

OBO Industry Advisory Panel Meeting Sept 18, 2008

Cost Management in a Changing Construction Marketplace

How are the public and private sectors dealing
with ever changing global dynamics?

OBO Champion – Kathy Bethany Cost Management Division Director

IAP Members:

Douglas Noonan representing CoreNet

Satch Pecori representing ACEC

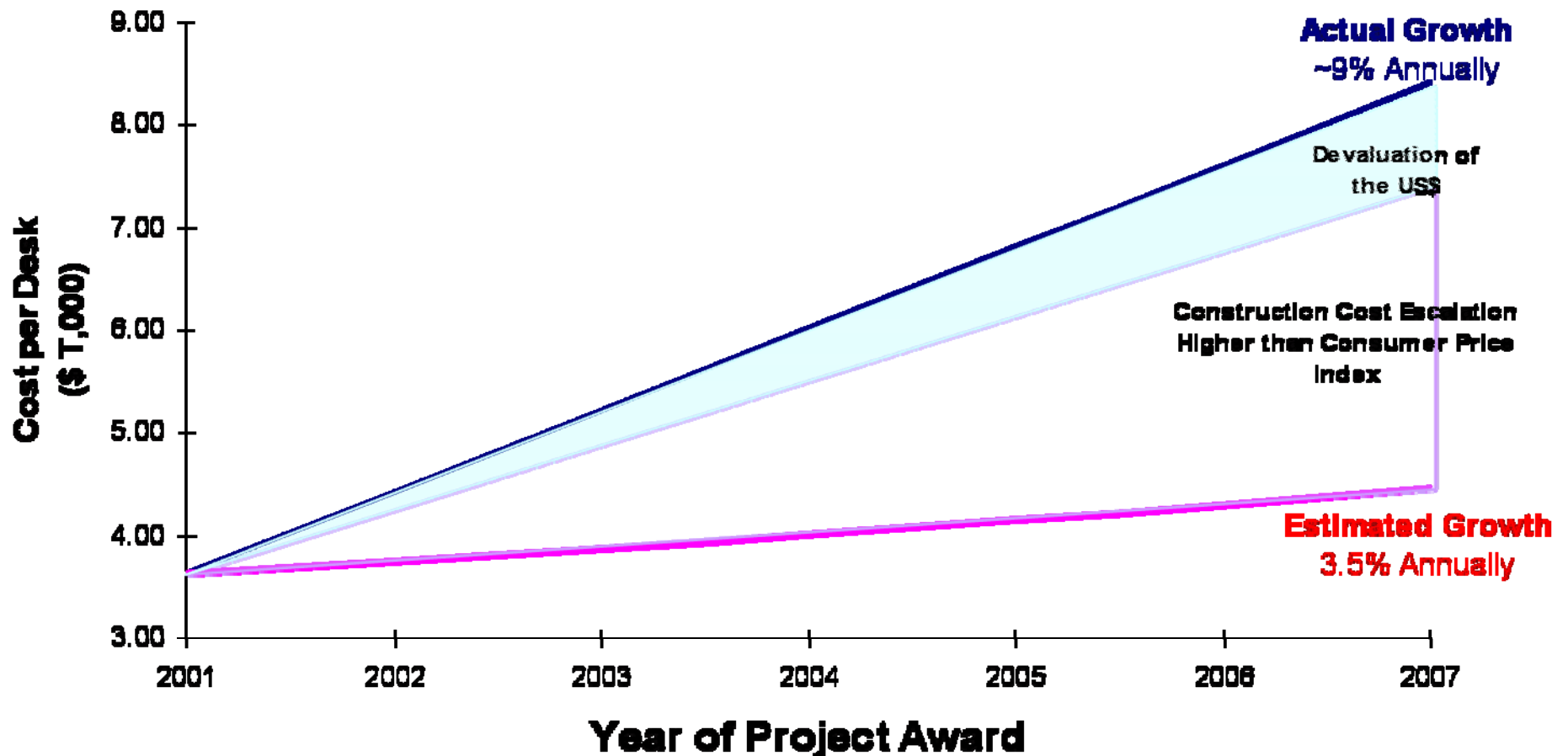
William Browning representing USGBC

Special Guest Speaker: Ken Simonson; AGC Chief Economist



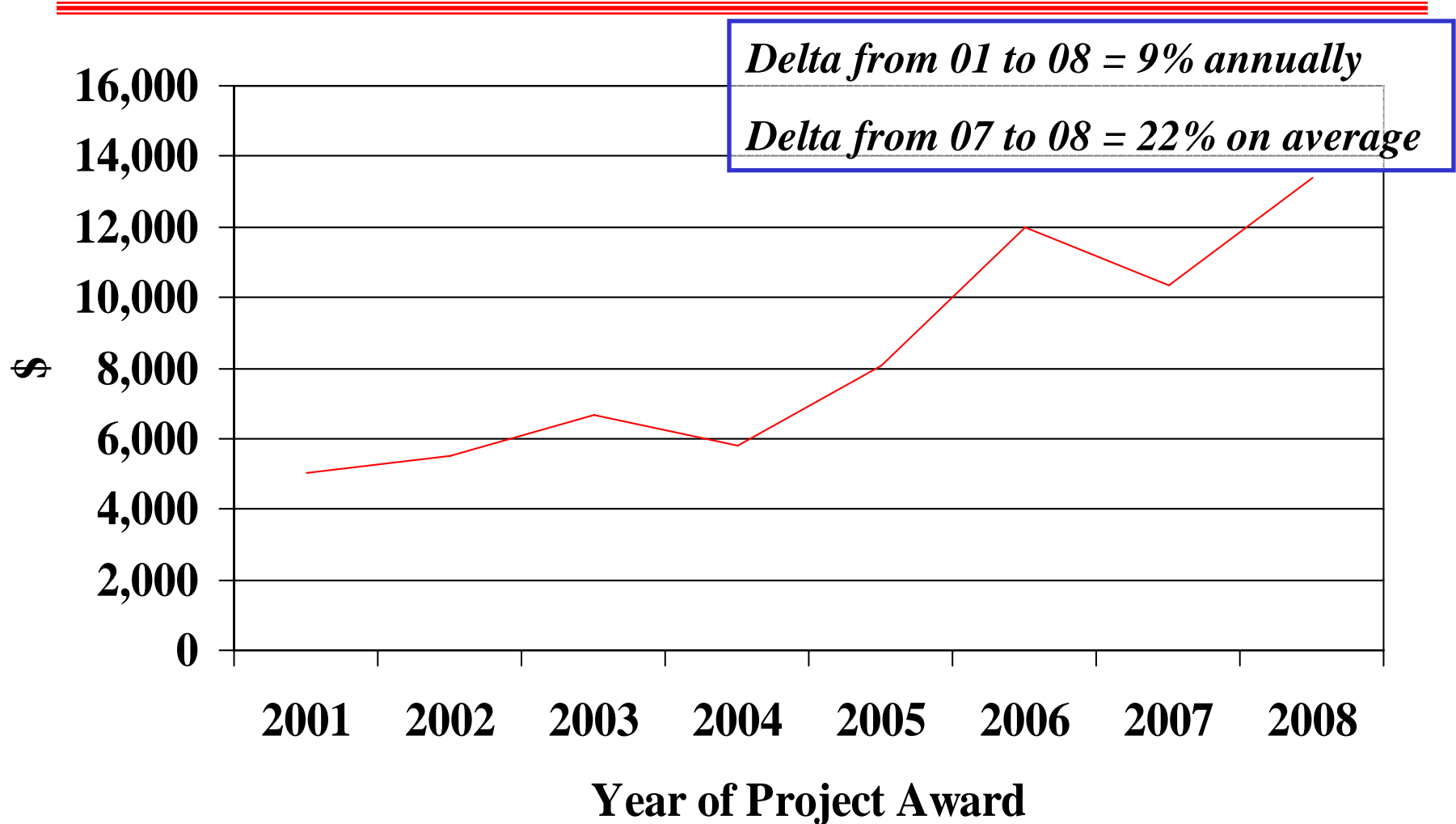
Why is this a problem?

