



NEW MEXICO
LEGISLATIVE
FINANCE
COMMITTEE



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Explaining Rising Construction Costs

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The views expressed in this presentation are the opinions of the presenters and do not reflect the opinions of the New Mexico Legislative Council or any other member of its staff.

Problem Statement

- Construction costs continue to increase in the wake of the Covid-19 pandemic
- Continued cost escalation will limit the state's ability to meet increased demand for capital improvements to public schools, higher education institutions, state facilities, and local infrastructure

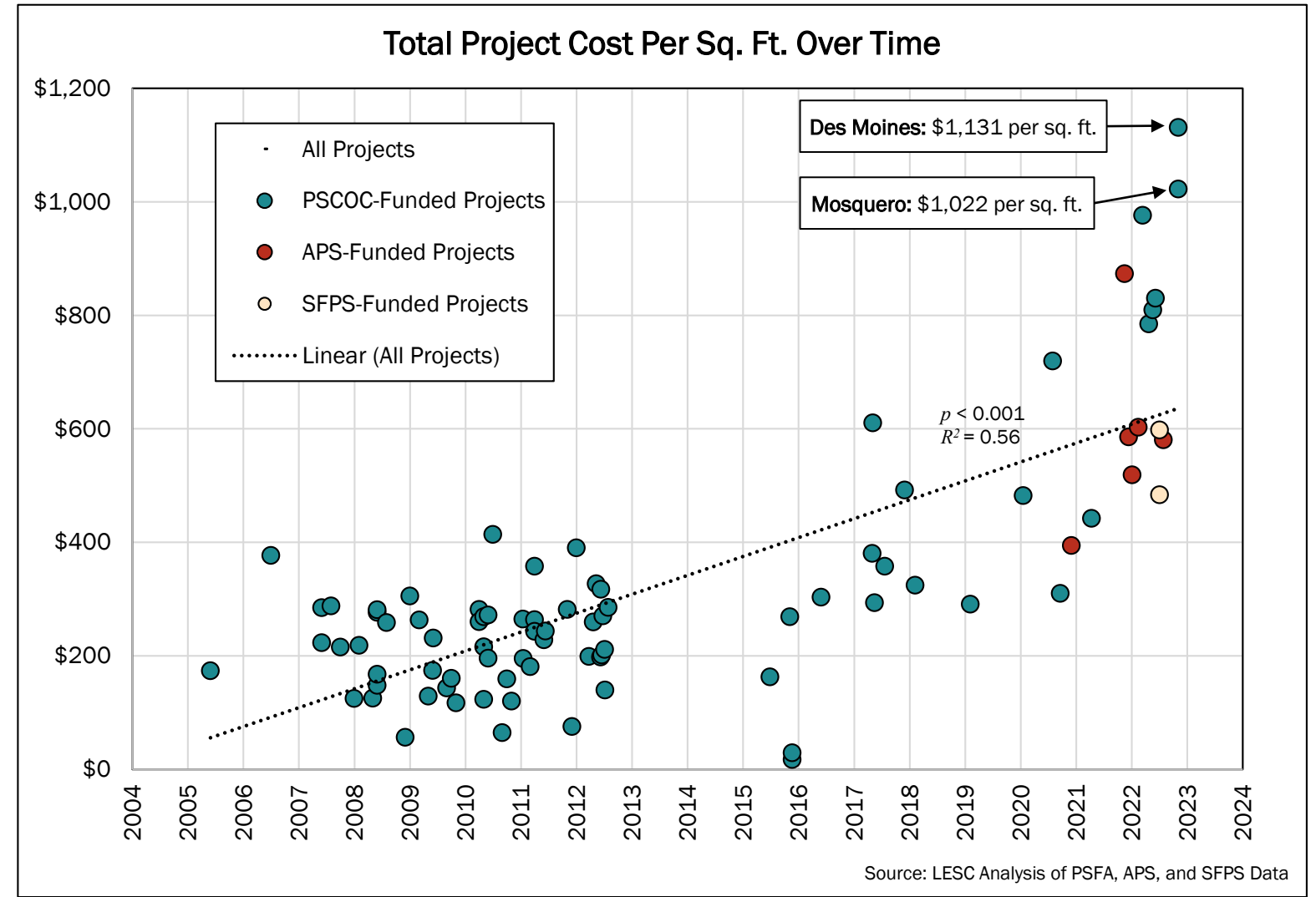
Costs

Last year, A linear regression estimated the cost of building a public school was \$425 per sq. ft.

Earlier this year, the model estimated a cost of \$582 per sq. ft.

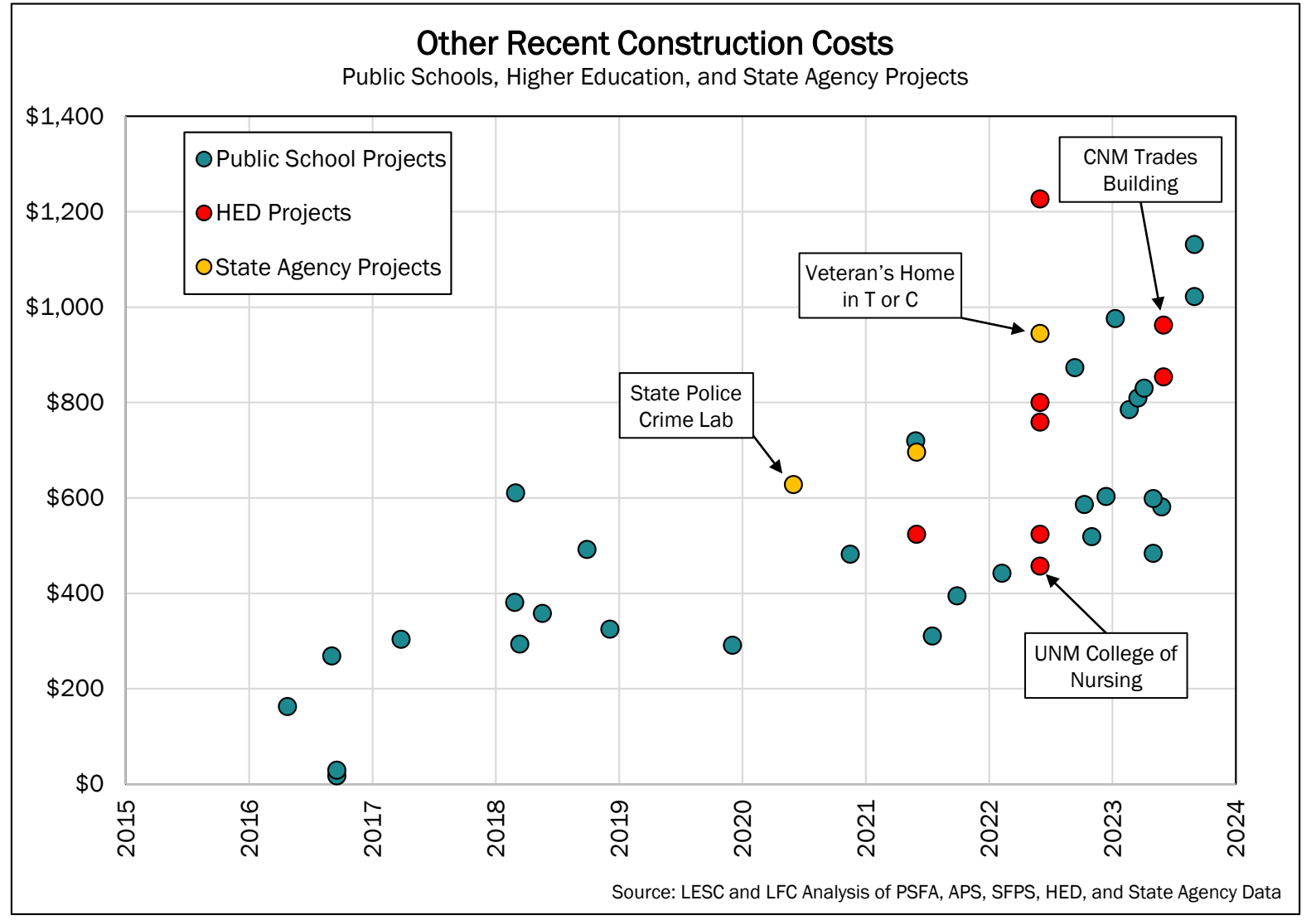
With adjustments to the model after new projects awarded this year, the model estimates a cost of **\$640 per sq. ft.**

Recent expensive projects have driven the predicted cost upward.



