2014 ALASKA'S CONSTRUCTION SPENDING FORECAST

Annual Report for the Construction Industry Progress Fund and the Associated General Contractors of Alaska

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Dear Alaskans,

The Construction Industry Progress Fund (CIPF) and the Associated General Contractors (AGC) of Alaska are pleased to have produced another edition of "Alaska's Construction Spending Forecast."

Underwritten by Northrim Bank, compiled and written by Scott Goldsmith, Mary Killorin and Linda Leask of the University of Alaska's Institute of Social and Economic Research (ISER), the "Forecast" reviews construction activity, projects and spending by both the private and public sectors for the year ahead.

The construction trade is Alaska's third largest industry, paying the second highest wages, employing nearly 16,000 workers with a payroll over $1 billion. It accounts for 20 percent of Alaska's total economy and currently contributes approximately $9 billion to the state's economy. The construction industry reflects the pulse of the economy. When it is vigorous, so is the state's economy.

Both CIPF and AGC are proud to make this publication available annually and hope it provides useful information for you.

AGC is a non-profit, full service construction association for commercial and industrial contractors, subcontractors and associates. CIPF is organized to advance the interests of the construction industry throughout the state of Alaska through a management and labor partnership.

Mike Shaw, CIPF Chairman

The 2014 Forecast is generously underwritten by Northrim Bank

OVERVIEW

The total value of construction spending "on the street" in Alaska in 2014 will be $9.2 billion, up 18% from 2013. [1, 2, 3]

Wage and salary employment in the construction industry, which was stable last year at about 16,300, should continue at that level through the next year.[4]

The oil and gas sector will account for most of the growth this year. It will total $4.3 billion, up from $3.2 billion last year.

Other spending will be $4.9 billion, up from $4.6 billion last year.

Private spending, excluding oil and gas, will be about $2.0 billion, up from $1.9 billion last year—and public spending will increase from $2.7 to $2.9 billion.

The robust projection of construction spending in Alaska in 2014 is due to four factors. The largest and most obvious is the petroleum industry's expanded investment plans.

Federal government spending will be higher than anticipated, because of both a larger Department of Defense budget and the one-time re-allocation of previously unspent federal highway funds.

State government spending will also be strong, notwithstanding the reductions in state appropriations for capital projects the last two years. In FY2013 the state appropriated a record high $2.8 billion (including transportation bonds) for capital spending for projects (excluding federal grants). That fell by $1.7 billion in FY2014, to $1.1 billion. For FY2015 the governor has proposed project spending of $0.6 billion.

State-funded construction spending has been largely insulated from that drop, for several reasons. First, the record-breaking appropriation in FY2013 pumped more money into the construction "pipeline" than it could handle, so many projects funded then are only now under construction. Second, many

2014 Alaska Construction Spending

		Level	Change
TOTAL	**$**	**9,176,000,000**	**+18%**
Total Excluding Oil & Gas	**$**	**4,921,000,000**	**+7%**
Private	**$**	**6,267,000,000**	**+24%**
Oil and Gas	$	4,255,000,000	+33%
Mining	$	205,000,000	-34%
Rural Other Basic	$	76,000,000	-280%
Utilities*	$	851,000,000	+17%
Hospitals/Health Care*	$	230,000,000	0%
Other Commercial	$	170,000,000	+13%
Residential	$	480,000,000	+9%
Public	**$**	**2,909,000,000**	**+6%**
National Defense	$	395,000,000	+89%
Highways and roads	$	765,000,000	-5%
Airports, Ports, and Harbors	$	425,000,000	-4%
Alaska Railroad	$	23,000,000	+41%
Denali Commission	$	9,000,000	-31%
Education	$	477,000,000	-2%
Other Federal	$	300,000,000	+20%
Other State and Local	$	515,000,000	+4%

* Many projects in these categories are supported by public funds.
Source: Institute of Social and Economic Research, UAA. Percent change based on revised 2013 estimates.

[1] Our revised projection for 2013 was $7.8 billion, slightly lower than originally estimated. The revision is based primarily on lower than anticipated oil and gas spending in 2013.

