Belgian construction sector faces a difficult year

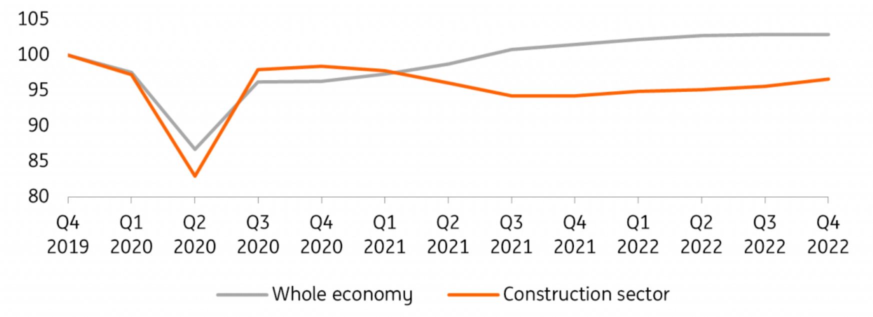
The Belgian construction sector had a decent year in 2022, despite challenges such as expensive construction materials and higher interest rates. However, there are signs of a slowdown in 2023, including a sharp drop in building permits for new housing, commercial properties, and renovations

Belgian construction sector still 3.4% below pre-Covid levels

In the fourth quarter of 2022, the Belgian construction sector saw growth of 2.4% year-on-year and 1% quarter-on-quarter, driven by well-filled order books and milder weather conditions. However, activity was still 3.4% below pre-pandemic levels, and it may take until 2025 for the sector to return to those levels. This contrasts with the Belgian economy, where activity in the fourth quarter of 2022 was already 2.9% above the pre-pandemic level.

The Belgian construction sector outperformed construction sectors in neighbouring countries last year. In France (-0.5%) and Germany (-0.7%), activity in the fourth quarter was even lower than in the same quarter of 2021. In the Netherlands, the sector grew by 1.5% year-on-year, which is still significantly lower than the Belgian growth rate. Factors contributing to the Belgian construction sector's strong performance include the reduction of the VAT rate for demolition and reconstruction, high demand for construction and renovations during the pandemic, and regional support for energy-efficient renovations.

Gross value added construction sector relative to Belgian economy (Q4 2019 = 100)

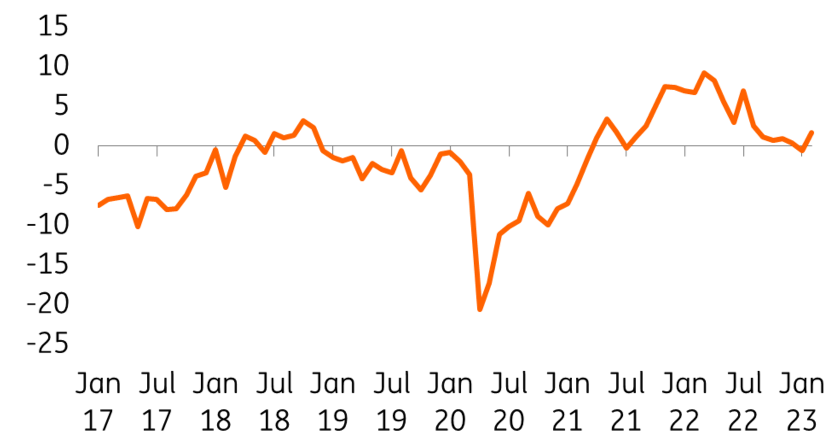


Source: Eurostat

Business confidence appears to be stabilising

The Belgian construction sector experienced a peak in business confidence in March 2022, reaching its highest level since 1990. However, confidence declined rapidly thereafter due to increased prices of construction materials, higher interest rates, and macroeconomic uncertainty. Nonetheless, there has been a visible stabilisation of confidence in recent months due to falling energy prices, inflation, and a more resilient economy than expected. Although confidence rose slightly in February, it is still too early to confirm a turnaround. Among Belgian producers of building materials, however, there is already a clear turnaround in confidence, although it is still below the historical average.