Costs

The costs of recent higher education projects appear to be following similar trends to those of public schools.

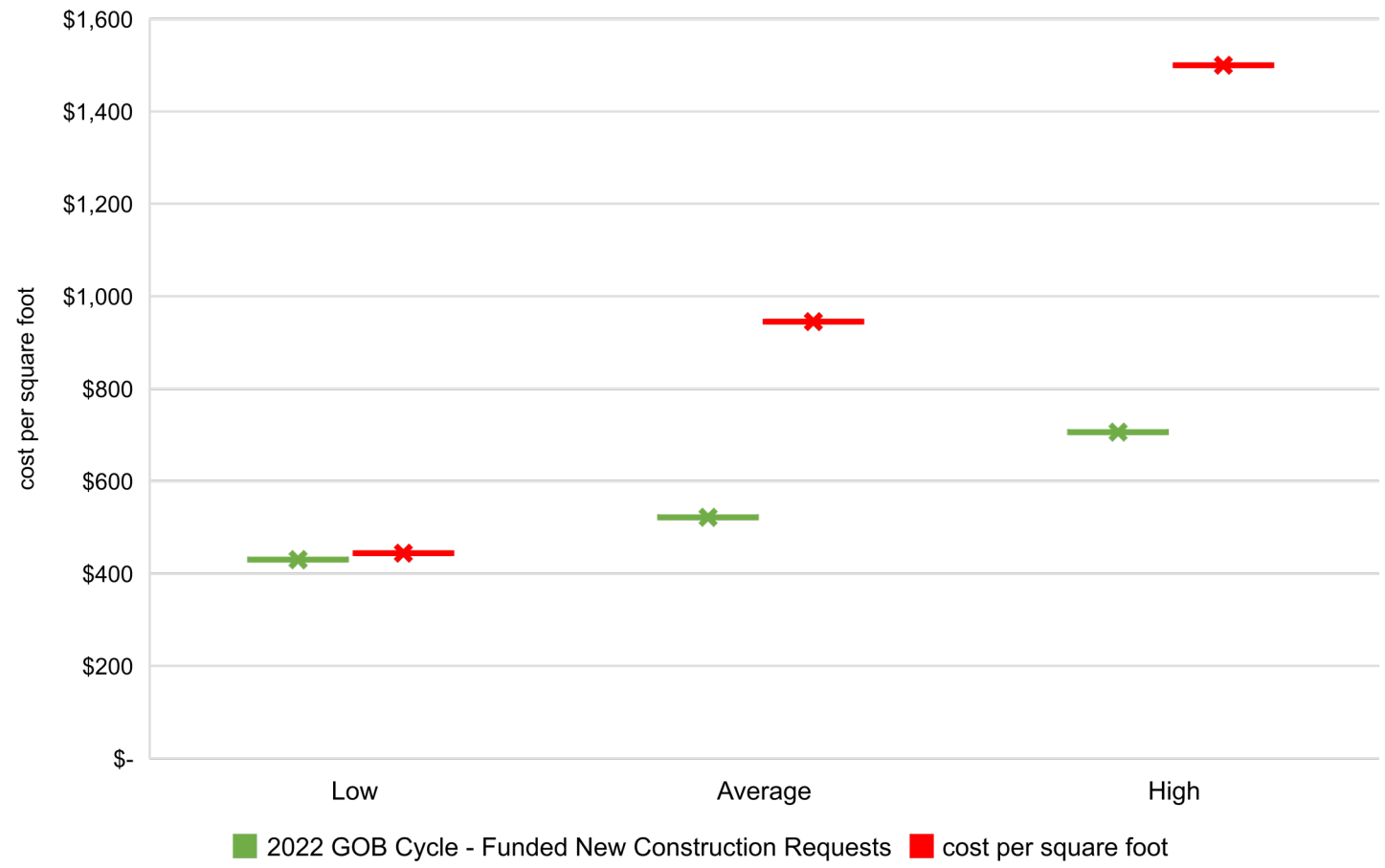


Costs

Rising costs are a topic of concern for the Higher Education Capital Outlay Committee.

Costs will likely present a challenge for the 2024 G.O. bond funding cycle.

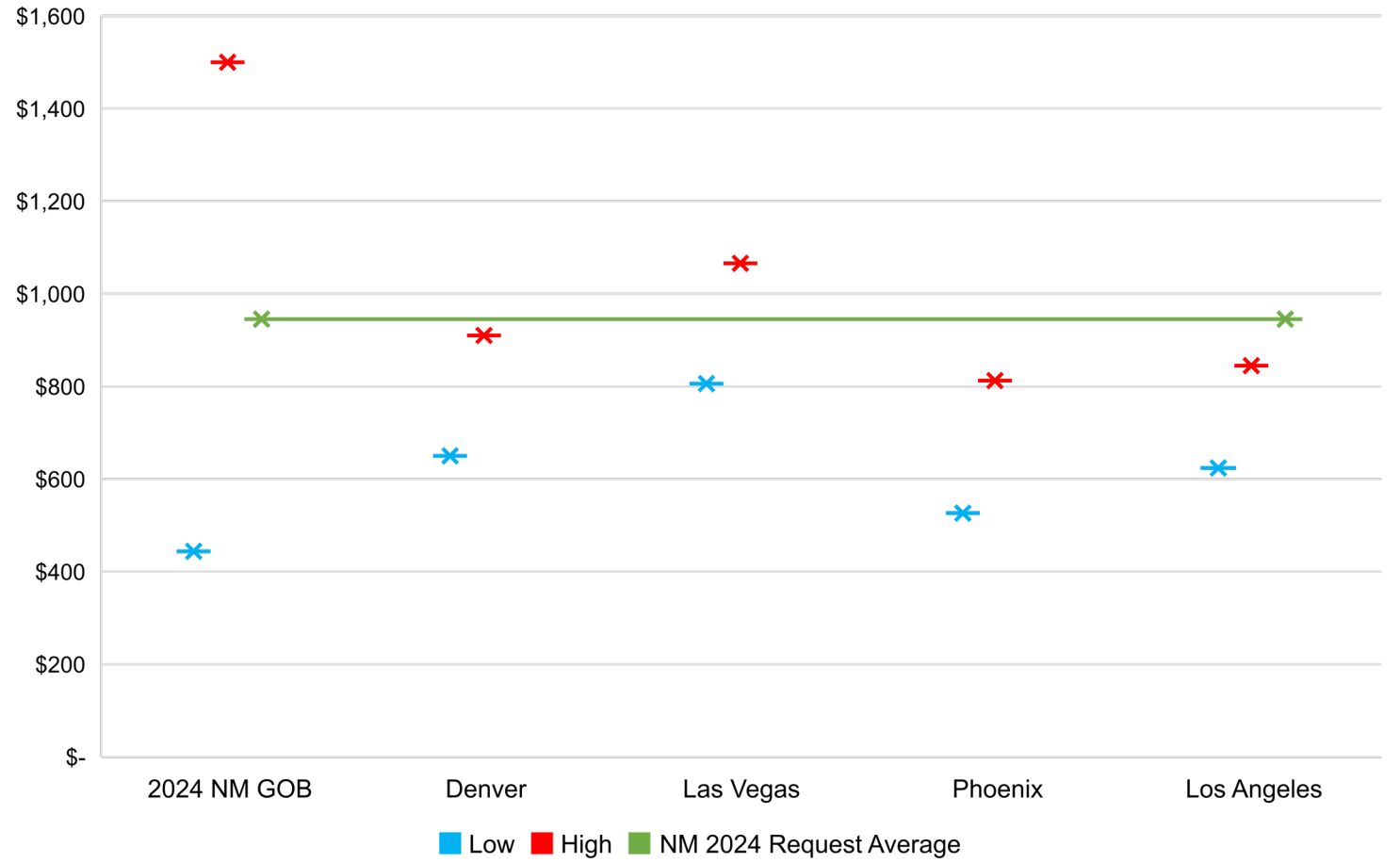
2024 Higher Education Requests Anticipate a Doubling of Construction Costs Since 2022



Costs

Cost estimates for higher education projects in New Mexico appear higher than costs in neighboring markets.

