

EU Construction Outlook: Contractors' optimism rising despite building material shortages

We expect further growth in the EU construction sector this year and next, despite a continuing shortage of some building materials. The EU Construction Confidence Indicator was positive at the start of 2022. Building volumes should be boosted by fresh investment from the EU recovery fund



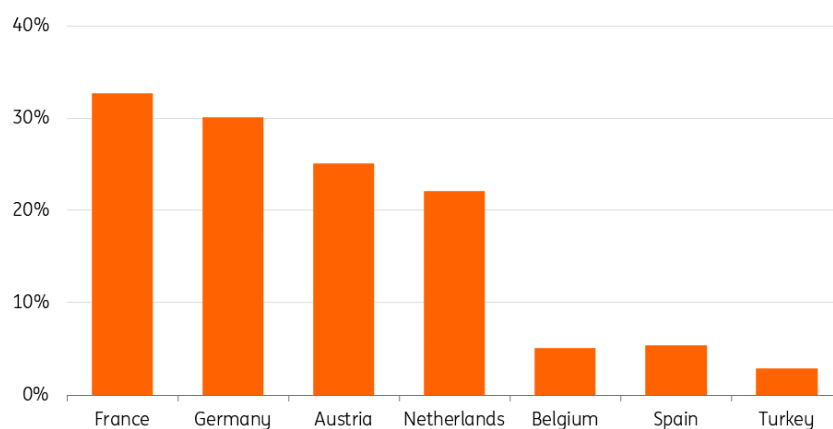
New homes being constructed in Stellendam in the Netherlands

Further increasing material shortages

The outlook for construction in the European Union has changed. Back in September last year, we noted in our [EU construction outlook](#) that supply chain disruptions, due to the Covid-crisis, were decreasing the supply of building materials. This was just as construction output bounced back after the first wave of the virus. This resulted in shortages and price hikes. In August, a record percentage (18%) of EU contractors indicated lower production due to a lack of building materials or at least a delay in their delivery. This percentage shot up (29%) in January 2022, with the highest shortages in France and Germany.

Highest shortage of building materials in France and Germany

% EU construction firms that have to limit production because of material &/or equipment shortages, January 2022



Source: European Commission, ING Research

New French regulations cause material shortages

In France, most contractors are faced with high material shortages compared to other main European countries. As French construction volumes haven't fully reached pré-corona levels yet, strong demand isn't the whole narrative. France has recently implemented a new law requiring half of the materials used in public buildings to be timber or other bio-based materials. This leads to increasing demand for these specific materials and shortages, especially as timber is still scarce.

Supply chain disruptions in other countries

Shortages are also high in Germany, Austria and the Netherlands as production levels, and therefore demand for inputs are, and have remained high, in these countries. We expect that building material shortages will continue for a while, not least because of China's 'zero-Covid' strategy and restrictions put in place to contain the virus in cities and ports that are very important to global production chains. However, there are very few construction firms that mention a shortage of building materials in Belgium, Spain and Turkey.

Higher sales' prices

Supply chain disruptions and higher energy prices lead to [higher building material prices](#). This puts pressure on profit margins and building companies are therefore passing through price hikes to their sales prices. This results in a record number of building companies that are planning to increase their prices at the beginning of 2022. On balance, 36% of EU building firms plan to increase prices in January 2022. This is the highest percentage for the last 20 years. German, Austrian and Dutch construction firms, in particular, expect to raise their sales price. These are the same countries that face material shortages due to high demand as we discussed above.

Highest % of contractors that plans to increase sale price

Balance of construction companies in EU that expect to increase/decrease output prices (over next 3 months)



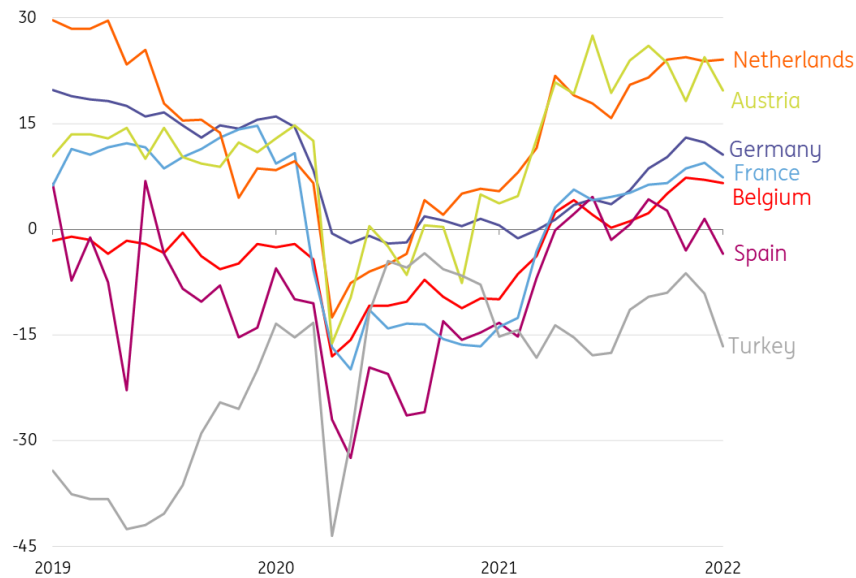
Source: European Commission, ING Research

