2021

Construction Payments Report

Insight into the $136 billion impact of slow payments in the construction industry

Rabbet

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INTRODUCTION

How the Speed of Payments Continues to Impact the Construction Industry

Well over one trillion dollars is spent on construction annually in the United States. In 2020, new construction put in place in the United States was valued at around 1.36 trillion U.S. dollars, a very slight decline from 2019 due to the impact of COVID-19. **This year there is a shift towards growth again as the U.S. is on trend to spend an estimated $1.59 trillion dollars in 2021.**

Each year Rabbet conducts a survey of subcontractors and general contractors about the speed of payments in the construction industry and analyzes the impact on cost for contractors, developers, lenders, equity partners and stakeholders within CRE.

This year's report compares survey data from 2021 with data collected in previous years to examine the accelerating cost of slow payments for the industry as a whole.

As stated in our 2020 Payments Report, subcontractors experience the primary effects of slow payments directly, including the cost of floating payments for payroll and supplies, higher risk of bankruptcy during downcycles, and challenges in growing a cash-intensive business. In addition, general contractors also face some of these primary effects alongside secondary effects like inflated project costs and delays.

Looking at survey data from both subcontractors and general contractors, the 2020 Construction Payments Report showed that 25% of all respondents report that work has been delayed or stopped due to a delay in payments to crew members in the last 12 months. In 2021, there was a 7 point increase to 32%.

Rabbet's Annual Construction Payments Report demonstrates the primary and secondary cost of slow payments and why all parties in the construction industry should take action to address them.

2021 SURVEY HIGHLIGHTS

83% of subcontractors claim that late payments from a general contractor affects productivity

72% of subcontractors would offer a discount in exchange for payments within 30 days

67% of subcontractors report choosing not to bid on a project due to a general contractor or owner's reputation of slow payments

76% increase in general contractors using each lines of credit and credit cards to float payments when payments are delayed

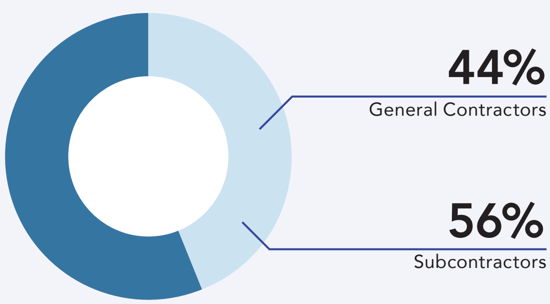
35% of all general contractors report that work has been delayed or stopped due to a delay in payments to crew members in the last 12 months

THE STUDY

The survey captured how 94 general contractors and subcontractors across the US managed working capital, bidding decisions, and project risks in the face of slow payments during the last 12 months. Participants completed the online survey during September 2021. Rabbet distributed the survey to contractors representing a wide diversity of trades and would like to thank all survey participants who gave their valuable time to participate in the report.

Rabbet Respondent Profile

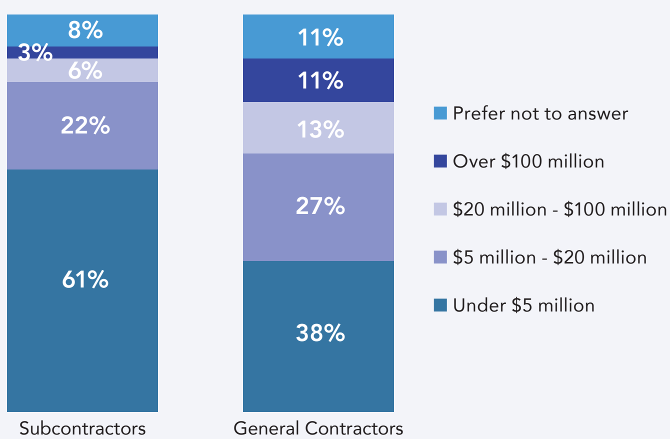
Respondent Breakdown



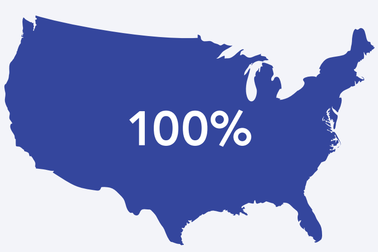
Top Trades Represented

- Roofing
- Painting
- Remodeling
- Framing
- Electrical

2020 Revenues



Locations Represented



THE REAL COST OF SLOW PAYMENTS

Because business expenses are incurred and must be paid before payments are received for work conducted, working capital is crucial to contracting businesses.