Estimated Total Project Cost Per Square Foot for Higher Education Projects in Neighboring Markets

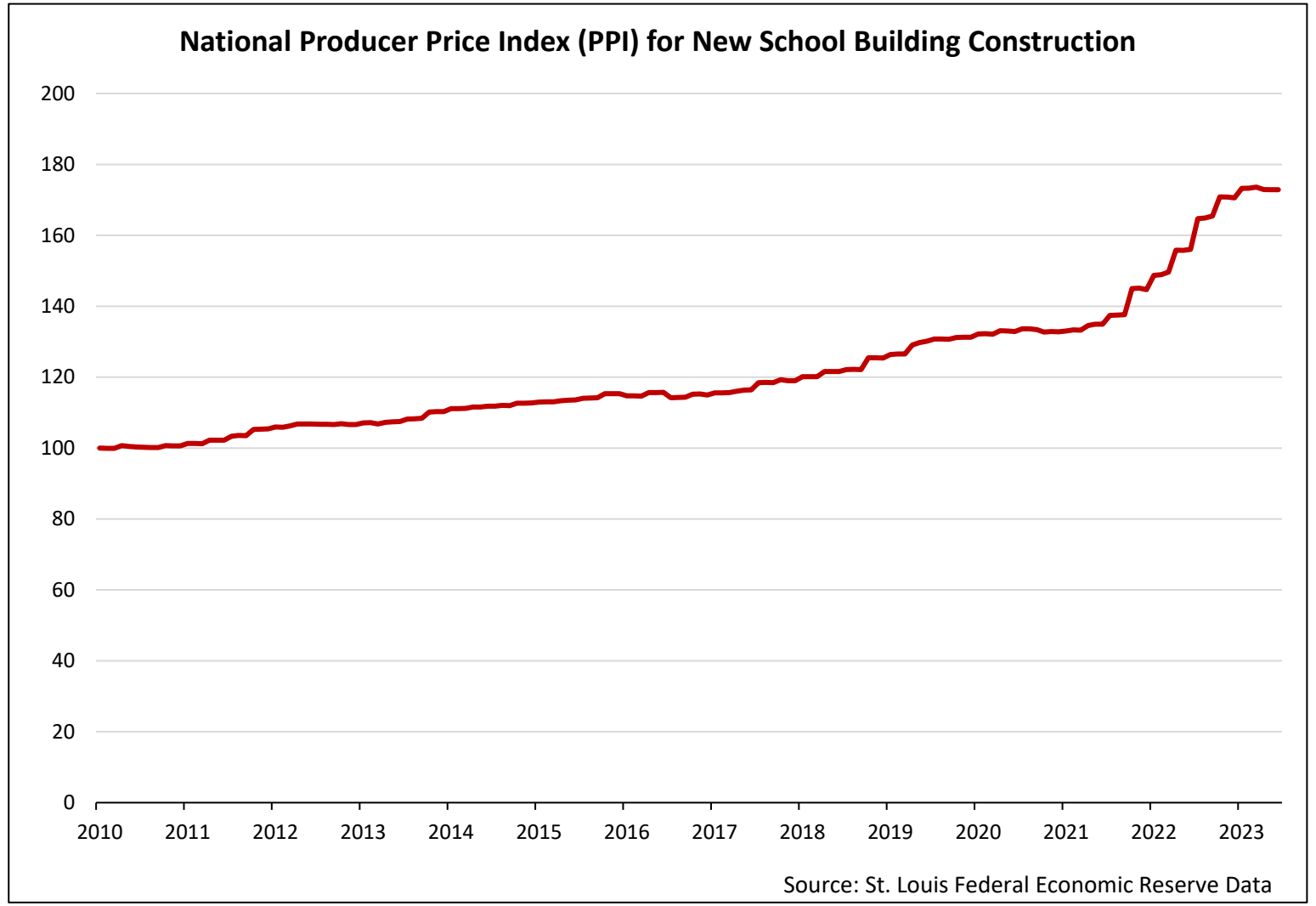


Costs

Nationally, school construction projects have become more expensive.

The Bureau of Labor Statistics' producer price index (PPI) for new school construction projects increased substantially during the pandemic.

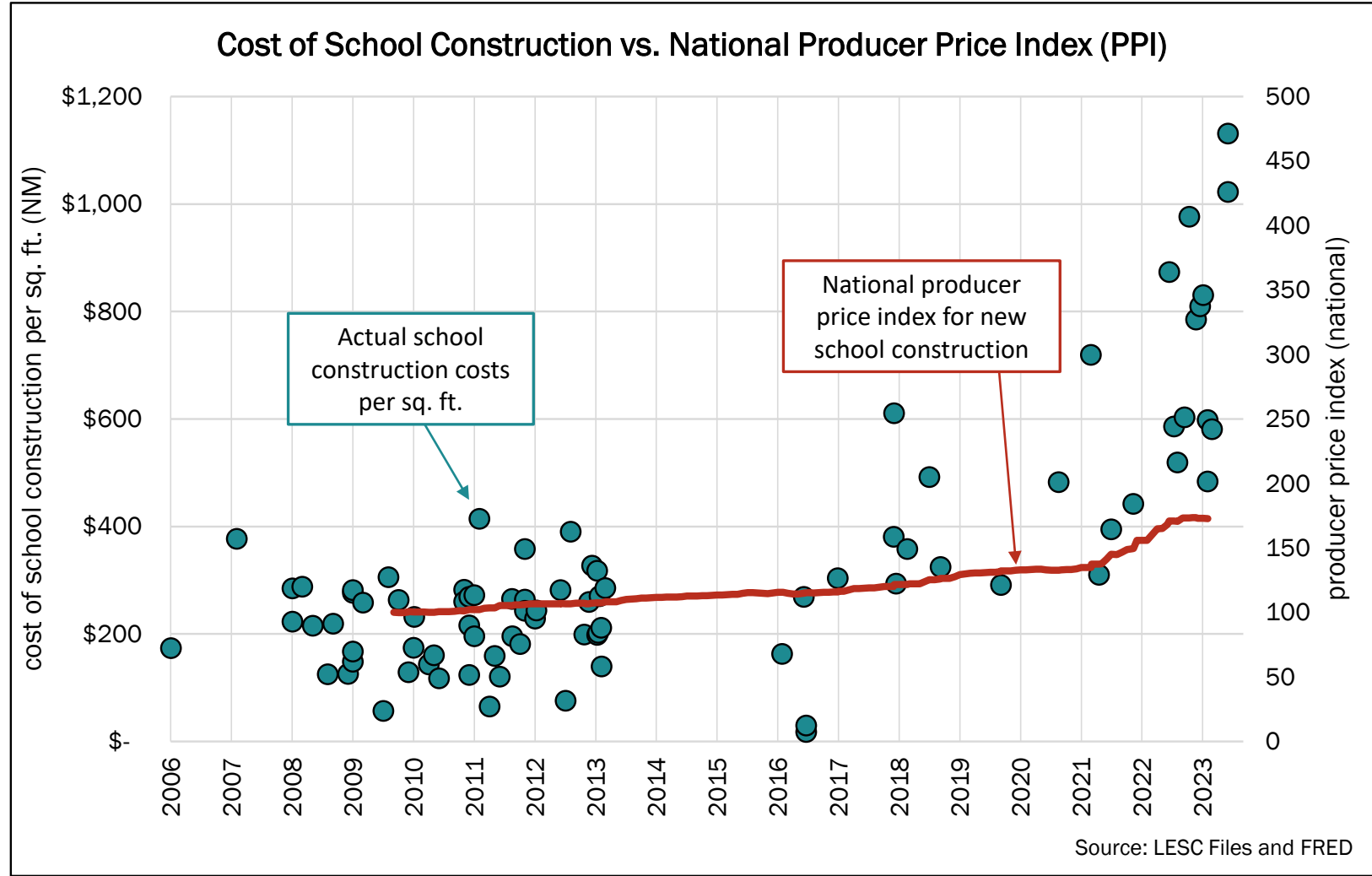
The PPI has stabilized over the past year.



Costs

New Mexico's school construction costs have closely mirrored the national trend until recently.

Certain construction projects approved in recent months have substantially exceeded the national trend.