[2] We define construction spending broadly to include not only the construction industry as defined by the U.S. Department of Commerce and the Alaska Department of Labor, but also other activities. Specifically, our construction-spending figure encompasses all the spending associated with construction occupations (including repair and renovation), regardless of the type of business where the spending occurs. For example, we include the capital budget of the oil and gas and mining industries in our figure, except for large, identifiable equipment purchases such as new oil tankers. Furthermore, we account for construction activity in government (like the carpenter who works for the school district) and other private industries. The value of construction is the most comprehensive measure of construction activity across the entire economy.

[3] "On the street" is a measure of the level of activity anticipated during the year. It differs from a measure of new contracts, because many projects span more than a single year.

[4] Alaska Department of Labor

projects now receive only partial funding in a single year—so many projects from the large budget years are still seeking additional funding to start or continue to completion. Third, the FY2013 bond appropriation has yet to be fully utilized. Also, many of the projects approved in the record capital budget were not construction-related.

Finally, the economy has continued to grow, adding jobs and population. This fact, together with the renewal of cautious optimism in the oil patch, has led to higher private spending in the residential and commercial construction sectors.

Most of the uncertainty in the forecast this year is in the oil and gas sector. We assume that the oil and gas companies will be largely successful in carrying out the plans they have announced for the year.[5] But plans can and do change, because of many factors associated with weather, logistics, availability of supplies, evaluation of work completed, regulatory and environmental challenges, prices of oil and gas, and other operational and strategic concerns. The continued uncertainty about the future direction of state petroleum tax policy, possible new energy policy initiatives put forward by the second Obama administration, and the prospects for construction of a gas pipeline to commercialize North Slope gas add a cautionary note not only to industry planning, but to the entire economy.

As in past years, some firms are reluctant to reveal their investment plans, because they don't want to alert competitors; also, some have not completed their 2014 planning. Large projects often span two or more years, so estimating "cash on the street" in any year is always difficult—because the construction "pipeline" never flows in a completely predictable fashion.

Tracing the path of federal spending coming into Alaska without double counting is also a challenge, and as the state capital budget grows it becomes more time-consuming to follow all the flows of state money into the economy.

We are confident in the overall pattern of the forecast—but as always, we can expect some surprises as the year progresses.

Kuparuk Airfield, Granite Construction

PHOTO BY DANNY DANIELS

UAA Sports Complex (Alaska Airlines Center), Anchorage, Cornerstone General Contractors

PRIVATELY FINANCED CONSTRUCTION

Oil and Gas: $4,255 Million

The biggest sector, and the one projected to increase the most this year, is oil and gas. We expect that if actual spending matches the announced plans and past experience in the industry, spending will be up 33% from $3.2 billion last year.

The growth is being driven by the continuing high price of oil, the increase in the cost of inputs to all phases of oil and gas operations, the growing need to maintain the aging infrastructure and facilities on the North Slope and in Cook Inlet, and perhaps most importantly, by the climate of optimism created by passage of the new production tax on oil and gas that went into effect at the start of 2014.

On the North Slope, Conoco Phillips will be conducting exploratory drilling at Kuparuk and in the NPRA (National Petroleum Reserve Alaska) west of the Colville River, where the company hopes to develop the Greater Moose's Tooth Prospect. Conoco's largest project will be developing the CD-5 satellite, also west of the Colville River and the Alpine field. Work this year will include a bridge, module installation, and pipeline fabrication. British Petroleum has announced an expanded capital budget this year, with concentration on more well workovers and well stimulations at Prudhoe Bay. The company has also begun to re-evaluate its Liberty prospect, and expects to increase capital spending by several billion over the next five years. Exxon Mobil is continuing work on development of its Point Thomson field.

Shell Oil is hoping to come back and complete the well it started to drill in 2012, on the OCS (Outer Continental Shelf) in the Beaufort Sea. Meanwhile, Statoil has not announced any plans to explore its prospects in the Beaufort Sea.

Also on the North Slope, ENI is continuing to drill wells in the Nikaitchuq field, and Savant is re-working wells at Badami. Pioneer has plans to expand its facilities at the Oooguruk field, with an additional onshore production pad and expanded island.[6]

[5] Some companies new to Alaska have tended to be overly optimistic in the last couple of years.