Evolution of business confidence in the Belgian construction sector, 2017 - Feb 2023



Source: Eurostat

Price pressure remains historically high

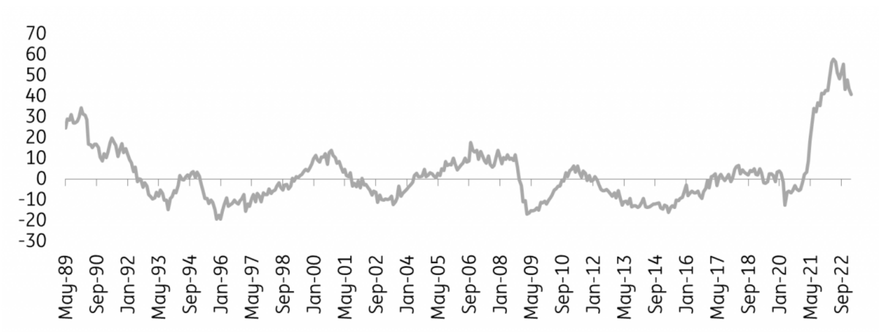
While some construction materials like wood and metal ores have become cheaper than they were last summer, their prices are still relatively high. Other materials, such as copper and steel, have rebounded after a period of cooling, and with the Chinese economy showing signs of improvement, there is a chance that global demand for building materials could increase, leading to new price hikes.

Despite falling energy prices, energy-intensive materials like concrete, cement, and bricks have yet to show any signs of price drops. We should not expect price drops in the near future, as many suppliers are still planning to increase their selling prices. This is partly because concrete, cement and brick are very heavy and bulky materials, making them more expensive to transport. Therefore, these materials are often produced locally, which means there is less competition, giving suppliers more pricing power and making them less likely to reduce prices in response to falling energy costs.

We expect prices of concrete, cement and brick to fall only when suppliers' inventories increase sharply, which would indicate much weaker demand. Although stocks have already increased, they are still below their historical average, so we should not expect an immediate price drop for these materials. Moreover, Belgium's resilient economy means that demand is holding up better than expected, making it easier for producers of these materials to pass on new cost increases or be less quick to cut prices.

According to a monthly survey by the European Commission, many construction companies plan to continue passing on higher input costs to their customers in the coming months. Although the number of firms planning to raise prices has decreased since the summer, the number still remains historically high. Besides more expensive construction materials, Belgian companies are also facing stronger wage increases than in neighbouring countries. Labour costs have increased by about 10% over the past year, due to automatic wage indexation.

Sales price expectations in the Belgian construction sector



Source: European Commission

Sharp fall in number of building permits in residential sector points to a slowdown in 2023

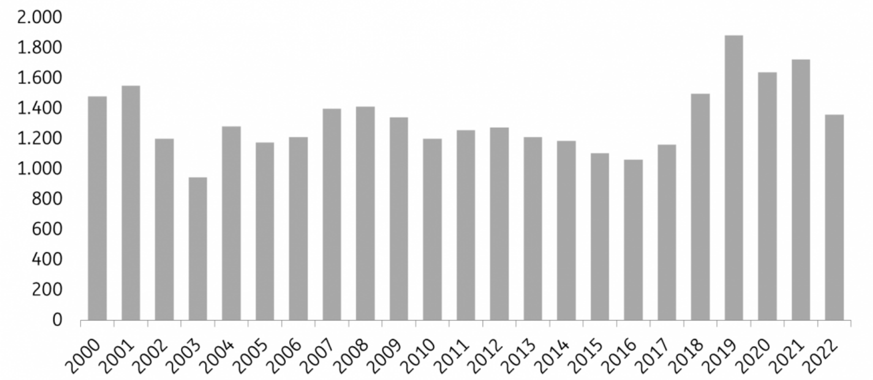
In the residential sector, the number of building permits issued fell 8.3% in the first ten months of 2022, with higher costs of building materials and rising mortgage rates cited as the main reasons. This decline signals a slowdown in construction activity in 2023. Flats are slowing down more than single-family houses: the number of permits for flats is down 11% compared to 7.7% for single-family houses. The number of permits for flats has been declining since 2018 due to rising construction costs, land prices, interest rates, stricter regulations, land scarcity and delays in permit procedures. These factors have made investment in flats less attractive to developers, and the pandemic has also contributed to lower demand for smaller flats due to changing housing preferences and the increase in working from home.