Costs

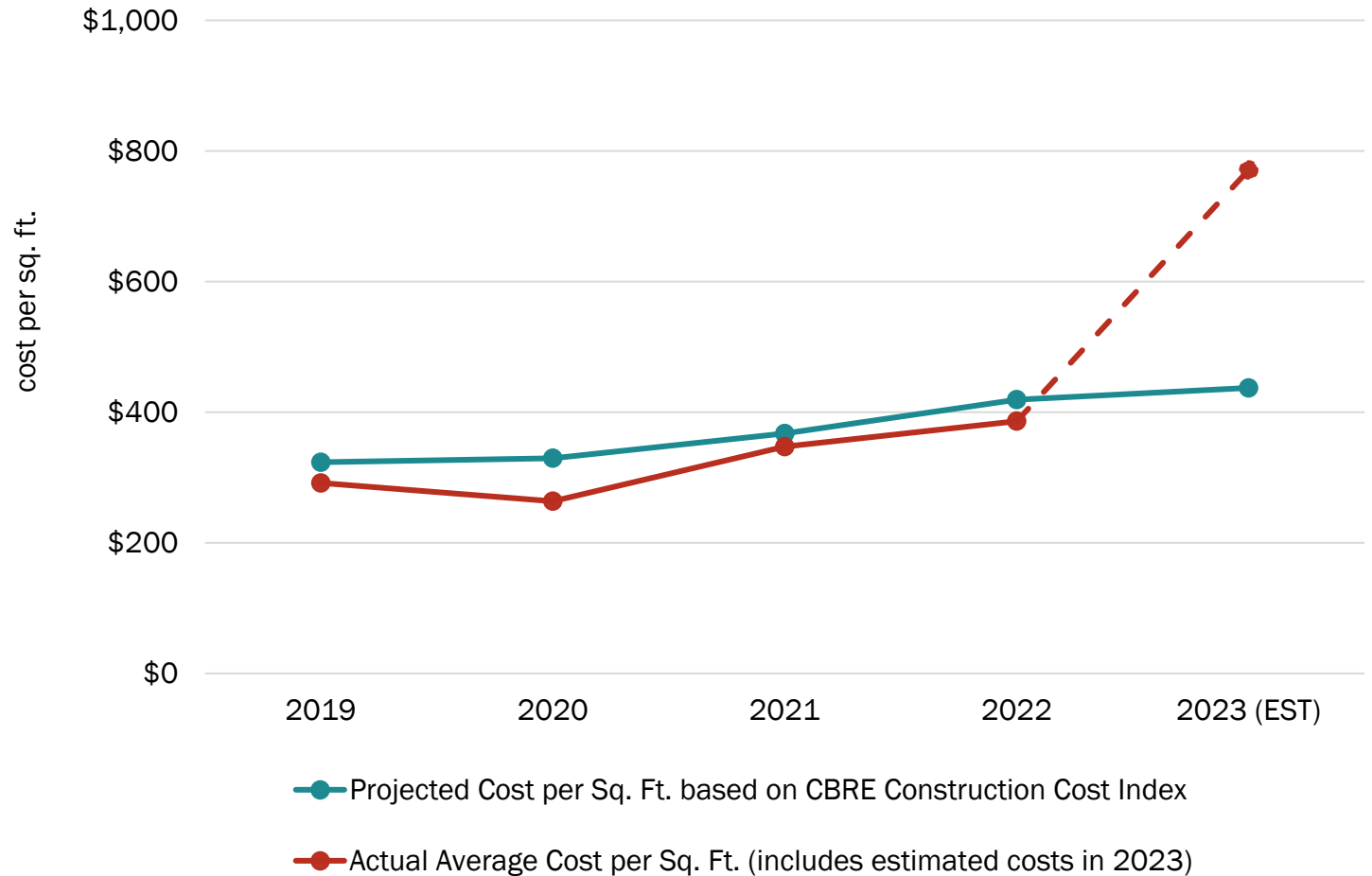
A national commercial real estate investment firm, Coldwell Banker Richard Ellis (CBRE), designed a “construction cost index” to summarize the net effect of changes across multiple dimensions of the construction market.

New Mexico’s construction costs were closely aligned to the CBRE index until this year.

Using the CBRE construction cost index, construction costs should be approximately \$437 per square foot this year.

Actual costs and contractor bids on four 2023 public school projects have averaged \$771 per sq. ft.

Actual Construction Costs and Construction Index Estimates



Source: LESC Analysis of CBRE and PSFA Data

Impact



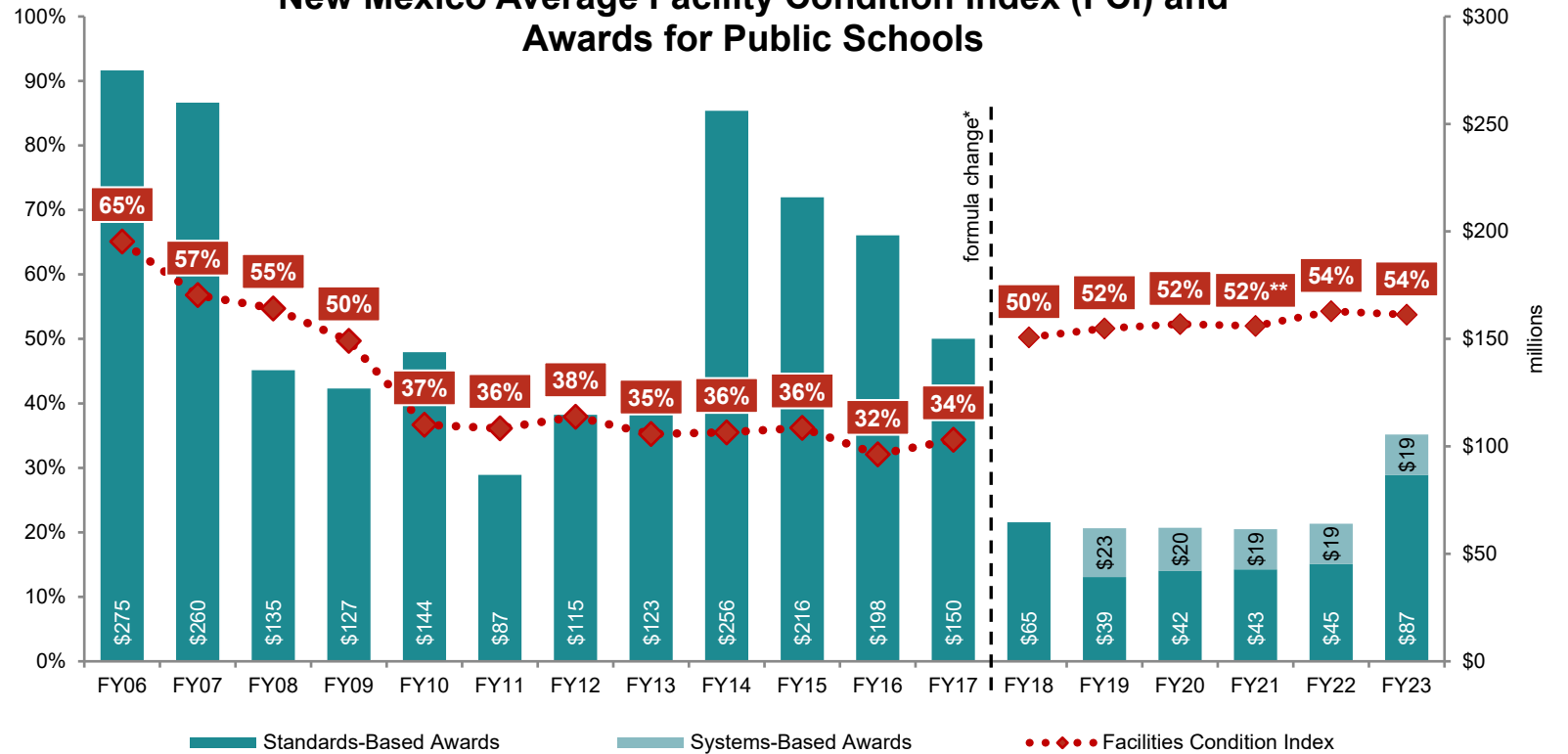
The cost of construction is inextricably tied to the state and local match formula and the statutory waiver criteria.

Higher construction costs means higher local matches.

Districts that can't afford their local match will request larger waivers from PSCOC.

Continued high costs will strain the state's capacity to make capital outlay awards each year.

New Mexico Average Facility Condition Index (FCI) and Awards for Public Schools



*In January 2018, PSCOC altered the methodology for calculating FCI, so FY18 scores are not directly comparable to prior year scores. The statewide average FCI of 50.3 percent for FY18 is equal to approximately 32.6 percent using the previous methodology.