[6] Pioneer recently sold its assets to Caleus.

Eva Creek Wind Farm, Brice Inc.

Brooks Range Petroleum is working to develop the Mustang field, west of Kuparuk, with financial assistance from the Alaska Industrial Development and Export Authority (AIDEA).

Repsol, Linc Petroleum, and Nordaq Energy are all planning exploratory wells this year, and Great Bear will be doing seismic work but no drilling.

A number of other companies, including Chevron and Anadarko, have interests in various fields on the North Slope but are not operators. Their expenditures are also included in the total.

Work continues on maintaining the TAPS (Trans Alaska Pipeline System) oil pipeline and modifying it to meet the challenges of reduced flow.

Spending in Cook Inlet will be dominated by Hilcorp, a relative newcomer to Alaska that recently purchased the assets of both Chevron and Unocal. Hilcorp drilled 10 new wells in 2013, and plans are for a similar number this year.

Buccaneer, Furie, and Cook Inlet Energy are the other most active players in Cook Inlet. Buccaneer has been using the jack-up rig *Endeavor* to explore in the Cosmopolitan unit. (It is also developing and operating fields on shore.) Furie used a second jack-up rig to develop its Kitchen Lites prospect and is currently installing the first new production platform there since the 1980s. Cook Inlet Energy is working several different fields.

Other companies active in Cook Inlet include Armstrong, Apache, Nordaq, Aurora, and XTO.

Elsewhere in the state, there will be exploration for gas near Nenana and Copper Center.

Mining: $205 Million

Spending by the mining industry—on exploration and development,[7] as well as maintaining and upgrading existing mines—will be lower in 2014 due to the drop in the price of gold.

Spending on maintenance, continued exploration, and new facilities at the six large operating mines will be $110 million. Spending for drilling and other site work will be down this year at the three world-scale mine projects currently in various stages of review (Donlin Creek, Pebble, and Livengood).

Numerous smaller projects across the state, such as the Bokan rare earth metals prospect in the Southeast, and the Nova Gold upper Kobuk mineral project, will see activity.

PHOTO COURTESY KEN GRAHAM PHOTOGRAPHY

Providence Alaska Cottages, Anchorage, Davis Constructors and Engineers and Superior Plumbing and Heating

Other Basic Industries in Rural Alaska: $76 Million

Investments in facilities to support tourism, the seafood and timber industries, and other natural resource industries often occur in rural areas. Holland America is planning extensive upgrades to a newly purchased hotel outside Denali National Park, and a new hotel is under construction on the North Slope. Two seafood processing plants, with total construction spending of $60 million, are planned for Naknek.

Utilities: $851 Million[8]

Spending for new and upgraded electric generating plants will drive utility spending higher this year.

Two new large plants will be under construction this year—the MEA (Matanuska Electric Association) plant at Eklutna, and the AML&P (Anchorage Municipal Light and Power) replacement plant in northeast Anchorage. GVEA (Golden Valley Electric Association) has taken over the Healy Clean Coal plant and plans there include spending for upgrades and emission control systems.

Smaller utilities are involved in a number of hydroelectric projects, including Blue Lake at Sitka and Allison Creek at Valdez.

Other electric utility projects involve renewable sources like wind and biomass, bulk-fuel upgrades, and other system efficiency upgrades financed partially through programs like the Renewable Energy and Energy Projects appropriations in the state capital budget.

Telecommunications spending will also be higher this year, driven by new firms moving into the market (Verizon), as

[7] Excluding exploration and development costs associated with environmental studies, community outreach, and engineering.

[8] Although we include utilities and hospitals/health care spending in private spending, there is also a significant amount of public spending for some projects in these categories.

well as continued expansion and upgrading of facilities by existing companies like GCI and Alaska Communications. Telecommunications spending in Alaska benefits from funds generated by the Universal Service Funds, which channel revenues collected from services provided in other locations to help pay for needs in Alaska.

Spending by ENSTAR, the natural gas utility, will be up as it continues expansion in the Homer area. But the state project to transport LNG from the North Slope to Fairbanks has yet to get underway.