In simple terms, cash flows out of a subcontracting business for wages and materials much quicker than the time it takes for cash to flow in. Wages must be paid weekly or biweekly, and materials are typically purchased on 30-day invoice terms. In 2021 an estimated 50% of contractors reported that they wait longer than 30 days to receive payment. This is similar to 2020 data where an estimated 54% of contractors claim they waited longer than 30 days to receive payment.

Like previously mentioned, cash flows outwardly for subcontractors and general contractors before payments for their services are ever received. Though close to 89% of subcontractors feel confident that they include enough overhead costs, 38% of them stated they had work delayed or stopped because of a delay in payments to crew members.

Financing Sources Subcontractors Use While Waiting for Payment

Source of Financing	2019	2020	2021
Balance Sheet	36%	41%	39%
Line Of Credit	22%	46%	36%
Credit Card	25%	36%	22%
Personal Savings	31%	20%	15%
Retirement Savings	8%	17%	6%

Subcontractors turn to many sources of financing for wages and materials while they wait for payment from the general contractor. In 2021 subcontractors report a dip in their reliance on lines of credit. Only 36% of subcontractors report the ability to rely on their balance sheet, nearly 25% use credit cards, and 8% rely on retirement savings. There was a noticeable 31% decrease in credit card usage to float payments and a spike in use of personal savings to 31%.

Better relationships yield better results

We asked subcontractors how a late payment from a general contractor affects productivity. 83% of subcontractor respondents claimed a late payment had an affect on their crew's productivity to some degree. 33% of subcontractors who said it affected their productivity said it had 'a lot' or 'a great deal' of an effect on their productivity. Over 95% of general contractors surveyed noted that they see the value in paying their subcontractors faster. **The communication, expectations, and relationships between general contractors and subcontractors can directly impact a crew's productivity which would then influence project timelines and overall quality of work.**

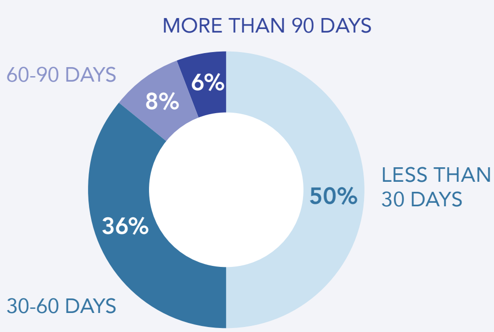
% Increase on Total Project Cost for Subconstractors Due to Slow Payments

2018	2019	2020	2021
+3.3%	+3.3%	+4.5%	+2.8%

Subcontractors

50% Of subcontractors wait longer than 30 days for payment

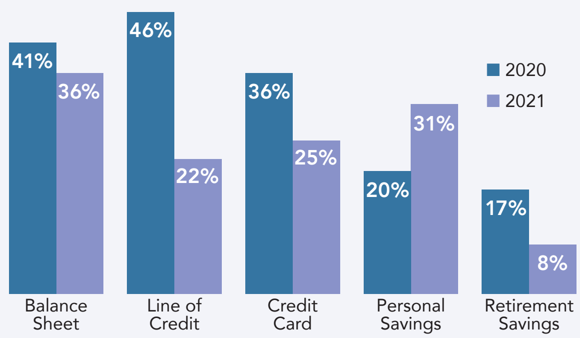
(2020: 54%)



How Long Subcontractors Wait for Payment

50% Of subcontractors incur financing charges while floating payments

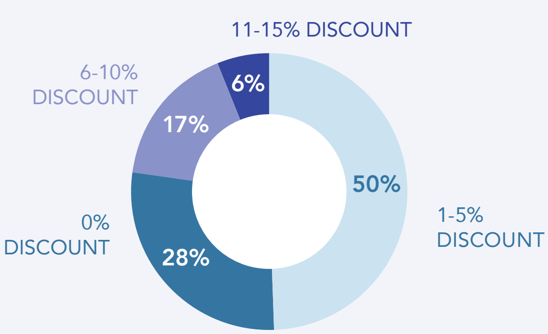
(2020: 68%)



