasing by 4.9% and construction volume rising 0.4% above its 2022 low of -2.7%.

## CONSTRUCTION VOLUME VS LABOR

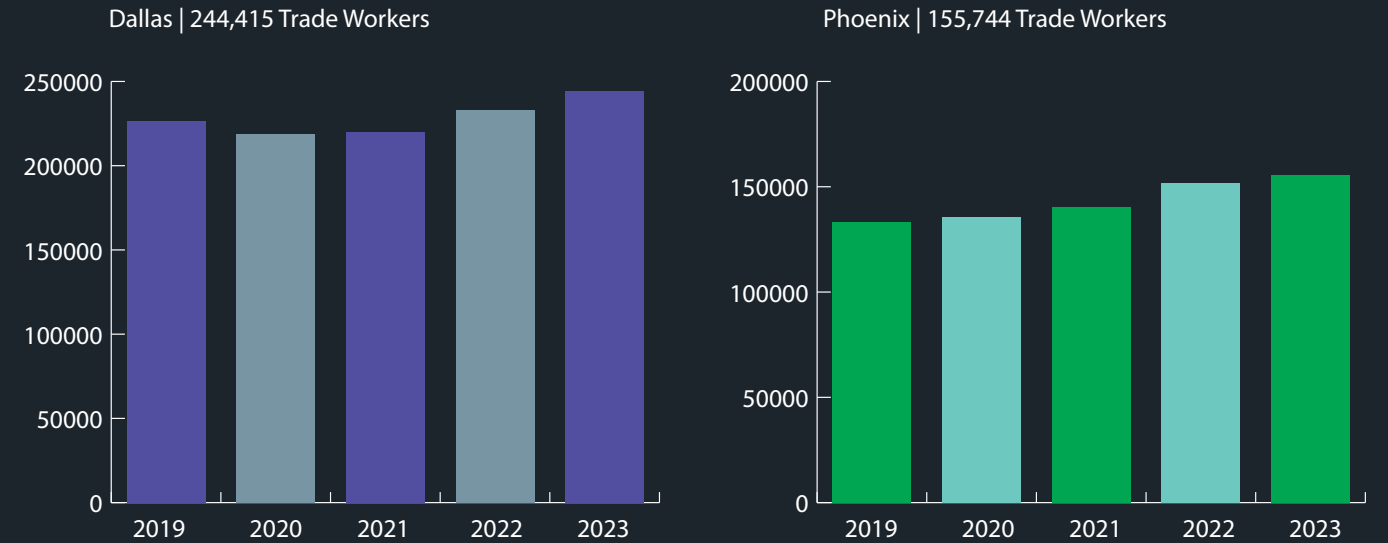
ANNUAL INCREASE/DECREASE



Note: Residential is the driving factor for construction volume decrease.

## REGIONAL CONSTRUCTION EMPLOYMENT

TRADE WORKERS



### DALLAS:

Despite fewer construction starts this year, Dallas leads in adding construction jobs. Dallas added 11,600 building sector jobs in the year ending in May – the most in the US, according to the Associated General Contractors. Construction employment in Dallas was 8% higher in May than a year before. This growth in construction jobs happened even as North Texas commercial and residential building starts slowed this year, with Q1 seeing a 23% decline in Dallas-Fort Worth commercial building activity.

### PHOENIX:

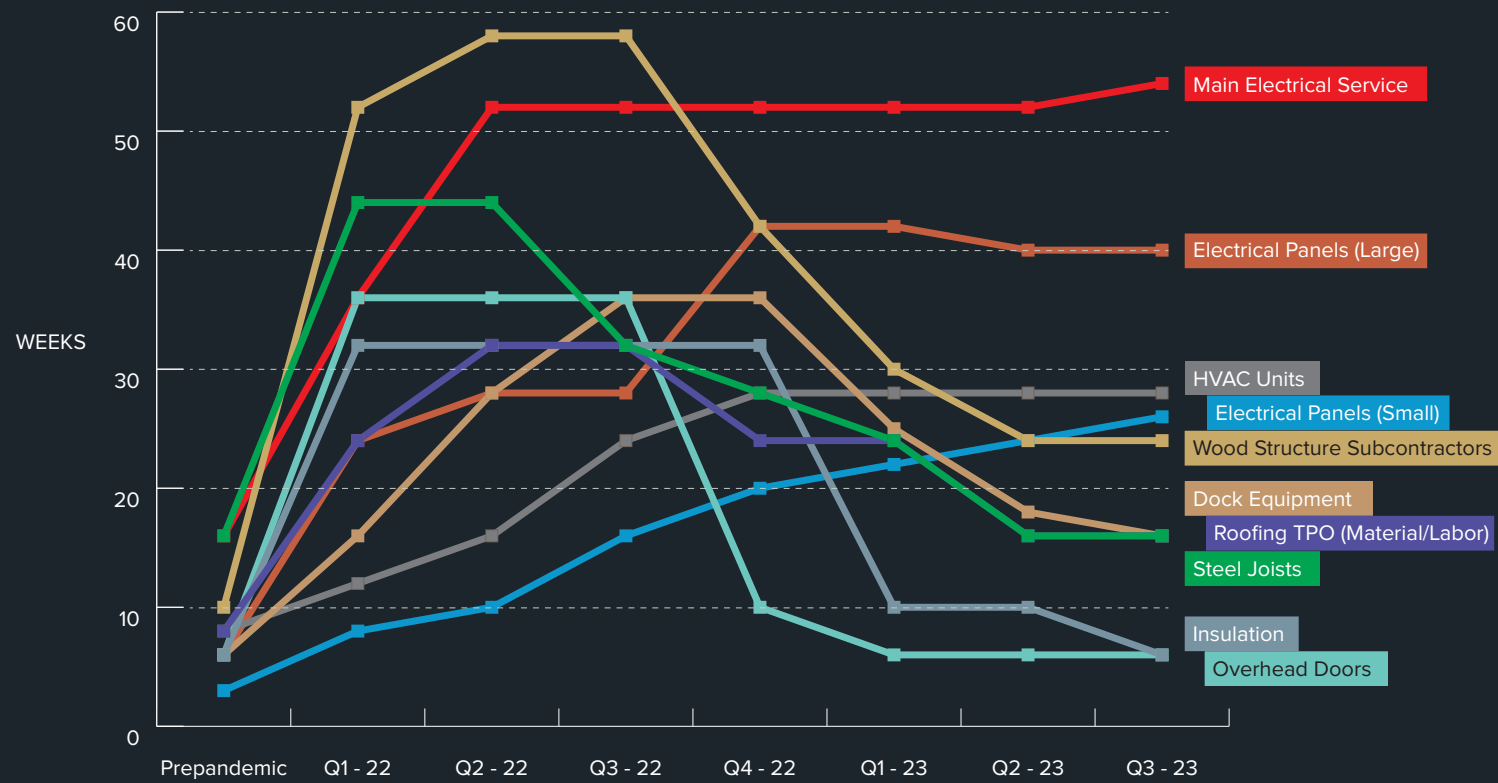
The construction unemployment rate in the Phoenix market has decreased slightly from 6% to 5.6% when comparing the current year to the previous one. However, despite this improvement, there are still challenges in finding available labor, particularly in more sophisticated trades. The increased demand in mission-critical and advanced industrial sectors, such as semiconductor and cleanroom construction, has made it even more difficult to find skilled workers in the Phoenix market.