PHOTO COURTESY KEN GRAHAM PHOTOGRAPHY

Providence Generations Surgery Center, Anchorage, Davis Constructors & Engineers

Hospitals and Health Care: $230 million

Spending was down in 2013, because new hospitals had been completed at Barrow, Nome, and Fairbanks. Spending for hospitals and other health care facilities in 2014 should be about the same as last year.

Hospitals around Alaska are continuously renovating and expanding. This year the largest planned project is at the Alaska Native Medical Center in Anchorage, where a state-financed residential housing facility for patients and their families is scheduled for construction, along with a new parking garage. Providence Hospital is nearing the end of its multi-year "Generations" expansion project, and Alaska Regional Hospital has announced modest renovations. Expansions are also expected to begin at hospitals in Ketchikan and on the Kenai Peninsula.

Smaller projects are underway across the state, in response to the growing need and aging of the population. For example, a new blood bank facility in Anchorage, and a long-term care facility for veterans in Haines, will be under construction.

No large projects have been identified for military hospitals this year.

PHOTO BY DANNY DANIELS

Tolsona River Bridge (Glenn Highway), Mowat Construction

Other Commercial: $170 Million

Commercial construction spending consists primarily of office buildings, banks, hotels, retail space, and warehousing.[9] The level of spending from year to year can be influenced by a few projects, like large office buildings. Vacancy rates for commercial space have been falling over the last three years in the larger markets, and we project modest growth this year in office space in response to both the tightening of supply and the expectation of future need associated with expansion in the oil patch. For example, Cook Inlet Regional Corporation (CIRI) is building a new larger headquarters to replace its existing building in Anchorage.

New national chains, such as Cabela's and Bass Pro shops, continue to move into the Alaska market, and a large new shopping mall is planned for the Mat-Su Borough, in response to a growing population there.

Residential: $480 Million

The residential housing market continued to tighten last year, as reflected in rising prices, higher rents, lower vacancies, and quicker sales—but that was not reflected in construction activity. For example, the number of new residential building permits in Anchorage did not increase last year.

We expect that the upward pressure on the market will result in a modest increase in new housing starts this year in the major markets in the Railbelt and Southeast.

PUBLICLY FINANCED CONSTRUCTION

National Defense: $395 Million

Defense spending, which had been falling and was projected to continue to shrink as the federal budget tightens, will take a

[9] Our commercial construction figure is not comparable to the published value of commercial building permits reported by Anchorage and other communities. Municipal reports of the value of construction permits may include government-funded construction, which we capture elsewhere in this report. We have also excluded hospitals and utilities from commercial construction, so we can provide more detail about those types of spending.

Seward Highway Reconstruction, Anchorage, QAP

big jump this year. The budget for MILCON (military spending for facilities on bases), which was only $33 million last year, is forecast to be $103 million. Funding includes seven new projects at Fort Wainwright, of which the largest is a $36 million warm-storage hangar. The environmental program budget, including FUDS (Formerly Used Defense Sites), will also be larger, at $127 million in 2014. This program includes cleanup of hazardous substances and contaminants at former defense sites as well as on current Army and Air Force installations.

Spending on the smaller civilian programs and other interagency programs will be similar to that in past years. This spending mostly funds Corps of Engineer projects for other federal agencies, and projects done in cooperation with Alaska communities, such as harbor improvements.

Missile defense spending, concentrated at Fort Greely, will increase this year to $90 million from only $18 million last year. This is the start of an announced $1 billion expansion that will add 14 interceptor missiles to the defense system at Fort Greely over the next several years.

Transportation—Highways and Roads: $765 Million

Spending on highways and roads will be marginally lower this year, because the large Tanana River Bridge project is nearly complete, and road funding from state sources is marginally lower.

But federal funding for highways will be at an all-time high, because the state was able to re-obligate about $100 million of unexpended federal dollars it had received in years past. Together with the annual federal appropriation under MAP21 (the Federal Transportation Reauthorization Act) and the state matching money, there should be more than $500 million available this year for highways funded through federal programs.[10]

These funds will pay for major projects throughout the state, such as reconstruction along the Parks highway, pavement preservation on the Seward and Sterling highways, bridge construction in Aleknagek, and extension of major arteries in Anchorage. Some federal funds also go directly to Alaska Native tribal organizations for transportation projects.

