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Rising Labor Costs Eat Away At Construction Firms' Profits

Written by: Joe Bousquin, Senior Reporter, Construction Dive

CONTRACTORS ARE PAYING MORE FOR LOW-SKILLED WORKERS BUT AREN'T BENEFITING FROM INCREASED PRODUCTIVITY, ECONOMISTS SAY.

The clamor over construction's labor crisis reached a fever pitch recently, with new evidence suggesting historic wage increases for low-skilled site workers are eating into contractors' profits.

Average hourly earnings for production and nonsupervisory employees in construction rose to $32.19 in May, according to the Bureau of Labor Statistics, a 6.3% increase from a year ago and the highest gain in 40 years.

But increasingly, those higher wages are coming on the bottom rung of the construction employment ladder, with unskilled laborers seeing the greatest wage gains, economists told Construction Dive. That means construction companies pay more for hard-to-find workers, without necessarily reaping the benefits of increased productivity or profits.

Construction's Shrinking Premium

The average construction wage of $32.19 in May was 17.8% higher than the average hourly earnings of $27.33 in the private sector as a whole, where wages rose 6.4% year over year, illustrating the premium construction companies pay their workers compared to other fields.

The industry has emphasized that higher pay rate to recruit more workers into what they often perceive as a more dangerous job, without the perks of remote work, climate-controlled offices, or more flexible hours.

As other industries have ramped up their pay rates in the face of worker shortages and skyrocketing inflation, construction is losing its lead in the wage race, according to Ken Simonson, chief economist for the Associated General Contractors of America.

"Construction still has a considerable premium, as I call it, in what it pays the average worker, compared to other industries," Simonson said. "But that premium has shrunk."

For example, before the onset of the COVID-19 pandemic in February 2020, construction wages were 20% to 23% higher than the private sector as a whole, Simonson said, compared to today's roughly 18% rate.

"So the average hourly wage in the rest of the private sector has come up, and that is squeezing what contractors are offering as a premium to go out and work in 100 degree heat," Simonson said.

More Workers, Lower Profits

At the same time, construction employers get fewer skilled workers for the higher wages they pay, said Anirban Basu, chief economist for the Associated Builders and Contractors.

"The 'unskilled laborer' is among the fastest growing occupational categories within construction," said Basu. That means companies are getting less value for their labor dollars. "Contractors are still hiring aggressively, but they're often just throwing bodies at jobs, without those bodies being more productive."

As a result, even as contractors anticipate hiring more workers in the months ahead, they don't anticipate profits going up, as they normally would while adding more employees to take on more jobs.

That's the latest reading in ABC's Construction Confidence Index report, which tracks contractors' expectations for sales, profit margins and staffing over the next six months, with any score of 50 or above indicating growth.

While May's CCI came in with a score of 62.8 for staffing outlooks, meaning contractors expected to add more jobs, profit margin forecasts were at just 50, or barely clinging to growth expectations.

"While you see many contractors still staffing up, the expectations regarding profit margins are flipping," Basu said. "They're becoming more pessimistic."

Just Half the Workers Needed

On the labor front, contractors hired 455,000 people in April. But that was less than the 494,000 jobs that were still open, a jump of 40% from a year ago, according to Simonson.

"We're in maybe the tightest market ever in the number of job openings for construction," Simonson said. "The implication is that construction firms, including homebuilders, would have brought on twice as many workers as they did, if they could have found enough qualified workers."

Indeed, a recent article in the Wall Street Journal pointed to labor shortages stymieing construction activity and company profits even as work from the $1.2 trillion Infrastructure Investment and Jobs Act kicks in.

Jim Schneiderman, mid-Atlantic vice president for Broomfield, Colorado-based Flatiron Construction, told the paper that higher employee costs were starting to eat into the firm's profits.

"We learned our lesson and will be building in those higher labor costs accordingly for future work," he said. "Everyone I talk to in the industry has had this same realization."

But Basu said that while contractors have generally been able to pass increased material and labor costs onto project owners during the pandemic, that could be changing now, given firms' expectations of lower margins, even as they staff up to take on infrastructure work.

"We are at an inflection point," Basu said. "Whatever the level of shortage has been in construction with respect to the workforce, it's about to get worse."

About the Author

Joe Bousquin has been covering construction since 2004. A former reporter for the Wall Street Journal and TheStreet.com, Joe focuses on the trends and challenges shaping the future of construction, development, and real estate as a senior reporter for Construction Dive. He holds a master's degree, with honors, from Columbia University's Graduate School of Journalism. He can be reached at jbousquin@industrydive.com.

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