# Supply Chain

On June 8th, White House officials announced that supply chains are improving. Port congestion has disappeared, and inflation has reduced to 3% in June 2023, the lowest level since March 2021. Container freight costs from China to the U.S. West Coast are now lower than pre-pandemic levels and transport costs have decreased from 2022 peaks, but remain elevated due to higher wages and fuel prices. Notably, ocean container rates dropped due to more capacity and less demand. Manufacturers and material providers have reported that the supply chain is healing, but challenges still exist. A survey called "2023 Supply Chain Perspective" found that 72% of companies are still facing supply chain challenges.

## MATERIAL LEAD TIMES

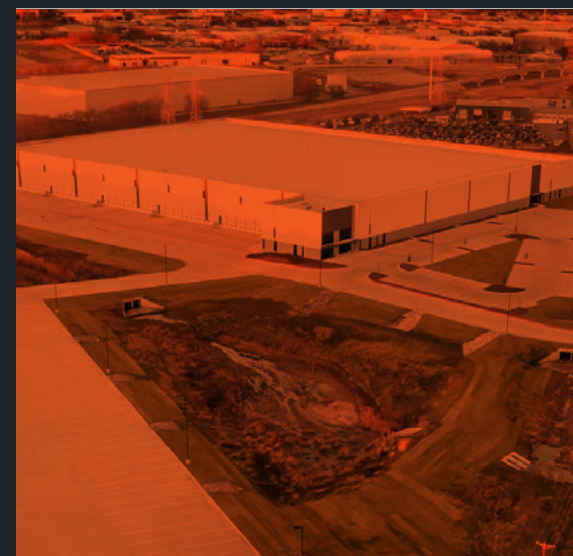
QUARTERLY INCREASE/DECREASE



**HVAC Units:** The lead times for HVAC units have been steadily increasing. While some manufacturers can provide the majority of the unit within 12-16 weeks, there is a notable delay in the availability of economizers, which are made by the same manufacturer. This delay in economizers can extend the overall lead times for HVAC units to a range of 24-36 weeks.



**Electrical:** The lead times for the main service sections to the building have remained relatively steady at around 12 months for the past year. However, there is a notable shift in lead times for electrical panels, with large panels (600A & up) now requiring 40-50 weeks, and small panels (under 600A) going from 16 weeks to a range of 22-26 weeks. This recent delay in panel deliveries is primarily attributed to a shortage of fuses, as per the latest information provided by our industry partners.



**Drywells:** Within the Phoenix market, subcontractors specializing in drywell installations have faced challenges in meeting demand across the entire valley. There are only a few subcontractors available for drywell installation within this region. Interestingly, it appears that the availability of materials plays a more significant role in the timing of drywell installations than the availability of manpower.

# Material Costs

A recent report by global construction advisory firm Rider Levett Bucknall (RLB) reveals that construction costs in Phoenix have risen in the past three years due to supply chain challenges and other factors. Although these cost increases are now showing signs of stabilizing, they remain higher than most markets. In May 2023, Phoenix's construction expenses were 7.58% higher compared to the same month the previous year, ranking it fifth in cost escalation among 12 major U.S. metro areas.