EU Construction confidence indicator positive

Despite price pressure, business confidence at the beginning of 2022 is positive among most contractors in the European Union and back to pre-covid levels. The highest values are registered in Austria and the Netherlands. Optimism among contractors in both countries was already high before the Covid-19 outbreak and recovered quickly after the first wave. Furthermore, construction volumes in these countries were barely hit during the lockdowns as construction sites remained largely open. Spanish construction sentiment has been hovering around neutral in the last few months though order books are improving. In Turkey, construction sentiment in January withered away, probably due to [high inflationary pressure](#) at the moment.

Optimism among most contractors

Construction confidence indicator, seasonally adjusted



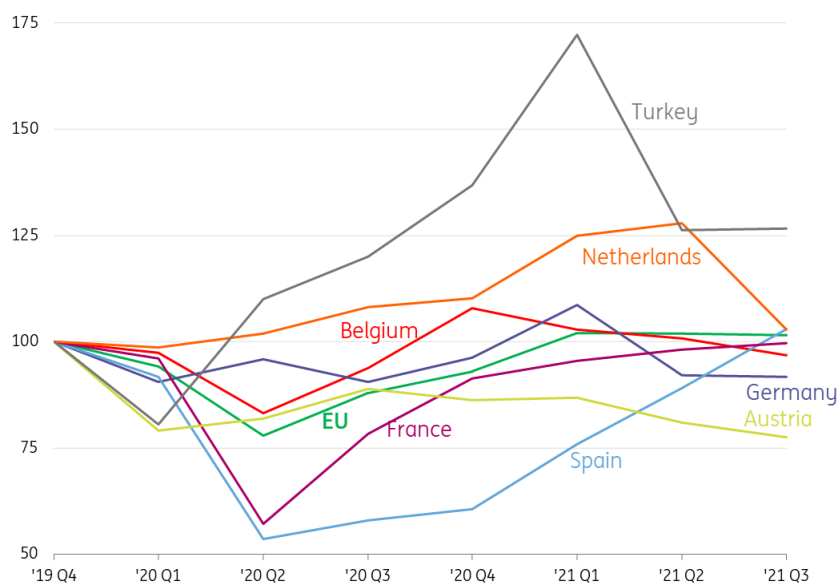
Source: Eurostat, ING Research

□ Issuance of residential building permits stable

The issuance of residential permits is a strong indicator for future production. Huge housing shortages in many European cities ensure sufficient demand in the residential sector. The number of approved new home permits in the EU has been stable in the first three quarters of 2021. It has been hovering around the pre-corona level since the end 2019. We, therefore, don't expect high growth figures in the EU residential building sector in the coming year. However, there are huge differences between countries.

EU permits for new homes remains flat

Building permits, number of new dwellings, (index 2019 Q4 =100, SA)



Source: Eurostat, ING Research

Europe at a glance

France and Spain back to pre-Corona levels

Spain has made up for the decrease it faced during the first corona wave. In the third quarter of 2021, it has even issued slightly more building permits than at the end of 2019. Spanish new residential output can profit from this in 2022. French permit-issuing has made a comparable move, although recovery started a bit earlier. Residential markets in Spain and France are also being boosted by the renovation market. France's MaPrimeRenov scheme offers generous grants (circa 30% of renovation costs), and interest-free loans to help households to finance the job. In Spain, the Recovery Plan includes €6.8 billion for incentive measures for housing renovation, plus another €1.0 billion for public rental housing.

Stable permit numbers in Belgium, Germany and Austria

Residential permit issuance in Belgium, Germany and Austria has mainly been moving sideways in the last few quarters. All three countries, like many other European countries, have a strong demand for new houses but shortages of building land, high prices and time-consuming permit procedures constrain further growth. For Austria, the graph shows that the number of Austrian permits was still below the level seen at the end of 2019. However, this is due to a peak in Austria's permit issuance in the last quarter of 2019.

Correction of issued permits in the Netherlands

In the Netherlands, the number of permits issued for new homes couldn't maintain its growth in the third quarter of 2021 and fell back in the third quarter of 2021. To solve the low supply of

houses, the new Dutch government proposes building 100,000 new houses per year. This is very ambitious, as 1989 was the last year this figure was reached and the current yearly number of completions is approximately 70,000. Nitrogen emissions are still an issue, but there are several new measures to keep construction on track. The central government has agreed to speed up decision-making processes for large housing projects and there are funds reserved to reduce the deposition of nitrogen in nature areas to compensate for construction emissions.