NEC Costs





Average Cost of OBO NECs per GSM





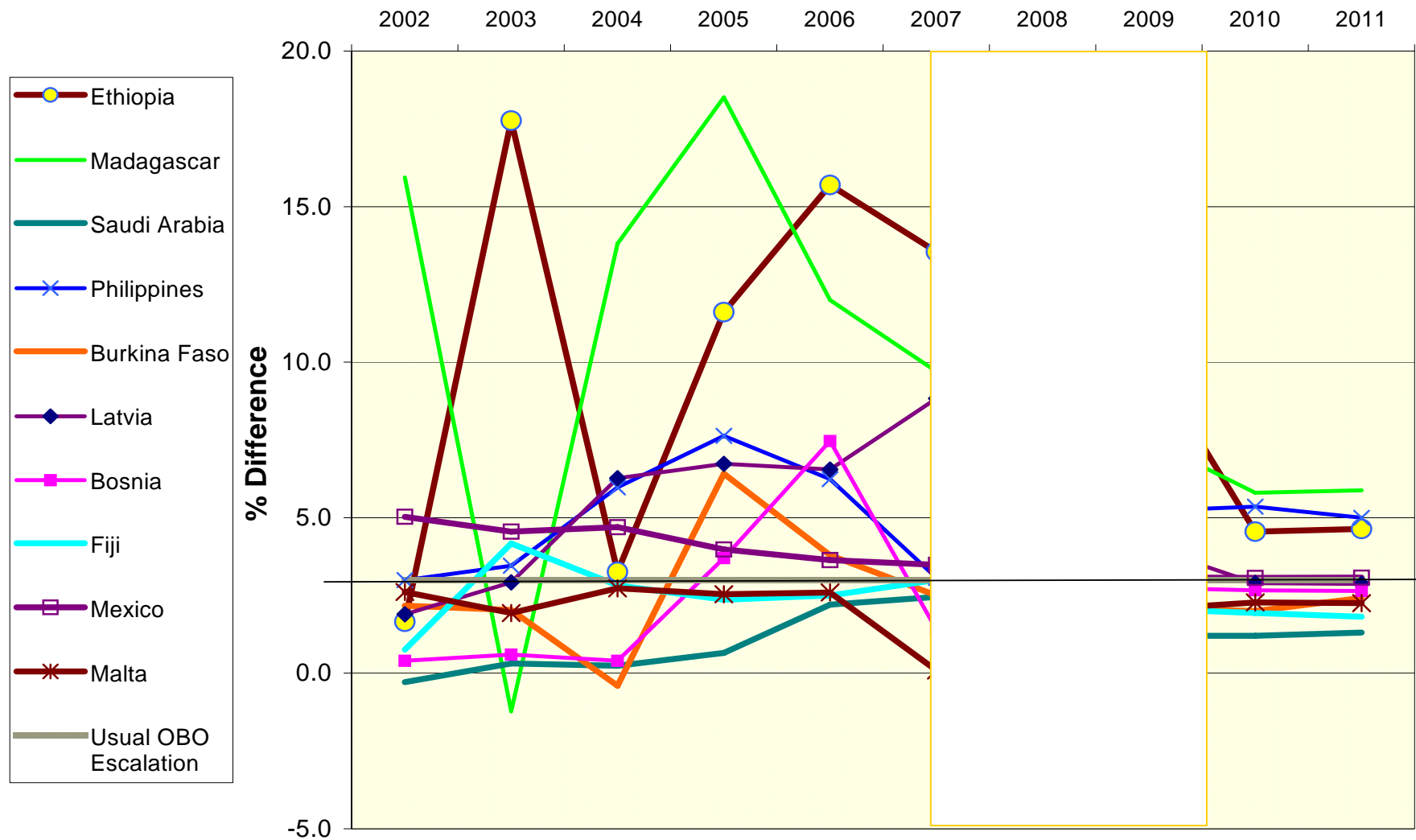
OBO CMD Escalation and Cost Alerts Report Sample

Issue	Source of Info	Potential Impact	Suggestions for Solving Problem
Rebar prices currently trending down are forecasted to rebound to the \$600/TN level in 2008.	ENR 2Q Cost Report of June 2007	2008 and 2009 program Construction cost increases	
Structural Steel prices continue to rise and are forecasted to reach beyond the \$800/tn level in 2008.	ENR 2Q Cost Report of June 2007	2008 and 2009 program Construction cost increases	
Overall materials costs for construction predicted to rise at a 6% to 8% rate, with wages rising at 5% by the end of 2007	Association of General Contractors (AGC) Construction Inflation Report	2008 and 2009 program Construction cost increases	Review Escalation Rate and redo as appropriate
Incentives to attract workers including higher per diem rates and guaranteed overtime could add up to 15% to project labor costs. Increase not reflected in any industry statistics or indexes.	ENR 2Q Cost Report of June 2007	2008 and 2009 program Construction cost increases	Review Labor Rates & Actual awards to determine if this is affecting our projects – if so change our labor rates
The gap between General Purpose Cost indexes and Seller price indexes trend continued in the 2 nd Qtr 2007	ENR 2Q Cost Report of June 2007	Evaluate 2007 proposal prices for potential impact	Monitor and analyze.