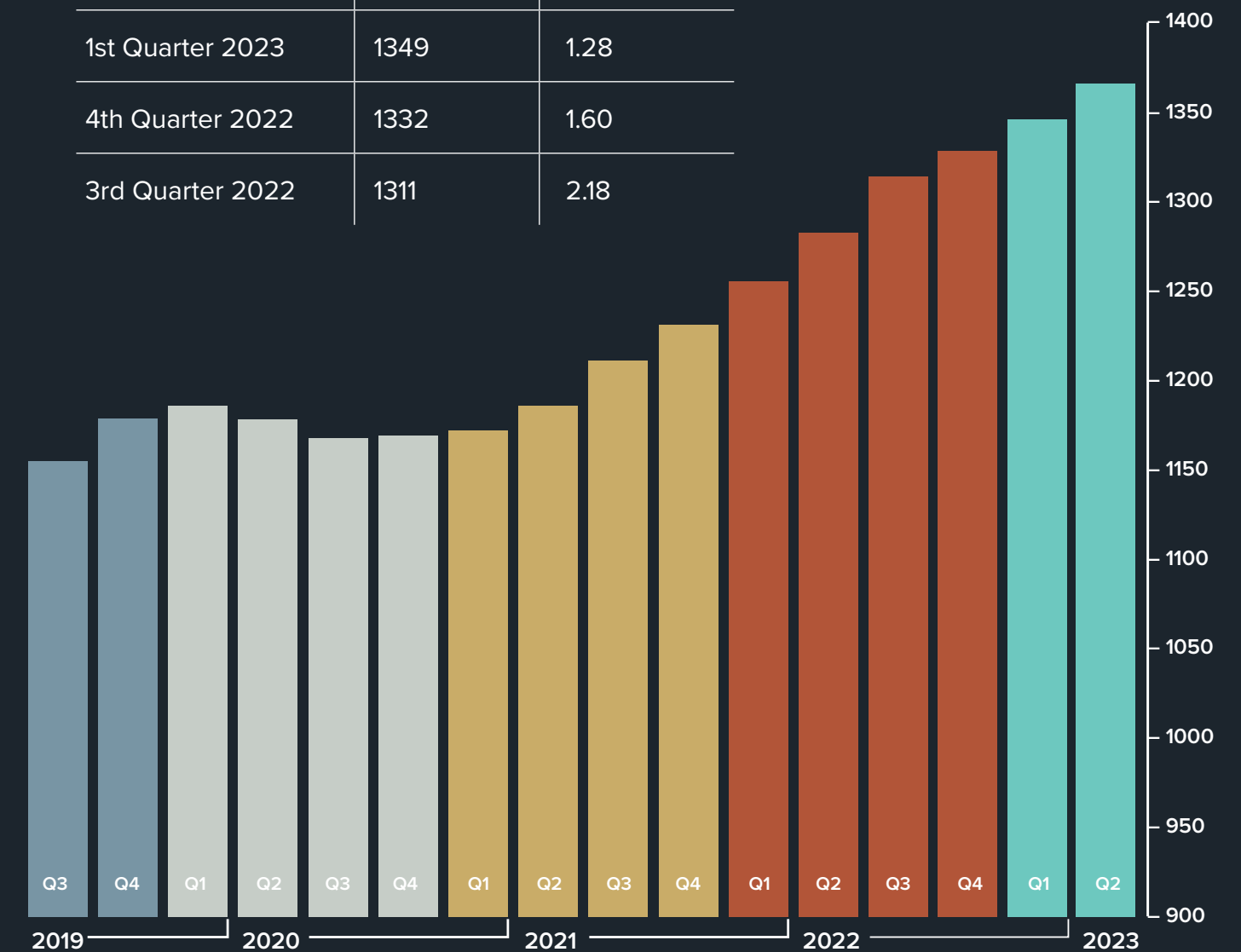
Meanwhile, in Dallas, efforts to combat inflation seem to be yielding positive outcomes. Despite supply chain disruptions causing delays, pricing has moderately stabilized. This excludes specific items with extended lead times such as electrical.



TURNER BUILDING COST INDEX

## CONSTRUCTION COST ESCALATION BY QUARTER

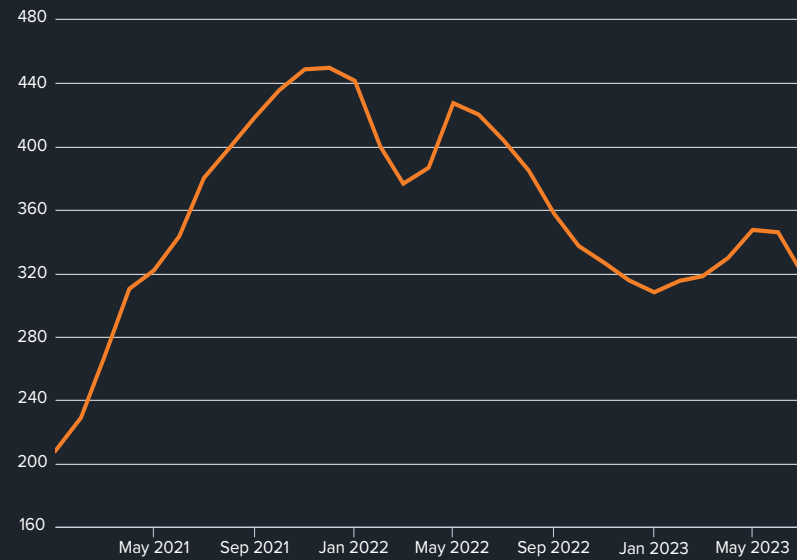
Quarter	Index	% Change
2nd Quarter 2023	1365	1.19
1st Quarter 2023	1349	1.28
4th Quarter 2022	1332	1.60
3rd Quarter 2022	1311	2.18



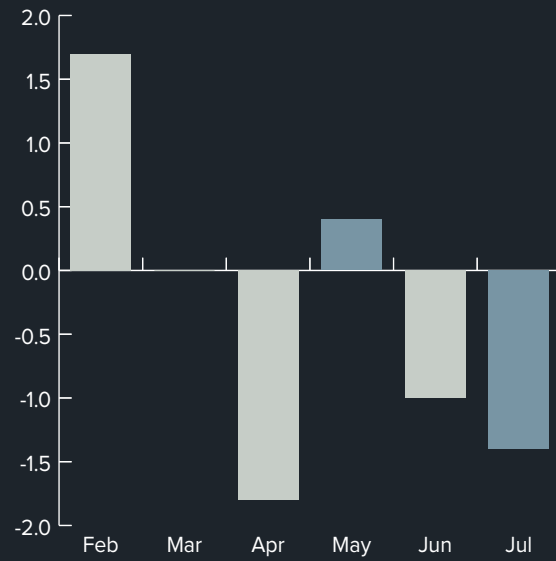
The Cost Index is determined by several factors considered on a nationwide basis, including labor rates and productivity, material prices, as well as the competitive condition of the marketplace.