The state also funds road construction through both the Department of Transportation and grants disbursed by the Department of Commerce, Community, and Economic Development. This source of funds will be marginally lower this year because the large size of the grant program in FY 2013 was not repeated in FY2014. Some money was also allocated for the state's Roads to Resources program, largely for continued planning. The state will continue to pay for deferred maintenance.

The $453 million state general obligation bond package for transportation that passed the legislature in 2012 included $227 million for highways and $35 million for bridges, with the rest allocated to ports. But not much highway construction associated with that bond package is expected in 2014. The bond money was divided between state highway construction and grants to local communities. Some of the specified projects are not yet "shovel ready," so it will take some time before this money hits the street. Also, many of the projects will need additional appropriations by the legislature to be fully funded and put out to bid.

The current federal legislation under which transportation funding is allocated to the states is scheduled to expire later this year. There is concern that Alaska will receive a smaller share under any new legislation.

Transportation—Airports, Ports, and Harbors: $425 Million

Federal funds, mainly from the Federal Aviation Administration's AIP (Airport Improvement Program), will provide the bulk of funding for airport improvements both at the large international airports in Anchorage and Fairbanks and

[10] Not all of the federal appropriation funds highway construction because it also includes the funding for the marine highway system and research and planning of transportation facilities.

PHOTO BY DANNY DANIELS

Cuddy Park Playground, Anchorage, JTA Construction

the smaller state-owned airports across the state. Major planned improvements at the Kodiak airport will boost airport spending marginally higher than last year.

Spending related to ports and harbors will be less than last year, because no activity is anticipated for the Port of Anchorage. A combination of federal funding, state general funds, the transportation bond package, and local sources is supporting many smaller projects around the state, including at Ketchikan, Port Lions, and Homer. No major work is yet underway to expand the Seward Marine Industrial Park to overwinter the Bering Sea fishing fleet, and potential expansion of Nome and Kotzebue harbors to provide a base for Arctic operations is still on hold.

Spending for the railroad spur line to the port at Point MacKenzie in the Mat-Su Borough is expected to be up this year, as construction continues.

Alaska Railroad: $23 Million

The core capital construction program for modernizing and upgrading the Alaska Railroad will be modest this year. State funding will allow continued work on a federally mandated collision avoidance system, a large, multi-year project. (Spending for the Tanana River bridge and the Port McKenzie rail extension are included in other parts of this report.)

Denali Commission: $9 Million

The Denali Commission—an innovative federal-state partnership Congress created in 1998 to more efficiently direct federal capital spending to rural infrastructure needs—continues to decline in importance. Most of its modest capital budget will be for energy-related projects.

PHOTO BY DANNY DANIELS

Tanana Chiefs Conference, Chief Andrew Isaac Health Care Center, Fairbanks, GHEMM Company

Education: $477 Million

Spending for education will be lower this year. In the past two years, the state has appropriated general funds for construction of several new rural schools, as part of the settlement of the Kasayulie case. Two of those schools, at Emmonak and Koliganak in western Alaska, will be largely completed in 2014. Construction will be underway at another, in Quinhagak, but construction at Nightmute and Kwethluk will not begin until next year. The general fund also contains numerous education-related grants for local school districts throughout the state.

New schools will be under construction in Valdez and Kodiak, and several in the Mat-Su Borough alone, funded by local bonds that are largely reimbursed by the state. Local school bonds in Anchorage, Fairbanks, the Mat-Su Borough, and elsewhere are also funding a large number of upgrades and renovations for other educational facilities.

University of Alaska construction spending will be lower this year, as the new Seawolf Arena in Anchorage is completed. Work in Anchorage will also include the building portion of the new engineering complex and renovations of several older buildings. In Fairbanks, work will also continue on a new engineering building as well as expansion of the Wood Center dining facilities. A variety of projects are also planned for the community colleges around the state.