CPI Escalation Trends – Aug 2007

CPI Escalation Trends from Global Insights





Reasons for Cost Increases (prepared in July 2008)

What	Amount used on Medium SED		Cost increase of:
Shipping –167% increase 40’ container to China from \$3,000 to \$8,000 – Projected cost of \$15,000 if fuel goes to \$200/barrel	200 containers		\$1.0M
Skilled Cleared US worker – 15% increase in price	66,000 Hours		\$0.8M
Rebar --92% increase in six months	1,600 Tons <i>main building only</i>		\$1.0M
The Bern project contained approx \$1.7M for the Vault (steel walls) this increase would cost \$2M or 6% increase in the cost of the project.			
Construction Prices increased at a 19% annual pace in the first five months of 2008.			\$19M for average NEC
US Dollar reduction against Euro – 13%			\$13M for average NEC
Airline Tickets (what our contractors pay)	<ul style="list-style-type: none"> • DC to Dubai 38% increase in the last 3 months • DC to Thailand 52% in the last year 		
Diesel Fuel – 58% increase in one year (and counting)	\$3.00/Gal in 07/07	\$4.73/gal in 07/08	



Material Costs

- Given the fluctuation for cost on basic materials such as steel, copper, cement, etc., how are you able to manage cost escalation on projects?
 - OBO tracks material costs both globally and in the specific project area adjusting estimates accordingly
 - Considerations under discussion are:
 - Contract Escalation clause e.g. allowing some commodities to be proposed with prices tied to a generic metric like the CPI
 - Estimating all projects in current year \$, and having a separate line item for escalation/currency fluctuation. So that if escalation/currency flux is greater than anticipated we'd have management reserve in the project budget



Fuel Costs

- How are you able to manage rise in fuel costs?
 - OBO tries to estimate the impact and adjust our project estimates accordingly – however unlike private industry, we are limited in our ability to deal with this (i.e. we can't hedge...)
 - Considerations under discussion are:
 - Contract Escalation clause & Current year project estimates (see material cost question...)
 - Decreasing the amount of materials shipped to site
 - More sustainable construction



Currency Fluctuation

- How do you manage project costs and pricing based upon foreign currency exchange?
 - This hasn't proven difficult when the exchange is stable, but wide fluctuation last year much more difficult – project specific
 - Considerations under discussion are:
 - Estimating all projects in current year \$, and having a separate line item for escalation/currency fluctuation. So that if escalation/currency flux is greater than anticipated we'd have management reserve in the project budget



Expatriate Labor Rates

- How do you structure U.S. based labor rates for personnel assigned to overseas projects?
 - OBO adds these costs into the labor rates for our estimates – but it is again project specific
 - There is a limited pool of cleared American labor that is highly competitive. Therefore, we also review the cost of this labor against more oversight of local labor.



Security

- How are security costs factored into the project?
 - Security is a big factor in all of our projects. Therefore, all of the estimates and contracts have elements of security contained in them. We articulate these requirements clearly in our SOW.
 - We also have a program of Cleared American Guards/Construction Security Techs that is used to monitor the construction contractors activities. There are more CAGs/CSTs required when there are less contractor cleared American labors provided. This means we do a cost analysis to determine the most economical mix of workers.