# CONSTRUCTION MATERIALS PRICE MOVEMENT

ALUMINUM MILL SHAPES

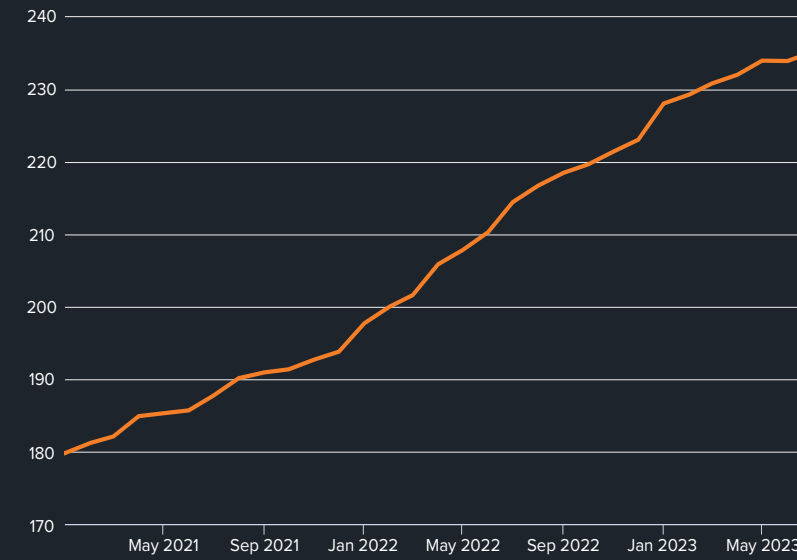


Price Index, Year-Over-Year

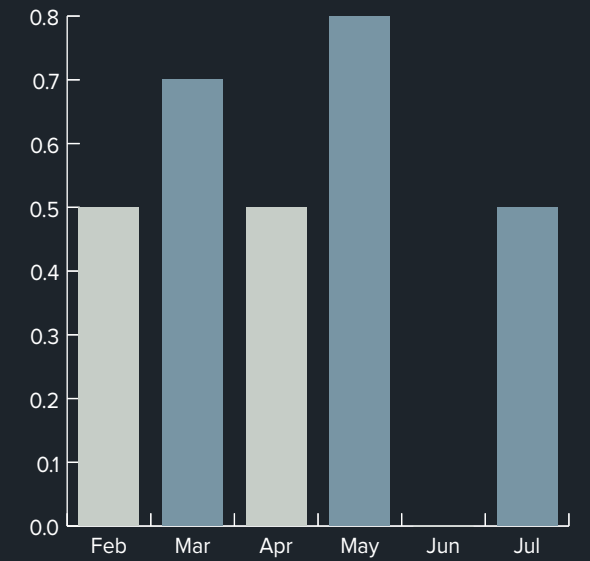


Percent Change, Monthly

CONCRETE

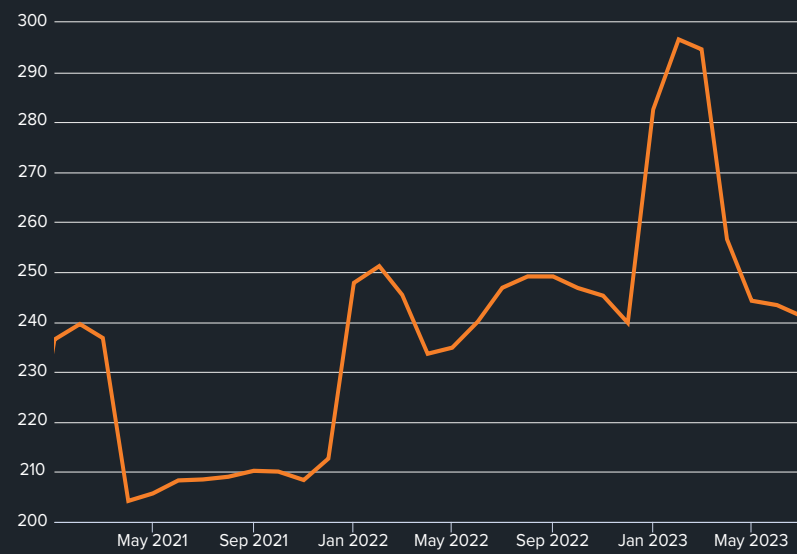


Price Index, Year-Over-Year

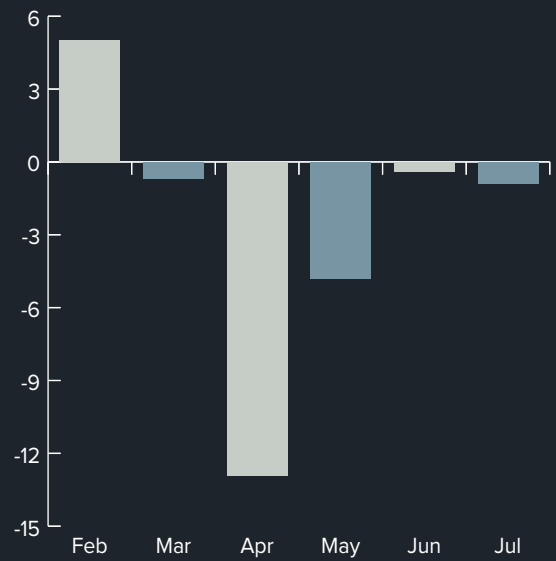


Percent Change, Monthly

ASPHALT & TAR PAVING MIXTURE

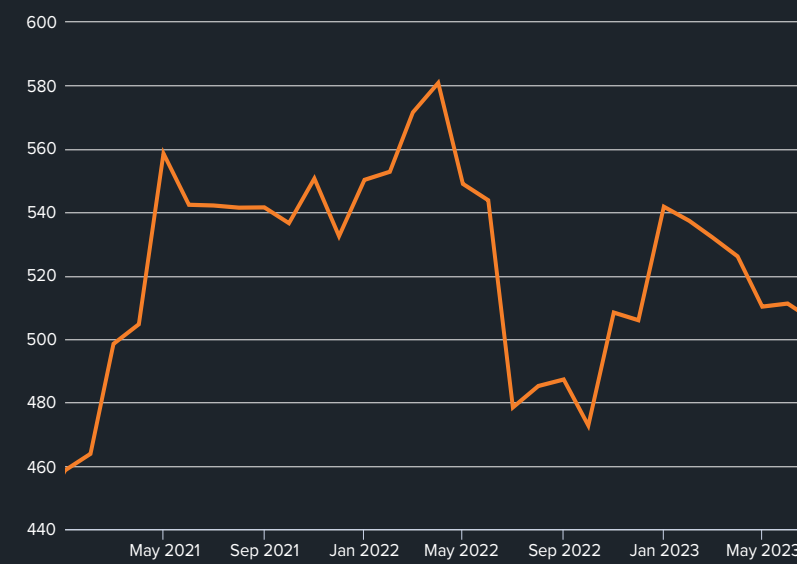


Price Index, Year-Over-Year

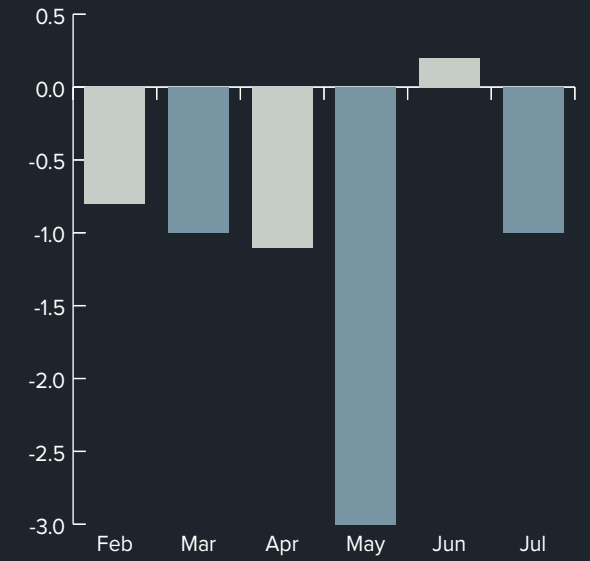


Percent Change, Monthly

COPPER



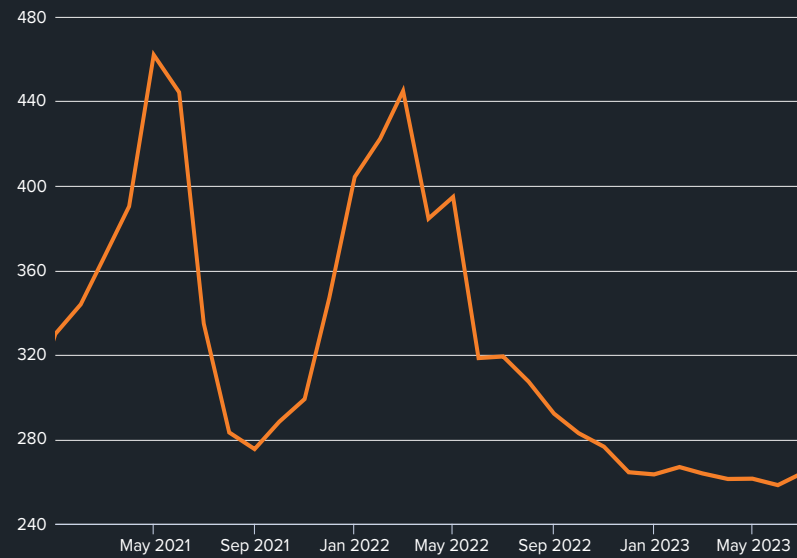
Price Index, Year-Over-Year



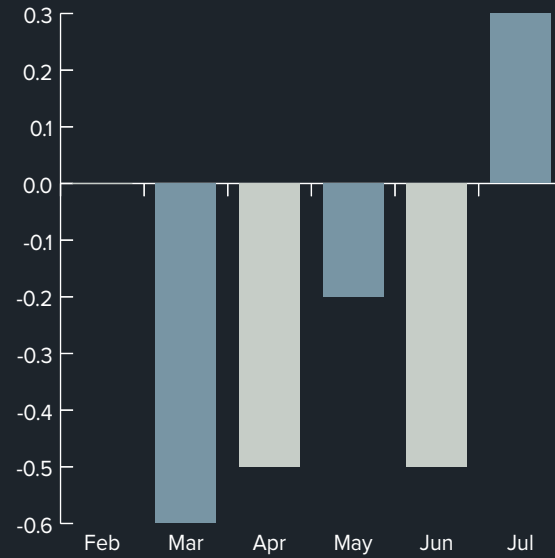
Percent Change, Monthly



LUMBER

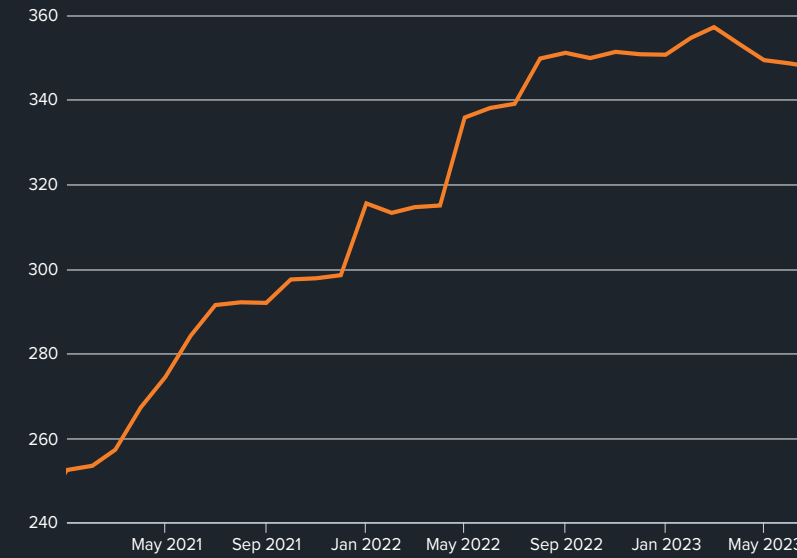


Price Index, Year-Over-Year