Financing Sources While Floating Payments

$57B Estimated discount subcontractors would offer in exchange for payment within 30 days

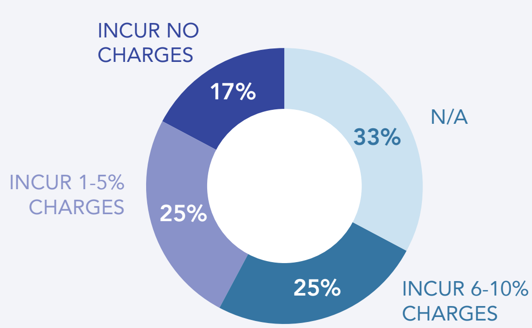
(2020: $81B)



Discounts Offered by Subcontractors

$44B Estimated overhead included in subcontractors' bids to finance slow payments

(2020: $61B)



% of Project Costs Incurred by Financing Charges

Subcontractors indicate that the value of faster payments is greater than the value of alleviating financing costs. While they report the average cost of floating payments is 2.75%, subcontractors say they would provide an average of a 3.6% discount (vs 5.9% in 2020) for payments made within 30 days. Even among those who say they did not incur costs for floating payments in the last 12 months, 72% (vs 42% in 2020) said they would offer a discount.

Subcontractors are aware of the risk associated with delayed payments and are even willing to offer a discount to developers for more timely payments. A notable 50% of subcontractors responded that they would at least offer up to 5% discount for faster payment. **Just over 22% of subcontractors said they would offer a 6-15% discount to general contractors for faster payment.**

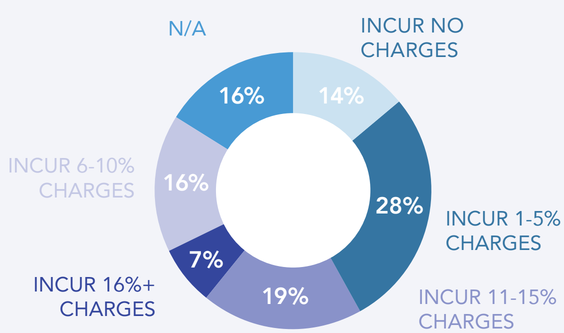
General Contractors

$92B Estimated overhead included in general contractors' bids to finance slow payments

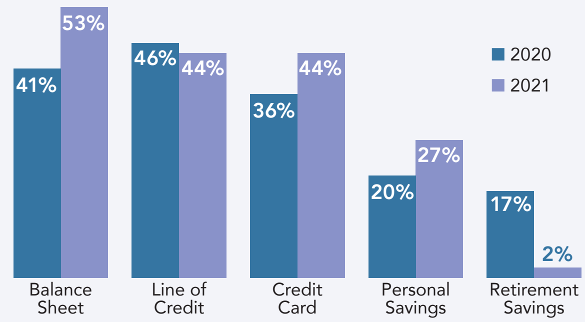
(2020: $41B)

63% Of general contractors incur financing charges while floating payments

(2020: 65%)



% of Project Costs Incurred by Financing Charges



Financing Sources While Floating Payments

General contractors aren't immune and still see value in expediting payments for subcontractors. This is the 3rd year in a row that Rabbet has included general contractors into our Annual Payments Survey. This information is imperative in understanding the full construction payment cycle.

In 2020, three out of four general contractors saw value in paying subcontractors faster. That number spiked significantly in 2021 with just over 95% of general contractors seeing value in faster payments to subcontractors.

63% of general contractors incur financing costs while floating payments to subcontractors, a minimal change from 2020 in which 65% of general contractors surveyed said the same. 95% of general contractors report paying at least some vendors more frequently than once per month (vs 40% in 2020).

