

Arizona roadways to get more bang for their stimulus buck

by *Sean Holstege and Ronald J. Hansen* - Mar. 27, 2009
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The Arizona Department of Transportation has begun soliciting bids for highway projects using the first batch of federal stimulus funds, and it says historic drops in construction costs mean the money likely will pay for more roadwork.

The dismal economy, which is more pronounced in Arizona's hard-hit construction business, has made contractors hungry for work, and bids have been coming in 10 to 20 percent lower than expected.

Arizona should complete more than the 41 stimulus projects planned if ADOT can award contracts before the economy rebounds.

"It means our dollars will go further," U.S. Transportation Secretary Ray LaHood told *The Arizona Republic* on Thursday. "It will last maybe until the economy improves."

Construction prices have fallen sharply since last summer, and state transportation departments across the country are already

realizing millions of dollars in savings as a result.

That was a cornerstone of President Barack Obama's \$787 billion economic-stimulus package: Spend heavily now while there are bargain prices.

So far, the government has steered \$3 billion to 33 states for roughly 1,000 highway projects, LaHood said.

"This is a big infusion of money into the economy," he said.

The window of opportunity won't last indefinitely, and what happens next to the construction economy will dictate how far the state can stretch its stimulus money, or whether savings dry up before they complete the list of highway projects.

For now, a historic global plunge in the prices of materials and a nationwide shortage of construction work will result in bids for stimulus projects up to 20 percent cheaper than comparable projects a year ago, said Kenneth Simonson, chief economist for the Association of General Contractors of America.

"I call it a limited-time sale," Simonson said. "It's the most widespread slowdown in materials in my 37 years as an economist."

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Brutal job market

Simonson's view is shared by the construction industry, highway planners and other economists.

Labor costs, too, are expected to stay low, and nowhere has the construction labor pool been worse hit than in Arizona.

From January 2007 to January 2009, Arizona shed one-third of its construction jobs, nearly triple the national rate of industry job losses. Next worst was Nevada, with a 25 percent decline, and all but one state west of the Continental Divide saw double-digit losses.

Tim James, an economics professor at Arizona State University's W.P. Carey School of Business, says ADOT can expect low bids for the rest of the year.

"I don't think there will be a big price hike later because there are enough people out there hungry for work," James said. "There are some big deflationary pressures at work."

Low bid results

ADOT need look no further than the California Transportation Department, the largest in the country, for proof of favorable bids. In bids opened this month, all but two

came in under estimates, an average of 23 percent lower than expected. The largest, a water-drainage job, came in at less than half the state's official estimate.

"It's consistent with what we've been seeing. We've been running at about 22 percent savings for a while," Caltrans Office Engineer John McMillan said. "It's a great opportunity to keep our program going."

In 2008, ADOT saved \$157 million from lowered bids, or 16 percent of the expected price.

Top ADOT officials told the State Transportation Board and state lawmakers recently that they hope those savings continue to be realized for the \$350 million in stimulus contracts the agency is managing.

The biggest of the 14 projects, worth an estimated \$86 million, that ADOT advertised this week is a \$43 million job to widen Interstate 10 between Verrado Way and Sarival Avenue in the West Valley.

But if costs climb again, as they have in the past after natural and man-made disasters, projects will be cut from the list.

ADOT is meting out work in roughly \$80 million batches to avoid overheating the

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bidding market or slowing down projects by overworking state engineers.

Economists and highway planners think construction prices will stay low until the home-building market rebounds.

Effect on Arizona

Which areas of the state win or lose is a matter of timing. Not all projects or regions are equal because priority lists have been split into three: for Maricopa and Pima counties and the rest of the state. As the money gets spent, ADOT will work down the priorities of each region.

Maricopa County has five large projects on the priority list. Even if savings continue apace, the region still could not afford the next project on its list.

That's not the case in rural Arizona, whose leaders opted for numerous small, mostly repaving jobs, to stimulate the local economy. At the current savings rate, rural Arizona could undertake three more projects, and even more if ADOT directs savings from the other regions.

About half the rural projects involve pavement repairs, heavily affected by the price of asphalt, the tarry byproduct of oil refining used for road surfaces.

Its price, however, is the most volatile of highway-construction raw materials. As the price of crude oil shot up last year, asphalt prices spiked 46 percent by September. When crude fell, asphalt costs slipped 16 percent by January. That makes rural Arizona's projects more susceptible to the swings of the global oil market.

Other essential highway-building materials have fluctuated less.

After steel prices peaked in August, costs slipped 35 percent as the global economy slumped, according to the Producer Price Index kept by the U.S. Bureau of Labor Statistics. But cement costs have been stable since early 2007.

These products are more likely to affect Maricopa County projects, which involve widening roads and improving interchanges.

A more general indicator, the Turner Building Cost Index, measures inflation in the construction industry, accounting for both materials and labor. Over the past year, construction costs have fallen 2.6 percent, according to the index.

The stimulus package, the American Recovery and Reinvestment Act, requires ADOT to spend half the money by July and the rest by mid-February.

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It remains unclear how long ADOT can expect savings on materials and labor to continue, as the commodity markets adjust to stimulus spending and contractors learn from each other's bids.

Political witch's brew

Currently, no plan exists for distributing potential savings or absorbing unforeseen costs.

If the state has to pivot, it sets up another political squabble like the one that occurred early this month when the State Transportation Board decided to allocate stimulus money by a set formula. The Maricopa Association of Governments complained that their region had been short-changed.

"I don't think they've thought through that. If the projects in this area come in under budget, we shouldn't be penalized for costs in another," MAG Transportation Director Eric Anderson said.

ADOT may face political and economic pressure to meet a goal of getting all 41 projects under contract by Memorial Day.

When the first bids come back next month, Arizona will have a better idea how far it can stretch its federal stimulus dollars.

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