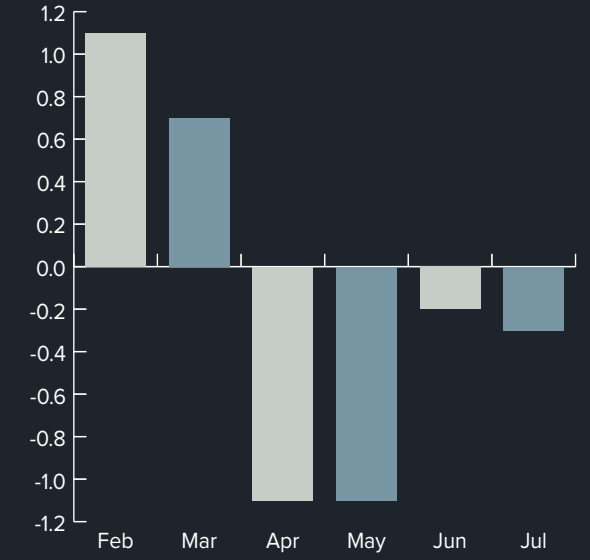


Percent Change, Monthly

GYPSUM

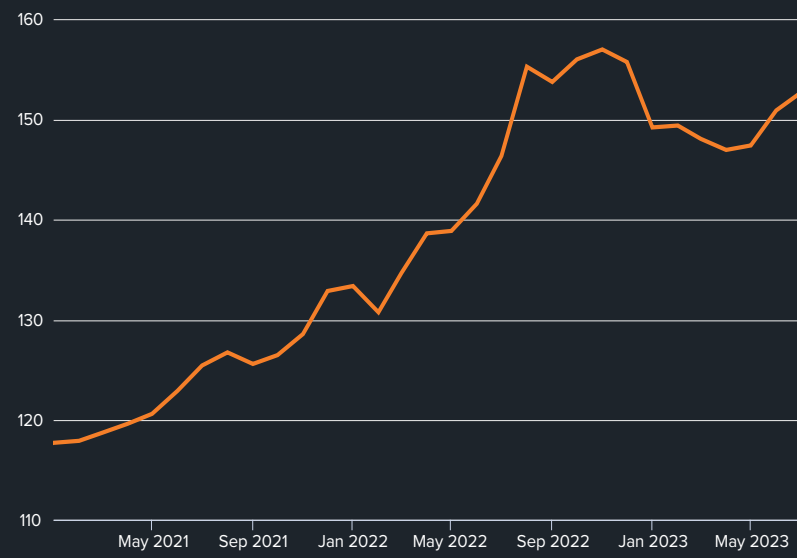


Price Index, Year-Over-Year

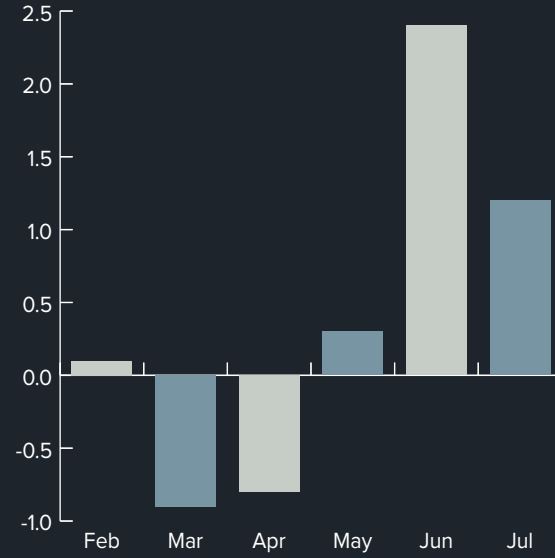


Percent Change, Monthly

FLAT GLASS

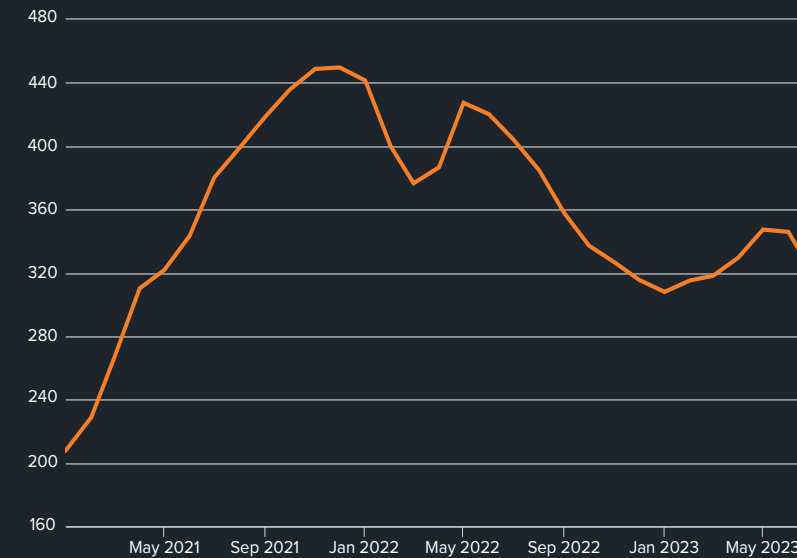


Price Index, Year-Over-Year

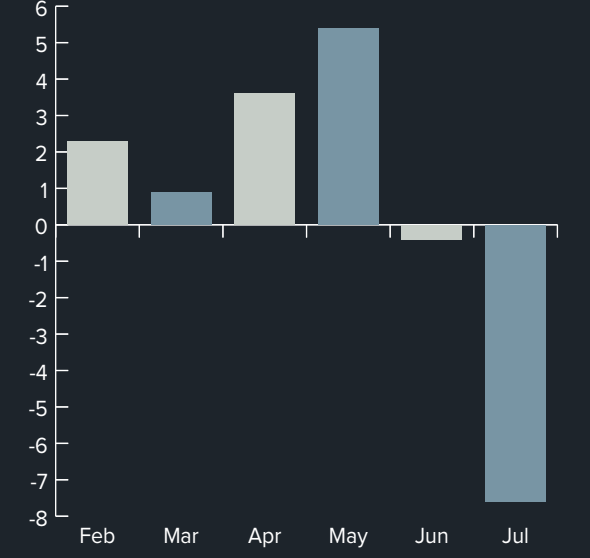


Percent Change, Monthly

STEEL MILL PRODUCTS



Price Index, Year-Over-Year



Percent Change, Monthly

# Design Expectations

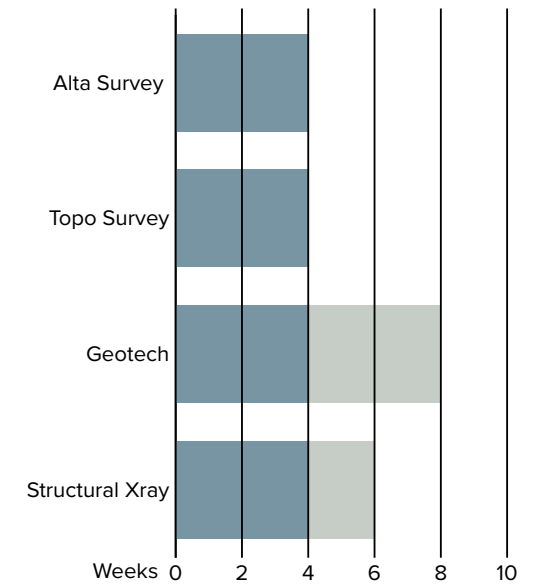
The continued effects of labor issues, supply chain problems, and material volatility are being felt by more than just the construction team. Our architectural team is tasked with conceptual design, preliminary pricing, entitlements, construction documents, and