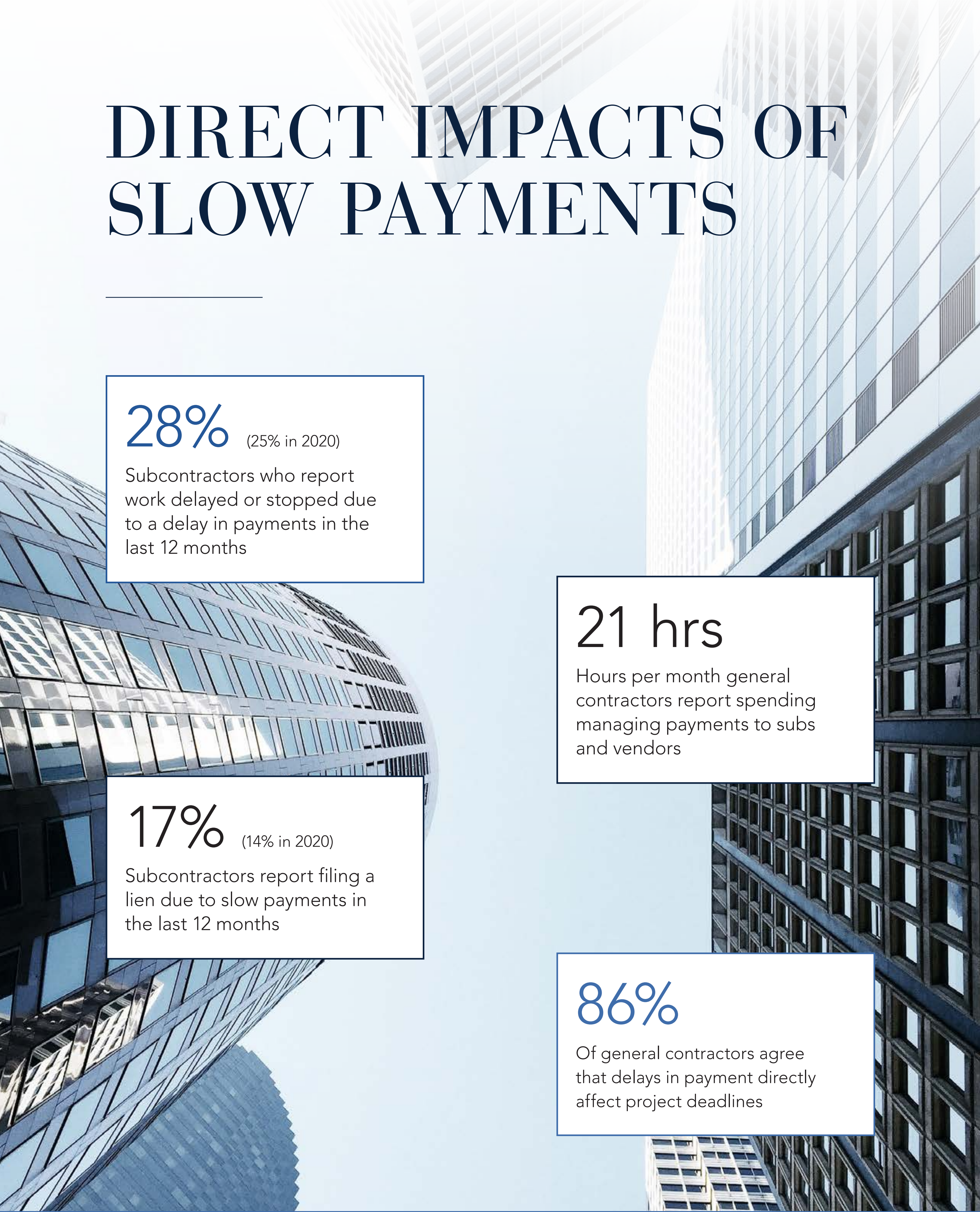
The waiting game: How general contractors float payments

Floating payments is not solely a subcontractor problem. When anyone in the process suffers from delayed payments, others in the payment cycle are inevitably affected. 53% of general contractors claim they rely on the balance sheet followed by a line of credit (44%), credit card (44%), personal savings (27%) and lastly, retirement savings (2%). The ranking of sources matches that of previous years but it is noteworthy that there was a nearly 76% increase from 2020 to 2021 in the reliance on both lines of credit and credit cards.