Pre-Purchased Agreements

- Do you use pre-purchased agreements?
If yes, how and to what extent are these agreements implemented?
 - Yes – OBO has a Government Purchased Contractor Installed (GFE) program to pre-purchase long lead time standard items (mainly furniture, FEBR Windows and Doors)
 - Considerations under discussion
 - Expansion of the program for other long-lead items
 - Scaling back the program to encourage design excellence



General Conditions Costs

- How do you structure your general conditions cost fluctuations in regard to materials, labor, currencies, fuel & travel costs, insurance, etc.?
 - We include risk elements and carry a nominal contingency



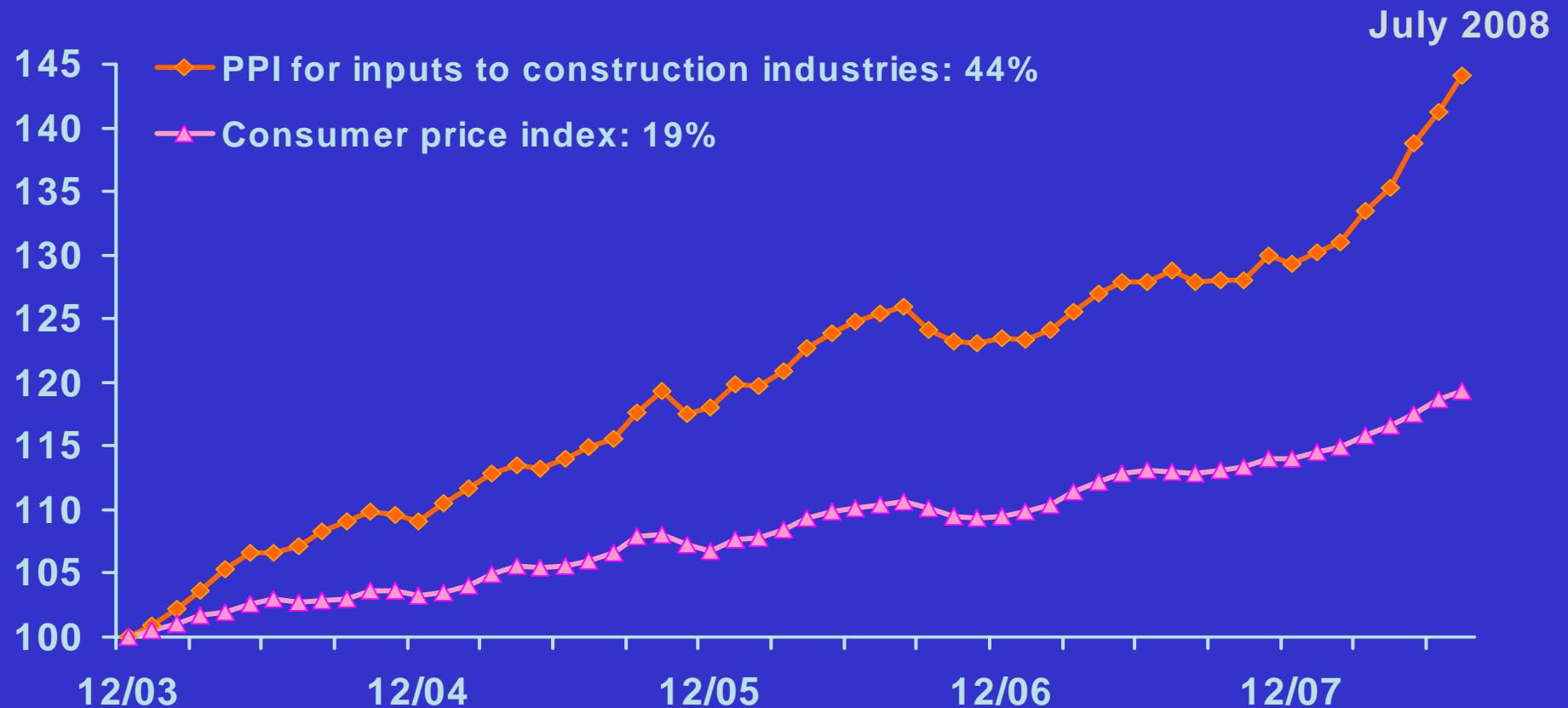
Cost Control and Budget Forecasting

- How do you control cost over long term projects?
 - We award firm fixed price contracts... problem is as economic conditions worsen....there is a greater disparity of our estimate of risk and our bidders estimate of the risk.



Escalation and Cost Alerts Sept 2008

Change in Producer Prices for Construction vs. Consumer Prices, 2003 - 2008
(December 2003 = 100)



Source: BLS (CPI, PPI)

Source: AGC Digest August 25, 2008