construction administration through completion. Many of these steps are seeing long lead times because of heavily booked due diligence consultants, ever-changing design expectations from municipalities, as well as increasing entitlement and permit review durations.



## Municipalities Design Expectations\*

Design aesthetics are becoming more and more influenced by the desires of the municipalities' Design Review Boards (DRB). In many of our current markets, we have seen a greater desire to have new industrial projects look more like Class A office buildings. This is being accomplished through:

- Increased plane changes across facades
- Increased glazing amount and height
- Multiple materials and textures
- Increased landscape requirements
- Taller parapets, removing the ability to use screen walls

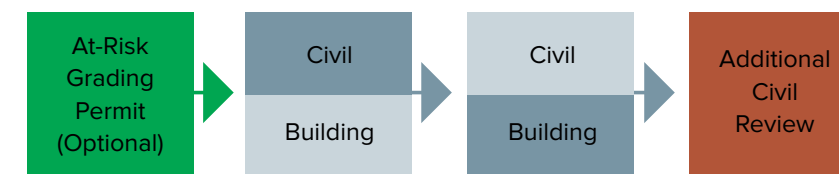


\*Does not apply to all municipalities.

## Entitlement and Permit Review Durations

Municipalities across the country are experiencing increased development demands, which is putting additional strain on their ability to meet the published review times. The expectation for timely reviews is no longer the reality.

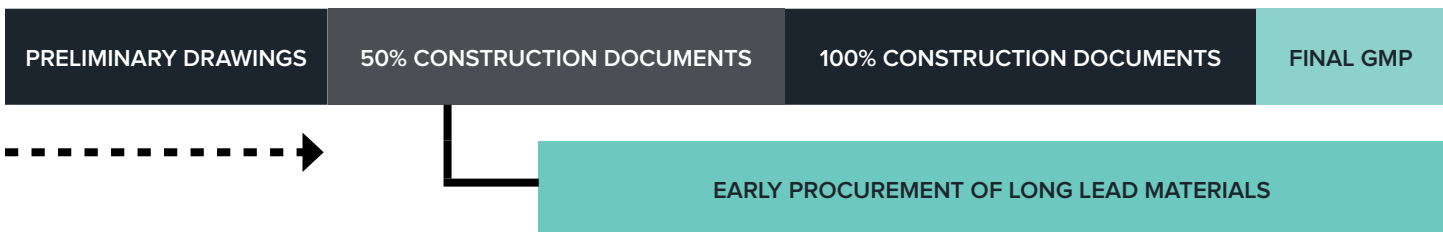
Some municipalities are seeing a 50 percent increase in review durations and certain ones are beginning to require an additional civil review, bringing the total to three. This is compounded by the already-existing two building permits required, which can be sought simultaneously with the civil reviews.