Financing Sources General Contracts Use While Waiting for Payment

Source of Financing	2019	2020	2021
Balance Sheet	38%	38%	53%
Line Of Credit	29%	25%	44%
Credit Card	15%	25%	44%
Personal Savings	6%	23%	27%
Retirement Savings	2%	3%	2%

The uptick in reliance on almost every financing source reflects the pressure general contractors are experiencing. **The almost doubled growth in line of credit usage and credit card usage is further evidence of the uncertainties revolving around materials costs and delays and could have led to more general contractors fronting payments from these various funding sources.**



DIRECT IMPACTS OF SLOW PAYMENTS

28% (25% in 2020)

Subcontractors who report work delayed or stopped due to a delay in payments in the last 12 months

21 hrs

Hours per month general contractors report spending managing payments to subs and vendors

17% (14% in 2020)

Subcontractors report filing a lien due to slow payments in the last 12 months

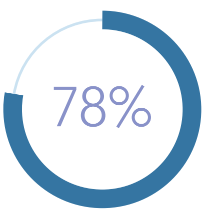
86%

Of general contractors agree that delays in payment directly affect project deadlines

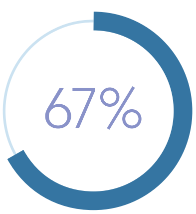
REPUTATION REMAINS A HUGE FACTOR

Developers and capital partners may not realize their role in the overall cost of a project.

The reputation of developers and capital partners is a huge variable in how subcontractors and general contractors bid on projects. In addition to the extra project costs which are direct effects from slow payments, subcontractors also factor in a general reputation for slow payments when deciding when and how much to bid on projects.



of subcontractors report considering the payment reputation of the owner when deciding how much to bid on a project



of subcontractors have chosen not to bid on a job because of a general contractor or owner's reputation of slow payments

It seems obvious but it stands true that when general contractors can't get the best bids from the best contractors, it becomes very difficult to manage project costs and schedules effectively. **An owner's reputation for slow payments threatens the general contractor's ability to earn competitive bids, and this challenge is further compounded by the enormous strain from a continuing worldwide pandemic.**

Ultimately, all owners, investors, lenders, developers, and general contractors share responsibility for slow payments in the industry. In fact, as stated in the 2020 Construction Payments Report, even though some industry participants are up to five degrees removed from the individuals who purchase materials and perform the work, they are not immune to the cost, schedule, and risk implications.

Subcontractors and general contractors have long been carrying the burden of slow payments—and all stakeholders suffer from the costs. It's time for owners, investors, lenders, and developers to adapt to 21st-century processes and technology to improve the construction industry for all.

THE OLD NORMAL

This year was unlike any other. Rabbet posed open-ended questions in the survey in order to dive deep into understanding the effects of COVID-19-related supply chain challenges and labor shortages.

It is no secret that the U.S. is experiencing an unprecedented labor shortage. Over 74% of general contractors reported that they have had to pay more for labor or charge more for labor to meet a project deadline in the last 12 months. This, however, is not the only newfound challenge plaguing the industry in 2021.

The survey asked general contractors which factors are negatively impacting cash flow and which of these factors have prevented them from bidding on a project in the last 12 months. All of these new challenges are negatively impacting cash flow; however, **the spike in material's cost edged out the others as the biggest concern for over 74% of general contractors**.

NEGATIVE CASH FLOW FACTORS (PAST 12 MONTHS)

42% of general contractors claim that **finding labor** has negatively impacted cash flow

40% of general contractors claim that **increased labor costs** have negatively impacted cash flow

74% of general contractors claim that **increased material costs** have negatively impacted cash flow

47% of general contractors claim that **longer material lead times** have negatively impacted cash flow

47% of general contractors claim that **COVID restrictions** have negatively impacted cash flow

BID PREVENTION FACTORS (PAST 12 MONTHS)

37% of general contractors claim that **finding labor** has prevented you from bidding on a project

40% of general contractors claim that **increased labor costs** have prevented you from bidding on a project

40% of general contractors claim that **increased material costs** have prevented you from bidding on a project

26% of general contractors claim that **longer material lead times** have prevented you from bidding on a project

30% of general contractors claim that **COVID restrictions** have prevented you from bidding on a project

General contractors and subcontractors highlighted opportunities for optimization and automation within the current processes that existed prior to the pandemic's monumental impact to the industry.