Source: PSFA

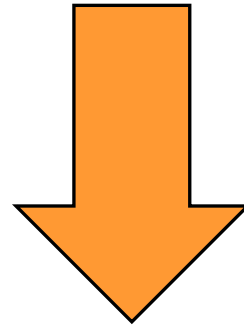
Supply and Demand Effects

Construction costs increased during the pandemic due to

- material costs,
- supply chain disruptions, and
- labor issues.

The supply chain has mostly stabilized, but some material and equipment costs remain high.

Labor appears to continue to drive cost increases, with surges in state and federal money for public projects contributing to the tight market.



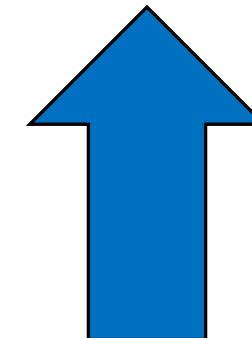
Decreasing Supply

- Tight labor market
- Workforce shortage, particularly in rural NM



Increasing Demand

- Public construction (state and federal)
- Private commercial construction
- Residential construction



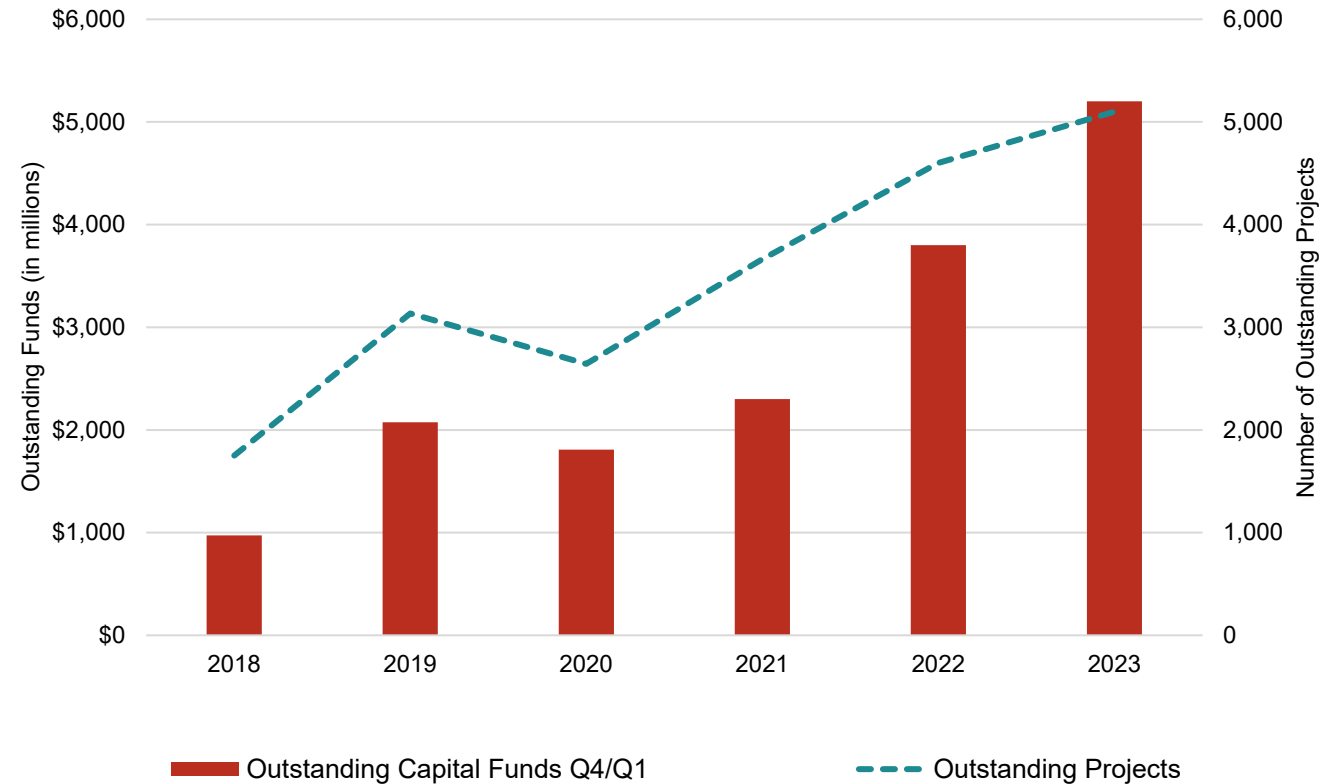
Demand

The Legislature passed historically large capital appropriations packages several years in a row.

At the end of the fourth quarter of FY23, outstanding capital funds totaled an estimated \$5.2 billion.

The number of outstanding projects totaled about 5,000.

Increased Capital Appropriations are Contributing to Construction Demand



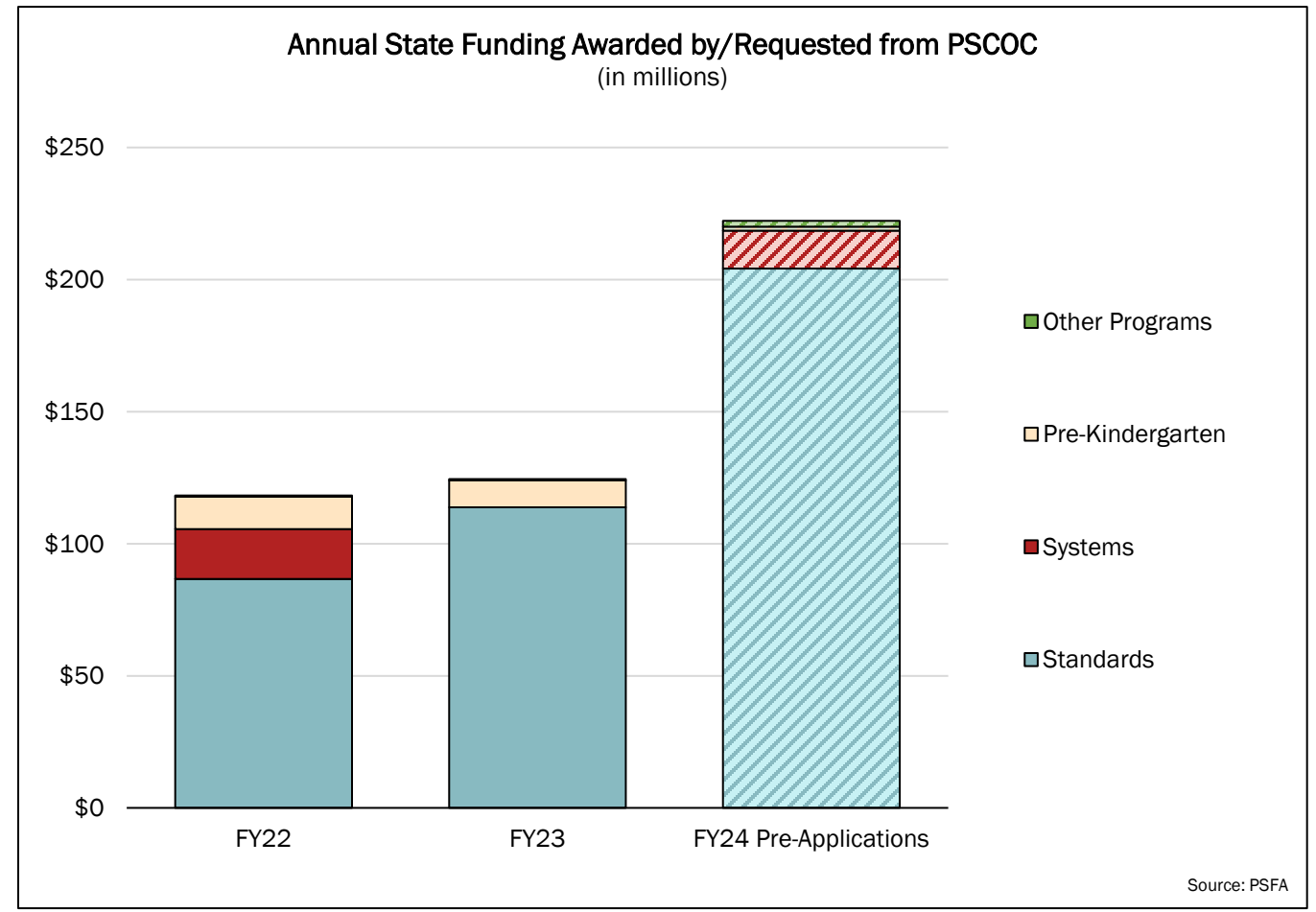
Source: LFC files

Demand

Senate Bill 131 from the 2023 legislative session decreased the local match for projects by 33 percent for most school districts, and 50 percent for micro-districts.