Issuing of Turkish building permits flat after volatile period

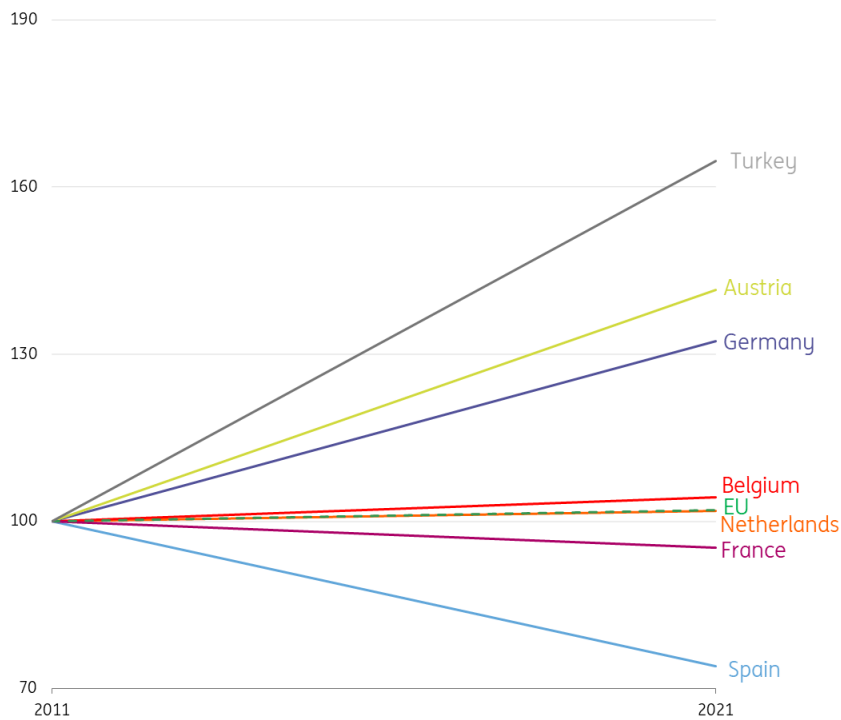
Turkey's issuance of new housing permits has been volatile in 2020 and in the first half of 2021. In the third quarter of 2021, it remained stable at a relatively higher level. However, this is far below that of 2017 before the Turkish exchange rate crisis which resulted in a big rise in construction costs and consequently a sharp drop in building activity in 2019. In addition, the next risk for Turkey is the primary concern at the moment of high inflation caused, in part, by the devaluation of the lira.

□ Low growth infrastructure sector

The EU infrastructure sector has shown moderate growth (+1.5% YoY) in November 2021. This after almost no growth (+0.2% YoY) in the same period a year earlier. However, there are large differences between countries. The infrastructure sector in Spain for example showed a sharp decline as many construction sites were closed during the first lockdown and the sector wasn't yet in a good shape from the aftermath of the financial crisis. However, Spanish infrastructure companies are at the beginning of 2022 positive about their future building activities, as Spain will be one of the biggest beneficiaries of EU Recovery and resilience funds.

Growing infrastructure sectors in Austria, Turkey and Germany

Development volume civil engineering (infrastructure sector), index 2011=100*



Source: Eurostat, EECFA, CBS & ING Research

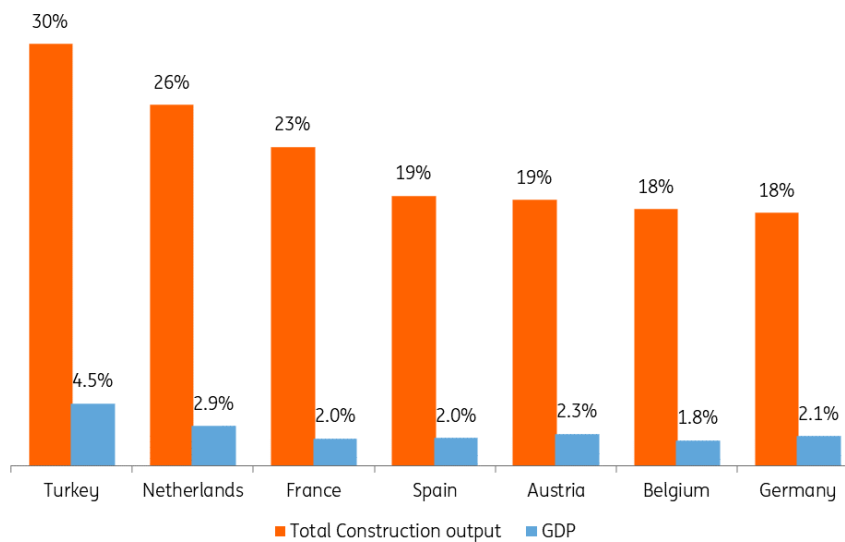
*Period Jan-Nov SA and Turkey & The Netherlands 2020 data