For non-residential property, the decline is even greater

Commercial property development is facing significant pressure, with building approvals for non-residential projects declining by 21% in the first 11 months of 2022 compared to the same period in 2021. Compared to 2019, the decline is even greater at 28%, although it should be noted that 2019 was an exceptionally strong year with an almost 80% increase in commercial space development. This decline is due to the growing trend towards online shopping and remote working, which reduced demand for physical shops and office space, along with economic uncertainty and sharply increased construction costs making companies more cautious with real estate investments.

Slow licensing policies, strict environmental standards, safety regulations, and limited land availability may also have contributed to the decline. However, there was some recovery in new office development in 2022, with the number of licensed square meters increasing for the first time since 2018.

Building permits for non-residential property in m² of floor area, first 11 months of each year only



Source: Eurostat

The number of building permits issued for the renovation of business premises has fallen significantly

The commercial property renovation market is cooling even faster than the new construction market: the number of permits for commercial property renovations reached a low in October 2022, equal to the 2017 low. To achieve the goal of making all commercial buildings climate-neutral by 2050, the number of energy renovations must increase significantly. This challenge may be greater for commercial properties than residential, as commercial properties account for a larger share of energy consumption and greenhouse gas emissions in the building stock, and commercial property emissions have increased by 20% since 1990, while residential emissions have fallen by 36%. However, this trend is due to the strong growth of non-residential buildings during this period.

Slow licensing policy slows down construction industry

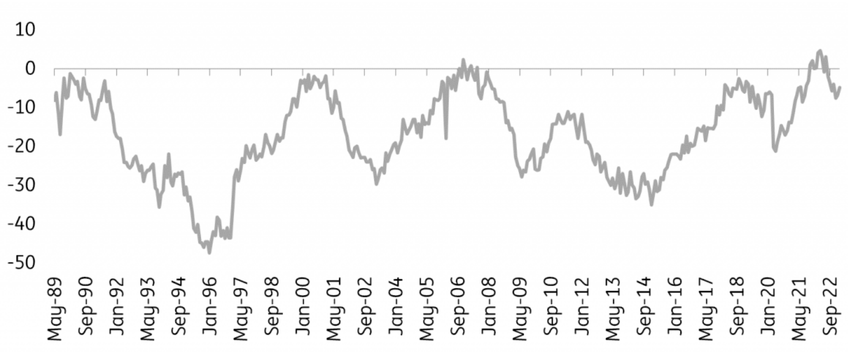
Belgium's slow permit policy is a major factor hampering activity in the construction sector. The long lead time for permits deters developers from investing in new projects because of the higher costs and uncertainty. Belgium scores poorly in an international comparison of permit processing time: according to the latest available World Bank figures from 2019, the country ranks 172 out of 208 countries. Compared to its neighbours and other major eurozone countries, Belgium performs worse in terms of processing time, with the exception of France.

The situation in Flanders (specific figures for Belgium are not available) deteriorated further between 2019 and 2021, with increasingly long processing times for permits granted at the municipal, provincial and Flemish levels. Long processing times and complicated appeal procedures cause delays, which is particularly problematic given the current context of more expensive construction materials and rising labour costs. In the long term, this could lead to a reduced supply of new construction, exacerbating the growing housing shortage and increasing purchase and rental prices.

Although facing significant challenges, the long-term outlook is favourable

The Belgian construction sector is currently struggling with several challenges, including escalating prices of building materials, higher mortgage rates and higher labour costs. Although price increases have cooled somewhat since the summer, the prices of many building materials have risen again in recent months and a resurgence in China may push prices up further. We also expect interest rates to rise slightly this year, which will further dampen demand for construction and renovation. Nevertheless, the sector is still in a relatively favourable position, with order books remaining above the historical average. We expect the Belgian construction sector to grow by around 0.5% this year and 1% the following year.

Evolution of order books, 1989 - Feb 2023



Source: European Commission

Future prospects for the Belgian construction sector are encouraging, especially with the upcoming renovation wave to promote the sustainability of homes. The European goal of being carbon neutral by 2050 should boost demand for insulation and renovation works. While new construction will remain essential, especially in regions facing a shortage of affordable housing, there is an increasing shift from new construction to renovation. This shift is driven by rising construction and land costs, which are prompting property developers to prioritise renovation projects over new construction.

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