The reduction has increased demand for PSCOC funded projects.

Most districts applying for PSCOC funds cannot afford their local match, which will increase the state's cost burden for school construction.



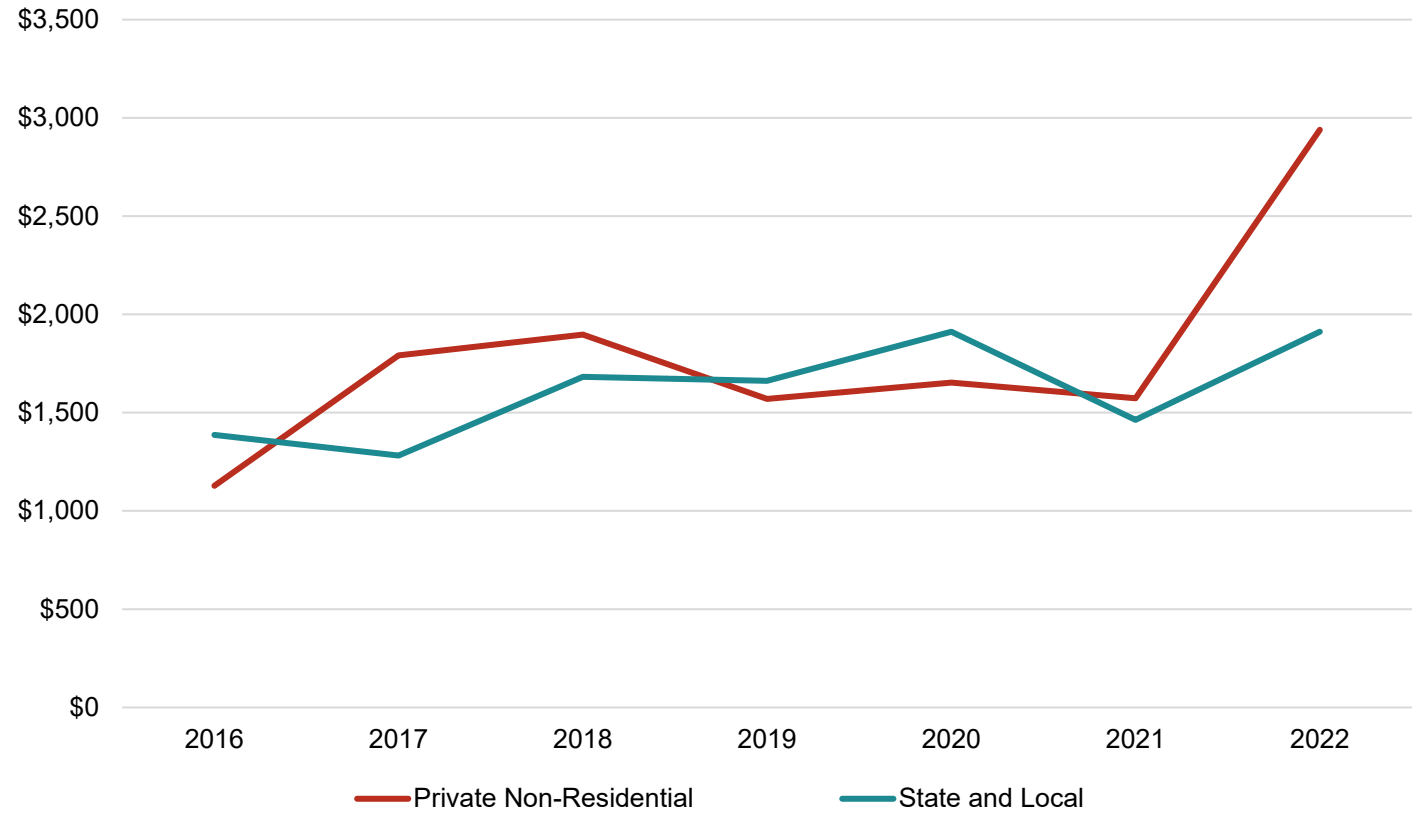
Demand

Activity in both the public and private construction markets in New Mexico has increased significantly in the last one to two years.

The year-over-year increase from 2021 to 2022 in private non-residential spending in New Mexico was 87% -- the third highest increase among all U.S. states, behind just Alaska and Arizona.

The year-over-year increase in state and local construction spending was 33% percent – the sixth highest increase among U.S. states.

Private and Public Construction Spending in New Mexico, 2016-2022
(in millions)

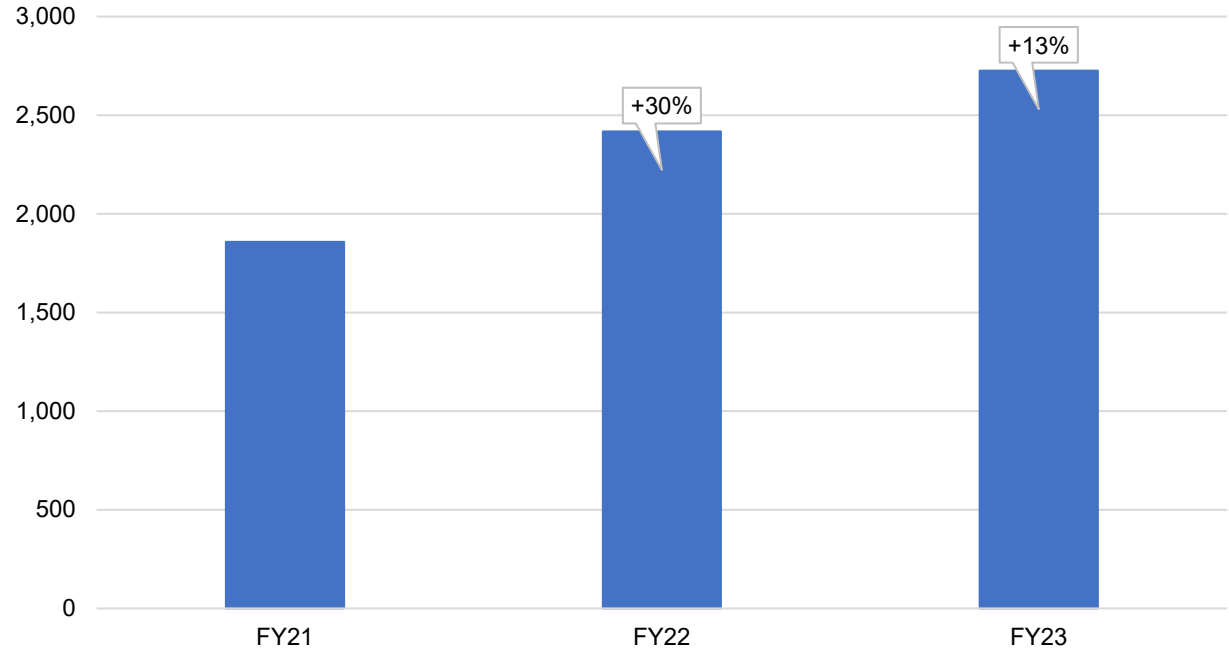


Source: U.S. Census, Value of Construction Put in Place Reports

Demand

Public construction demand is continuing to increase in New Mexico.