This survey also aimed to understand the circumstances within existing processes that impact payment speed. General contractors and subcontractors were asked what the one change they would make to the current process would be and what the biggest contributing factors to delayed payments were. The expectation was that the newfound challenges of the last year would be amongst the most popular responses; however this was not the case. Though 2020 was a tough year, as indicated by this report, respondents highlighted the common challenges that have proved problematic to this industry and their processes for quite some time.

With countless new challenges being faced by the industry as a whole, it was surprising to see that the true wants and needs of subcontractors and general contractors were associated with updating the antiquated payment processes that have long existed.

Both subcontractors and general contractors were asked what they would change if they could change one thing about their current payments process.

Overall, subcontractors and general contractors would prefer a process that is faster, consistent, more streamlined, and potentially automated. Many respondents claimed that automatic, instant, or direct payments would allow them to plan ahead and utilize their time better because they would not be spending extra time and resources chasing down payments owed to them. A subcontractor who filled out this year's survey and specializes in framing stated that they would want "better ways to process the payments [and] a more user friendly program or service that would assist" with payments. Almost all of the responses addressed the challenges associated with decentralized information sharing.

Respondents mentioned frustrations with shuttling documents back and forth via email and traditional mail.

Traditionally, subcontractors are waiting on general contractors for payment. General contractors are waiting for developers or owners for payments. Developers and owners are potentially waiting on funding from banks. Banks are sifting through documents that may have to be revised by developers. All of these payments and communications happen via email, spreadsheets, and physical mail. One respondent, a general contractor, simply asked for "less people involved" in the payments process and another general contractor "would like if the process was faster and more streamlined." Currently, all parties are waiting for other parties for payment, but none have status updates from the others. There is no insight into who is delaying the process or how long it will take. Most of the people involved are left with little to no information. **This process severely lacks transparency, automation, tracking, and one true source of information.**

Respondents were also asked what the most common reason for delays in payment was in their experience.

General contractors and subcontractors had various reasons they believed contributed to delayed payments, but there were a few responses that seemed to be consistent amongst the group. First, it's important to note that the process in general is extremely antiquated. The construction industry is notorious for adopting technology and advancement late if at all. Some of the responses received were "mailed checks" and "slow internal processing of job orders and check writing." Traditional mail, individual and decentralized documentation, and slow internal operations and approvals plague this process and create many opportunities for delays, error, risk, and miscommunication.

As mentioned, reputation **holds a tremendous amount of weight in this industry**. Clearly, effective and transparent communication is crucial to an efficient process. A subcontractor focused on framing pointed out that the "most common reason they have heard or experienced is the process of bank draws. Especially with the pandemic going on some banks have gotten really strict about releasing payment until proof of delivery, which is an invoice but sometimes [subcontractors] don't see invoices for up to a week after delivery." **Managing expectations and offering insights in the process at all levels can mitigate frustration and many of the consequences of slow payments.** If a payment is delayed but the delay is communicated, the payments schedule can be adjusted and factored into the process. This would potentially minimize the hidden costs associated with late payments and strengthen the relationship with the vendors.

One interesting discovery was the lack of emphasis around lumber costs. Skyrocketing lumber costs has been a hot topic in the industry for the past year. The expectation was that this one challenge would have an immense effect on payments, but recently lumber prices have dropped and somewhat stabilized. **What general contractors, subcontractors, and even developers, financiers, and stakeholders are craving is predictability.** Materials costs in general have spiked and lead times for these materials have continued to extend; however, one of the largest hurdles for the construction industry as a whole is not pricing, but scheduling. Subcontractors are even being asked to buy materials in bulk and in advance to offset the unpredictability of many materials. Asking subcontractors to make large purchases in advance to minimize schedule impact is a rather large concern in pricing and forecasting, even more than the cost of goods themselves. **Delayed payments are one of the side effects of these types of unknowns and variables.**