Since 1994, our design-build process has been outperforming the traditional construction approach. Typically, our process saves clients 2-4 months and continues to deliver despite the many challenges found in the market.

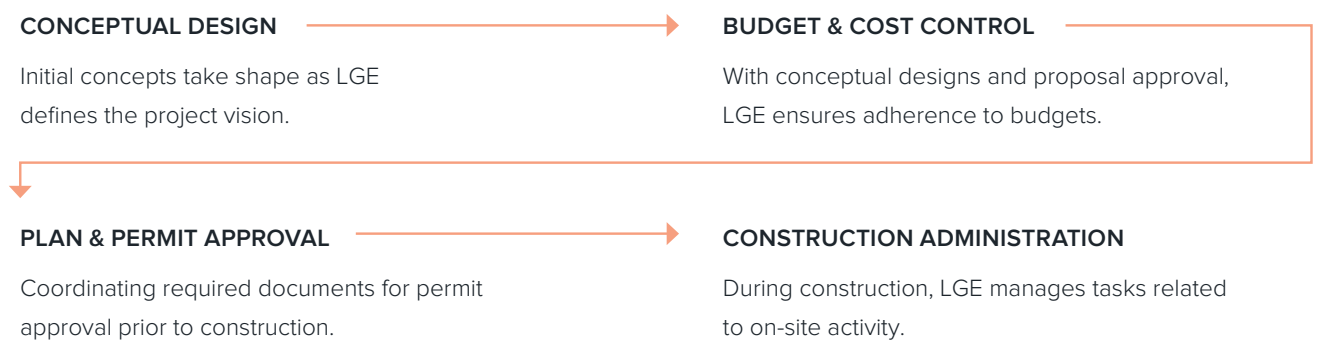
**LGE DESIGN BUILD'S PROCESS:**



# Solutions and Strategies

Early collaboration of design and construction is the critical difference between design build and a traditional approach. Developers, engineers, architects, and subcontractors are interacting on a daily basis, using their insight to avoid future issues. We can avoid issues that have severely impacted other firms by sourcing project materials early, ensuring project budget adherence, and coordinating permits and approvals. Our process tackles these issues up-front, while defining the project vision with our architectural teams and clients.

**DESIGN-BUILD PROCESS:**



# Final Thought

“As we wrap up the third quarter of the year, LGE Design Build maintains a sense of optimism regarding the construction industry's outlook. While we acknowledge the ongoing challenges highlighted in this report, we are firmly confident in our industry's adaptability and resilience.

From the growing sectors in Dallas-Fort Worth to the endurance of the Phoenix market, these regional successes are emblematic of the broader potential for growth and our ability to overcome obstacles together. If you're seeking guidance or solutions tailored to your specific project needs, please don't hesitate to reach out.”

– Grant Blunt, Vice President of Construction, LGE Design Build



### LGE Design Build, AZ

1200 N 52ND STREET  
PHOENIX, AZ 85008  
[www.lgedesignbuild.com](http://www.lgedesignbuild.com)  
480.966.4001

### LGE Design Build, TX

1280 LEVEE ST  
DALLAS, TX 75207  
[www.lgedesignbuild.com](http://www.lgedesignbuild.com)  
469.498.0998

#### SOURCES:

[https://insights.cumming-group.com/wp-content/uploads/2023/07/CCORP23Q2\\_MarketOverview\\_Final-718.23.pdf](https://insights.cumming-group.com/wp-content/uploads/2023/07/CCORP23Q2_MarketOverview_Final-718.23.pdf)  
<https://insights.cumming-group.com/regional/dallas/>  
<https://insights.cumming-group.com/regional/phoenix/>  
<https://www.bizjournals.com/phoenix/news/2023/08/02/phoenix-industrial-growth-2023-outlook.html>  
<https://www.plantemoran.com/explore-our-thinking/insight/2023/plante-moran-cresa/q2-2023-office-real-estate-market-report>  
<https://www.cushmanwakefield.com/en/united-states/insights/us-marketbeats/us-office-marketbeat-reports>  
<https://www.us.jll.com/en/trends-and-insights/research/office-market-statistics-trends>  
<https://www.azcommerce.com/media/ntnmgfvb/emp-report.pdf>  
<https://www.dallasnews.com/business/real-estate/2023/07/05/dallas-area-adds-the-most-new-construction-jobs-in-us/>  
<https://insights.cumming-group.com/regional/phoenix/>  
<https://www.constructiondive.com/news/falling-material-prices-expected-reverse-course/651744/>  
[https://www.bizjournals.com/phoenix/news/2023/06/28/rider-levett-bucknall-construction-cost-report.html?cx\\_testId=40&cx\\_testVariant=cx\\_9&cx\\_artPos=7#cxrecs\\_s](https://www.bizjournals.com/phoenix/news/2023/06/28/rider-levett-bucknall-construction-cost-report.html?cx_testId=40&cx_testVariant=cx_9&cx_artPos=7#cxrecs_s)  
<https://azbigmedia.com/business/here-are-some-fast-facts-on-the-arizona-water-supply/>