Number of Wage Decisions for Public Construction Projects in New Mexico



Source: Department of Workforce Solutions

Demand

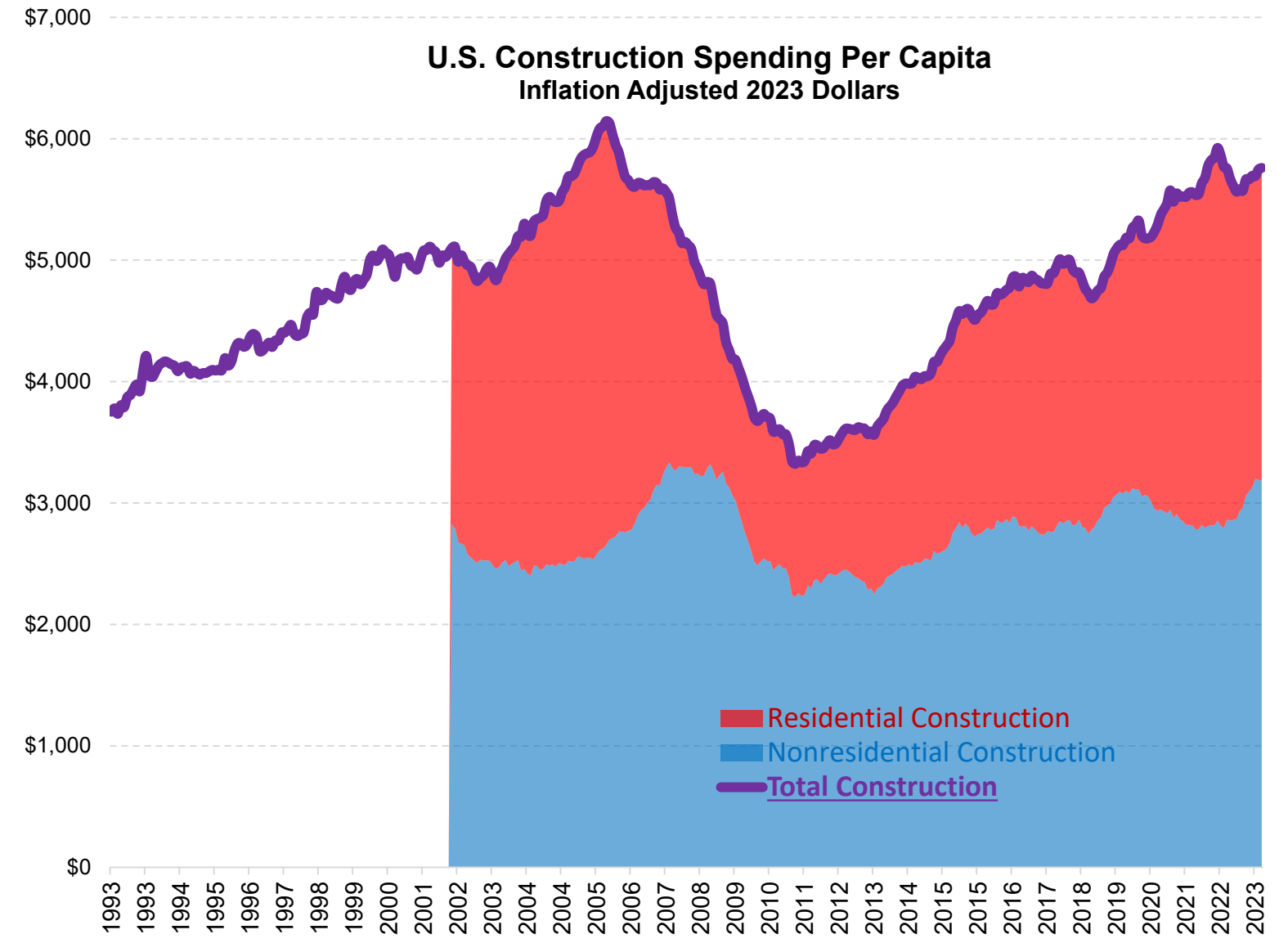
Even after adjusting for overall nominal U.S. dollar inflation and population growth, nationwide construction spending is near all-time peak levels.

Chart created by Legislative Council Service staff

Source: U.S. Census Bureau, Construction Spending
<https://www.census.gov/construction/c30/c30index.html>

Inflation adjusted with CPI-U (<https://www.bls.gov/cpi>)

Per Capita with (U.S. Bureau of Economic Analysis, Population
<https://www.bea.gov/data/income-saving/personal-income>)

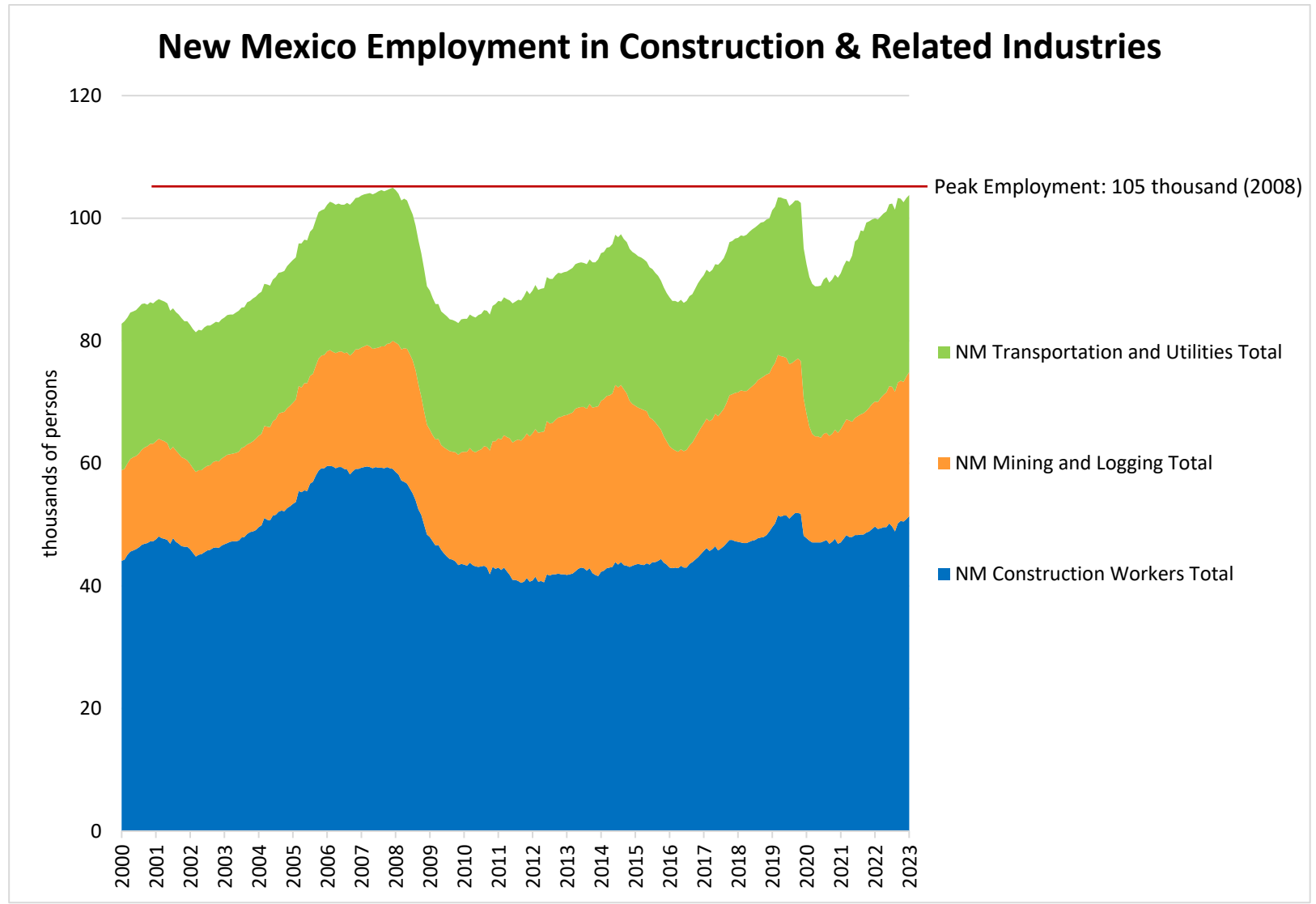


Supply

The total employment in construction and related industries in New Mexico is near – but still below – its peak.

New Mexico’s employment in construction and related industries has never exceeded a peak of 105 thousand laborers in 2008.