Huge differences in the long run

In the whole European Union, production levels in the infrastructure sector have been quite stable for the last 10 years. However, it dipped a bit during the aftermath of the financial crisis when central governments were cutting budgets but caught up after that. The infrastructure volumes in Belgium, The Netherlands and France are also around the same level as 10 years ago. In Germany, investment in rail and roads increased by more than 30% in the last decade. That is needed because German infrastructure is in a patchy state. For instance, the Tallbrücke Rahmede viaduct, which is part of an important highway through the Ruhr Area, is neglected in such a way that it's impossible to renovate and has to be torn down and rebuilt. Despite the high growth rate, the infrastructure sector is still relatively small in Germany compared to many other European countries.

Relatively large infrastructure sector in Turkey and small in Germany

Production infrastructure sector in 2020 as a % of GDP and total construction output



Source: Euroconstruct, Eurostat, EECFA, ING Research

More growth expected for EU construction sector

In general, our EU Construction Outlook remains optimistic. Despite the shortages of building materials and structural shortages of labour, we expect further growth in the EU construction sector in 2022 and 2023. Building volumes can be boosted by new investments from the EU Recovery fund. Ongoing housing shortages and high house prices provide structural demand for new residential construction. Furthermore, non-residential construction will see a rebound as the Covid-crisis fades, and entrepreneurs are less reluctant to invest in new company premises or renovate their existing properties.

2.5%





EU construction output in 2022

Forecast (volume % YoY)

The construction sector in **Germany** has been quite resilient during the Covid crisis. It was the only country that did not witness a decrease in construction volumes in 2020. However, construction output development was almost flat in 2021. Bad weather at the beginning of 2021 and pull-forward effects due to the termination of a VAT reduction at the end of 2020 hampered growth last year. In addition, German contractors are among the most constrained by labour and material shortages at the moment. Nevertheless, we expect that German construction will resume growing. The growth of permit-issuing for residential building is moderate, order books are at their highest peak this century and supply chain disturbances will probably diminish in 2022.

EU Construction Forecast: Growing construction volumes

Volume output (value added) construction sector, % YoY

	2020	2021*	2022*	2023*
 Austria	-3.0%	4.2%	2.5%	2.0%
 Belgium	-4.9%	7.0%	2.0%	1.0%
 France	-16.1%	12.8%	2.5%	1.5%
 Germany	2.8%	0.0%	2.0%	1.5%
 Netherlands	-1.1%	2.0%	3.0%	2.5%
 Spain	-11.2%	-4.1%	3.5%	4.0%
 European Union	-5.0%	5.0%	2.5%	2.5%
 Turkey	-5.5%	3.0%	1.5%	2.0%

Source: Eurostat, ING Research

*Forecasts

For **Spain**, we forecast a recovery of construction volumes this year and next but it won't make up for the large drop from the last two years. Yet Spanish building backlogs are better filled and Spanish construction confidence was almost neutral in January 2022. Furthermore, building permit issuance is on the rise but output will still suffer a bit from the lower levels during the last two years. The Spanish construction sector will see positive effects from investments of the EU recovery funds.

The **Netherlands** witnessed minor growth in 2021 in construction output. Building restrictions due to excessive nitrogen emissions have limited production, especially in the infrastructure sector. We expect slightly stronger growth in 2022 and 2023. As several government measures are being introduced and the newly installed government intends to create a fund for "national programme" in rural areas. This fund is mostly aimed at reducing nitrogen emissions (including buyouts for farmers near protected nature areas, cumulatively the size of 3.1% annual GDP) which also could give some space for new building projects. Even though building permits dipped a bit in the third quarter 2021, the Dutch confidence indicator is still at a high level and order books are well filled. We expect that construction production growth will continue this and next year.

We see further recovery in **France** and **Belgium** this and next year. The construction sector in both countries was severely hit by the pandemic in 2020, therefore the high growth rates in 2021 reflect a rebound from low levels. Furthermore, French construction output still won't reach its pre-Covid level this year.

For **Turkey**, expectations are uncertain due to the effects of current high inflation in the country. In November 2021, Turkish construction turnover soared by more than 50% (YoY) mainly due to high inflation. Volume growth was consequently a lot lower. Demand for new construction is hindered by these high prices and we, therefore, diminished our growth expectations compared to our September forecast. Still, there will be some low growth left for this year and next but output

volumes won't reach levels seen before the Turkish financial crisis.

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