# GSA Construction Funding Evaporation and Its Implications

By Timothy Hughes

For the past three years, the commercial construction industry has been battered by a challenging economy, extremely high unemployment and little signs of consistent private sector growth.

The one consistent spot has been government spending. Between typical infrastructure spending at the local, state and federal level, and the influx of funding from the American Recovery and Reinvestment Act of 2009 (the so-called *Stimulus*), government spending on construction expanded significantly. This infrastructure investment has halted precipitously over this year, drastically changing the construction economy moving forward. Considering the current national political landscape, all signs point towards more significant changes for the industry over the next several years.

## The U.S. General Services Administration (GSA) Footprint, Nationally and Regionally

GSA owns and leases over 354 million square feet of space in 8,600 buildings nationwide. In its role as the coordinator of the federal government's various real estate holdings and ventures, GSA helps shape the marketplace through is procurement, design and construction efforts.

GSA's regional impact is proportionally even greater than its nationwide presence. GSA's National Capital Region oversees a portfolio of 96 million rentable square feet, consisting of 53 million square feet of leased space and 43 million square feet of owned space in Washington D.C. and surrounding areas, making its impact on the regional economy significant.

## Recent Stimulus and GSA Funding for Construction

GSA reported a net funding level of $894 million for FY 2010 for construction and acquisitions. Given that much of GSA's funding for its projects comes from fees paid to GSA by the various agencies utilizing facilities, GSA's facility spending impact is significantly broader than its budgeted net federal funding.

In addition to the standard FY 2010 budget, GSA received a significant portion of stimulus funding totaling over $6.7 billion. Most of the funds were dedicated towards infrastructure and energy, with $4.5 billion directed towards conversion of GSA facilities to high-performance green buildings, $1.05 for construction of new buildings and $300 million for upgrading the federal motor fleet.

## The Axe Falls in April

The federal political and budgetary debate translated to particularly significant cuts for GSA. In April 2011, Congress failed to adopt an actual budget and instead provided for a continuing resolution (CR) that ravaged GSA's construction budget. GSA's request for 2011 included $676.3 million for new construction and $321 million for significant renovations, with a planned 2012 request of $840 million for new construction and $869 million for renovations.

The April CR simply evaporated GSA's funding. Only $82 million was approved for construction and acquisition and $280 million for repair of federal buildings and courthouses. Of that $82 million, $30 million was dedicated towards the re-purposing of the old St.

Elizabeth's Hospital in Washington, D.C. for the Department of Homeland Security. Another $44 million went to funding the FDA's facility at White Oak. ***This left around $8 million for literally all the remaining projects of GSA nationwide.*** Needless to say, that $8 million does not go very far.

FY 2012 is still up in the air. Initial action in the House of Representatives zeroed out GSA's new construction budget; and recent Senate appropriations called for $65 million for construction and acquisition and $280 million for repair. Given the current state of federal politics, predicting an end result is very difficult, but it is clear that GSA is dealing with a *new normal* in terms of construction and acquisition funding.

### Regional Ripple Effect

After dominating much of the local commercial real estate discussion, GSA vanished from deals for the first half of 2011. The national political debate appeared to freeze GSA in place as the agency attempted to sort out where the funding would be and what the implications would be for leasing and property acquisition. More recently, the deal flow has begun to return albeit in different form. GSA has begun to approve lease renewals in existing facilities and put out some solicitations, and the House subcommittee overseeing government real estate has in turn begun to move some of these deals forward. The current budget fights mean that incumbent landlords with GSA as a tenant likely hold a tremendous competitive advantage and that GSA's deals are likely to consist primarily of lease renewals for some time.

The drying up of funding leaves the status of the very significant project at St. Elizabeth's somewhat uncertain. Other projects nationally will continue to face impediments as well, potentially leading to projects being shelved during construction and resulting delays, cost impacts and disputes.

### The Impact on Green Building

GSA has long been a thought leader with regards to sustainable design and construction. This leadership was demonstrated most recently by GSA's 2010 announcement that all their new construction needed to obtain a LEED Gold rating from the USGBC.

What is clear is that with no new construction, this requirement becomes a window dressing. GSA funneled many new construction projects, as well as existing buildings and tenant lease facilities, into the USGBC's LEED rating program. Evaporation of funding for new construction and new leased facilities means that GSA will not be a source of significant influx of green building projects into the LEED rating pipeline. Coupled with the end of the stimulus funding and its significant source of funding for retro-fitting buildings, it remains to be seen what the scope of the impact is on USGBC moving forward.

### The State of the Construction Economy

Beginning in July 2008 when the construction industry had eight percent unemployment, unemployment rates increased dramatically, reaching peak unemployment of 27.1 percent in February 2010. Since then, the rate has dropped back down to 13.3 percent. While still well above the eight percent starting point, this rate is obviously a big improvement over the recent high point.

The real question is how much this improvement may be directly attributed to federal and other government spending. As the stimulus funding dries up and governmental budget cuts result in the drastic curtailing of government funded construction, will construction firms be forced to cut back their workforce again? As it stands today, the private sector has yet to fully ignite so we may not see private sector jobs take up the slack created by governmental funding cuts.

### What Is Next?

Taking out the crystal ball, it is likely that we will continue to see ugly, bruising fights in Washington over funding and budgets. This likely will translate to the use of continuing resolutions rather than annual budgets. We will also likely see some level of interim funding towards GSA that is sufficient to keep the couple of big local projects moving forward; however, we are likely to see neither a dramatic increase in GSA funding nor a complete end to such funding. A fair estimate is funding in the $30 to $80 million range for construction and acquisition and little more.

So what happens next? Stimulus funding is already starting to run out and talk about bidding at or below cost in order to keep some level of cash flow continues in the construction community. ***This is simply not sustainable.*** The private sector needs some level of consistent confidence and growth in order for the resurgence of the construction industry to continue.

Smart contractors need to hedge themselves against the termination of government funding for construction and anticipate that the highly competitive bidding environment will continue over the next several years. Many contractors who traditionally did not perform government work flocked in that direction over the last few years; watch for that same flow to reverse as many traditionally government space players try to push into the commercial market over the next two years in reaction to these macro funding trends.

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