Chart created by Legislative Council Service staff



Supply

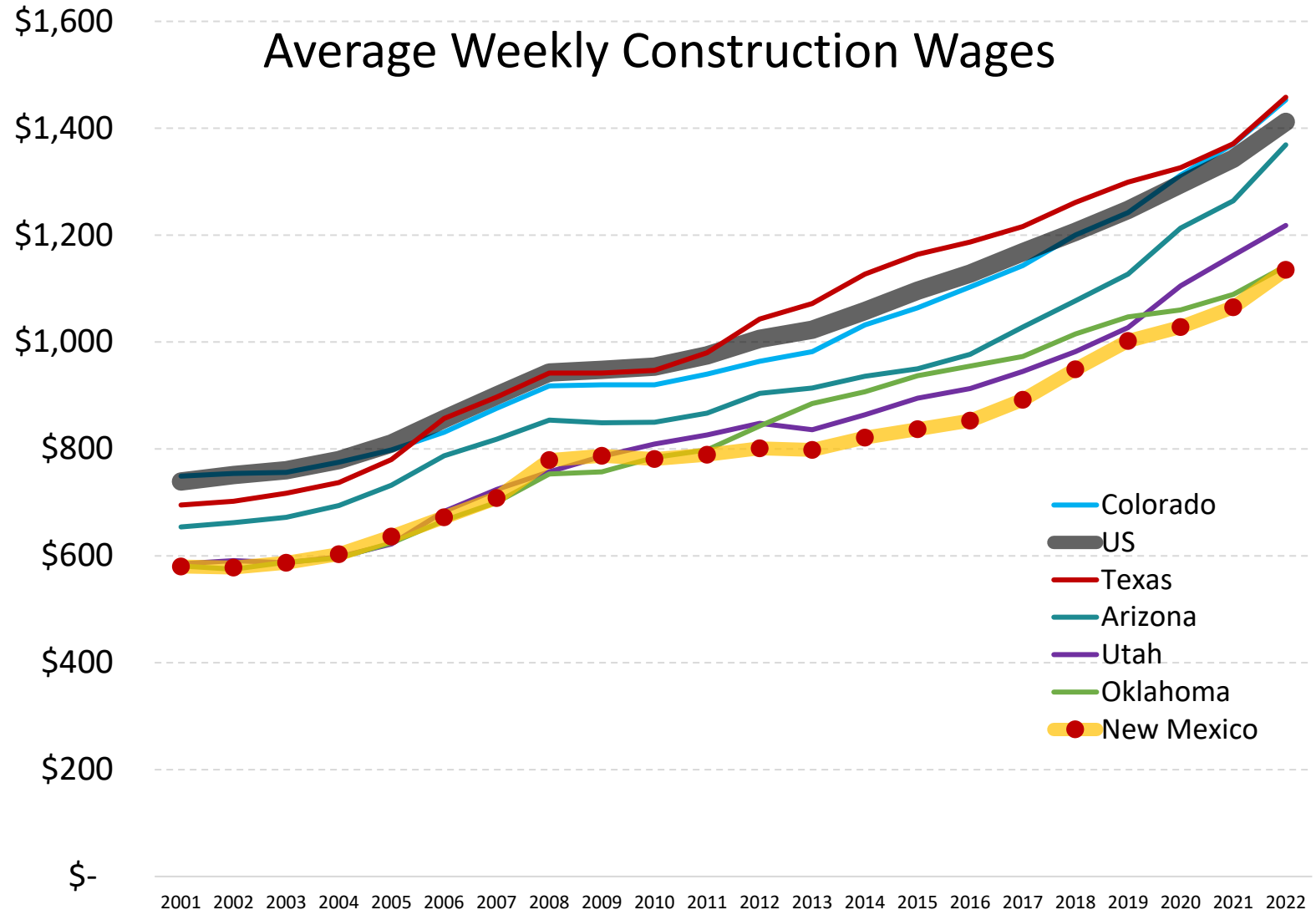
Construction wages in New Mexico are below surrounding states.

In 2010, New Mexico's construction wages were the 7th lowest in the nation. In 2022, they were the 4th lowest in the nation.

On average, New Mexico construction laborers make 20 percent less than the U.S. average for construction workers.

Low wages and busy markets in neighboring states may make it difficult to grow the workforce.

Chart created by Legislative Council Service staff



50 State Data: <https://datawrapper.dwcdn.net/bam73/1/>
County Level Data: <https://datawrapper.dwcdn.net/thVVs/1/>

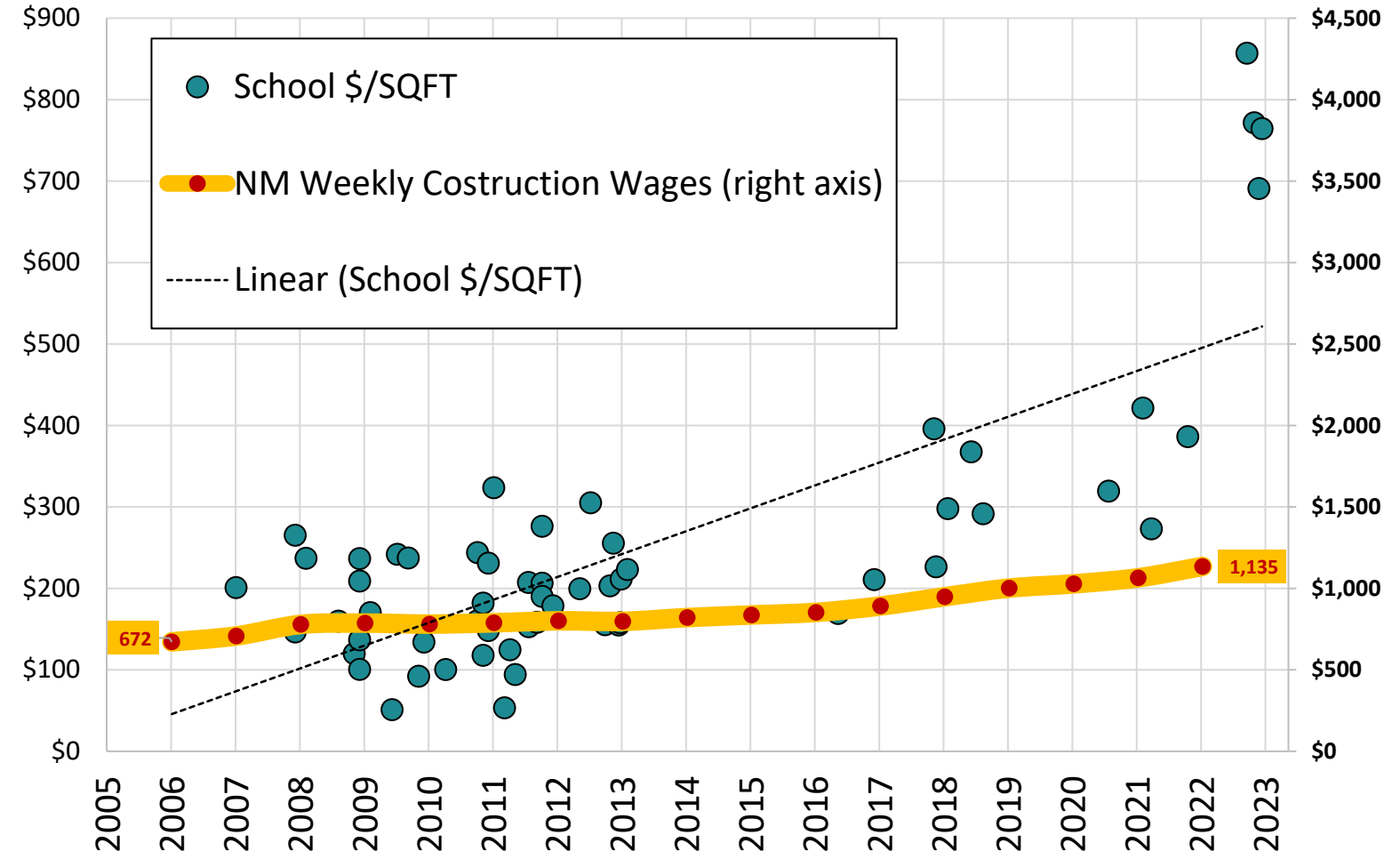
Source: Bureau of Labor Statistics

Supply

Increases in construction wages have not kept pace with increases in construction costs.

Chart created by Legislative Council Service staff

Construction Cost Trends



Policy Considerations

Issue	Considerations and Research Questions
The construction workforce is at capacity	<ul style="list-style-type: none">• Continue investments in career technical education• Effect of project delivery and procurement methods on cost and efficiency• Regional competition and opportunities to attract out-of-state contractors and incentivize rural work• Capital appropriations strategies to prevent flooding the market with new projects
School districts cannot afford their local match, even after SB131 shifts a greater share of costs to the state	<ul style="list-style-type: none">• Update PSCOC waiver policies• Explore options to provide districts with financing options• Revisit state and local match formula

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Q & A