Based on the findings of this report, the data from Rabbet's 2021 State of Construction Finance Report, which addresses the construction industry as a whole and the interpersonal relationships that comprise this industry, and conversations with an esteemed team of developers, there is evidence backing a transition back to office spaces for developers and lenders. As previously mentioned, communication internally and externally can have a positive impact on payment speed outward. Consolidating teams back to central locations is expected to help this slightly. It is interesting to note that buyers are now gravitating towards fully built out spec offices instead of the previous trend of buyers pursuing offices that are blank slates with options for configuration, customization, and furnishings. Because the market is unpredictable and timing is critical, companies are purchasing fully finished and furnished spaces to accommodate their team's new hybrid operations.

TRENDS

The construction industry as a whole has been plagued with many bottlenecks this year. Last year sudden changes to job site requirements and the introduction of remote work as a result of the COVID-19 pandemic forced contractors, real estate developers, and lenders to optimize their processes quickly. According to Rabbet's 2021 State of Construction Finance Report, though lenders and developers are choosing to move the majority of their teams back in office in the future, over 21% of lenders say that a portion of their teams will likely continue to work remotely. While 55% of developers say they have teams working remotely due to the pandemic, 100% expected to return to office soon. This will further the need for digitized processes as well as systems that are collaborative and centralized regardless of physical location. Now, more than a year into this global pandemic, this report is able to look into the long-lasting effects of the pandemic and what the "new normal" will look like. Though there is a slow push back to "normalcy," there are a new set of challenges that developers and lenders are currently facing.

As previously stated, 86% of general contractors agree that delays in payment directly affect project deadlines. **The pandemic, like in most industries, illuminated the need for contingency plans and efficient processes that can adapt to unexpected circumstances.** Though the problem is now recognized, the construction industry has been slow to adapt to technology and process improvements that could enhance the payment process for lenders and developers and ultimately build a more copacetic and reliable relationship with general contractors and subcontractors.

Slow payments are an industry-wide problem that requires an industry-wide solution. It is crucial for industry participants to work together to eliminate the manual, complicated processes involved in invoice approval and payment distribution.

Whether you are a developer or a lender, we urge you to pay close attention to these trends and use these takeaways to help guide your construction finance strategy.

Trend		Takeaway
Late payments compromise the productivity of the subcontractors and general contractors and add schedule risk due to competition for labor.	▶	A streamlined payment process with timely and reliable payments will limit schedule impacts on the existing projects.
Contractors and general contractors highlighted lack of visibility into other parts of the payment cycle and a lack of effective communication practices as the biggest weakness in current processes.	▶	Providing more payment transparency may be as valuable as providing payments faster. The first step in providing more transparency about payments externally is organizing end-to-end invoice processes internally.
Slow payments continue to add unnecessary risk in the form of liens, project delays, and unforeseen costs.	▶	Expediting payments is a critical component of risk management. Inefficient processes that lead to slow payments can derail projects with liens and added risk.
Uncertainty in supply chain is impacting material costs and project schedules, both of which create extra pressure on cash flow. Only recently have material costs started to stabilize.	▶	Developers who have good business practices such as timely payments have more open communications with their general contractor about planning for and solving material supply issues to minimize impact on project schedules and budgets.
Late payments put cash flow pressure as well as additional operating costs on general contractors and subcontractors. These costs get passed through in bids. Cash flow is being negatively affected by many new challenges in 2021, but the labor shortage is a consistently huge factor plaguing construction processes and costs currently.	▶	Building strong relationships and creating an environment that construction teams can happily work in and learn to expect timely payment is crucial in gaining competitive yet realistic bids from contractors. Reputation and reliability are key in combating the impacts of the labor shortage.

About Rabbet

Rabbet provides cloud-based solutions for commercial lenders, real estate developers, equity partners, and service providers to centralize construction finances, automate administrative tasks, and reduce the time spent managing draws. Based in Austin, TX, Rabbet was founded in 2017, and offers visibility and efficiency across billions of dollars in commercial construction projects.

How Rabbet Works

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