Other Federal: $300 Million

Other federal construction should be higher this year due to an increase in direct procurement, led by spending by the Coast Guard on housing in Kodiak and a hangar at Cold Bay. Direct spending by other federal agencies—the Department of the Interior (National Park Service, U.S. Fish and Wildlife Service, and Bureau of Land Management), the Postal Service, the Department of Agriculture, and NOAA (the National Oceanic and Atmospheric Administration)—will be modest.

In addition to funding a large share of spending on transportation infrastructure through grants from the Department of Transportation, the federal government funnels construction dollars to the state though many other programs.[11]

[11] It is difficult to track all the federal dollars that find their way into construction spending in the state, because there are so many pathways, and they change every year. The possibility of double counting funds as they pass from agency to agency, or become part of a larger project, also creates difficulties for the analyst.

Akutan Airport, Kiewit Infrastructure West

PHOTO BY DANNY DANIELS

Municipality of Anchorage, Fire Station 5 Replacement, Roger Hickel Contracting

Most of the funding for the state- administered Village Safe Water program for rural sanitation comes from federal sources, including the Environmental Protection Agency and the Indian Health Service. With the state contribution, it is expected to be constant at about $60 million this year. Other types of federal grants fund armories and veterans' facilities and ferry terminals, among other things.

The federal government also provides construction grants to Alaska tribes, non-profit organizations, and local governments across the state.[12] Alaska Native non-profit corporations, housing authorities, and health-care providers receive most of this money. The largest of these programs in Alaska is NAHASDA (the Native American Housing Assistance and Self-Determination Act), which provides about $100 million annually for housing construction in Alaska Native communities, through grants to federally recognized tribes and Alaska Native housing authorities statewide.

Other State and Local: $515 Million

State and local government capital spending—excluding transportation (roads, airports, and ports), education, health, and energy—will be marginally higher this year, as many of the projects in the large state capital budgets of the last two years are completed. Many of these projects were funded through the grants by the Department of Commerce, Community and Economic Development to local governments and non-profits throughout the state.

The state budget also includes the ongoing state weatherization and home energy rebate programs, which have now been expanded to include commercial buildings. Work is expected on a number of state-funded buildings, including the new library-museum in Juneau. The first phase of the South Denali visitor center should be completed. This category also contains about $100 million of deferred maintenance spread across all state departments.

Local government capital spending, from general funds and bonds as well as enterprise funds and direct federal grants, tends to be modest and stable from year to year. A large share of this spending is for water and sewer facilities, but it also includes other construction, such as buildings, recreational facilities, and solid waste facilities.

[12] Federal spending on health care projects for the Alaska Native community funneled to Alaska Native organizations is included in the Hospital/Health Care section of this report.

Cover Photo: Alaska State Crime Lab, Anchorage Neeser Construction

WHAT'S DRIVING SPENDING?

The three primary drivers of construction spending are private basic sector investment (mainly petroleum and mining), federal spending (military and grants to state and local governments and non-profit organizations), and state capital spending (which ultimately depends on petroleum revenues), through the general fund and bond sales.

These large external sources of construction funds also give a general boost to the economy—and thus add to the aggregate demand for new residential, commercial, and private infrastructure spending.

CONSTRUCTION IN THE OVERALL ECONOMY

Construction spending is one of the important contributors to overall economic activity in Alaska. Annual wage and salary employment in the construction industry in 2013 was about 16,300 workers, with an average annual payroll of $70 thousand, second only to mining (including petroleum). But that figure doesn't include the "hidden" construction workers employed in other industries like oil and gas, mining, utilities, and government (force account workers). In addition, it does not account for the large number of self-employed construction workers—estimated to be about 9,000 in 2011.

Construction spending generates activity in a number of industries that supply inputs to the construction process. These "backward linkages" include, for example, sand and gravel purchases (mining), equipment purchase and leasing (wholesale trade), design and administration (business services), and construction finance and management (finance).

The payrolls and profits from this construction activity support businesses in every community in the state. As this income is spent and circulates through local economies, it generates jobs in businesses as diverse as restaurants, dentists' offices, and furniture stores.

Ketchikan Berth I and II Rehabilitation, Orion Marine Contractors