

EU construction outlook: Two years of modest decline in the building sector

Material shortages are decreasing in the EU building sector but labour scarcity remains a challenge. The share of renovation is growing due to sustainability work. This makes the sector less volatile. Therefore, only a modest decline is expected in 2023

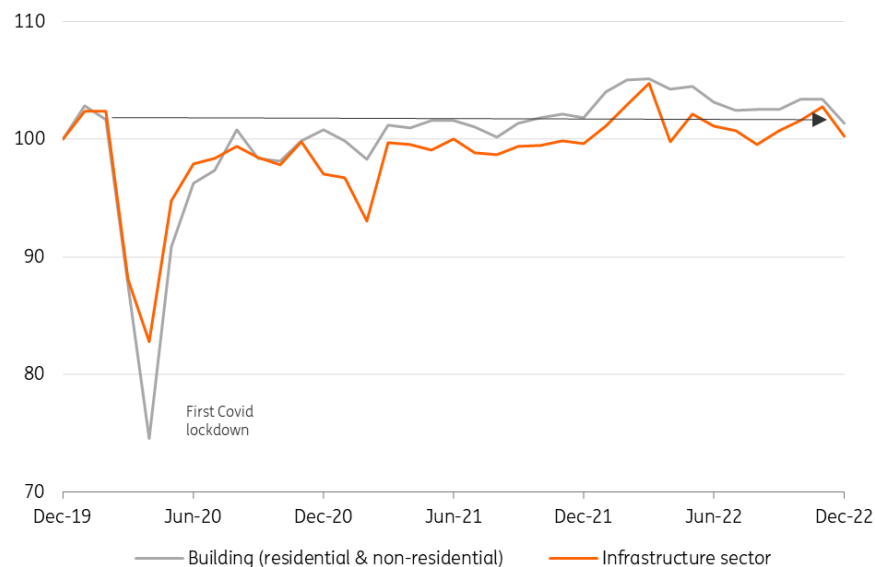


Construction volumes remain stable

In December 2022, the EU's construction output was approximately at the same level as at the end of 2021. This counts for both subsectors; building and infrastructure. Despite economic headwinds, order books are still well-filled. On average, EU construction companies had exactly nine months of work in stock at the beginning of 2023. That's 0.2 months more than in the last quarter of 2022.

EU construction volume keeps hovering around the pre-pandemic level

Development EU construction sector volume (Index December 2019=100, SA)



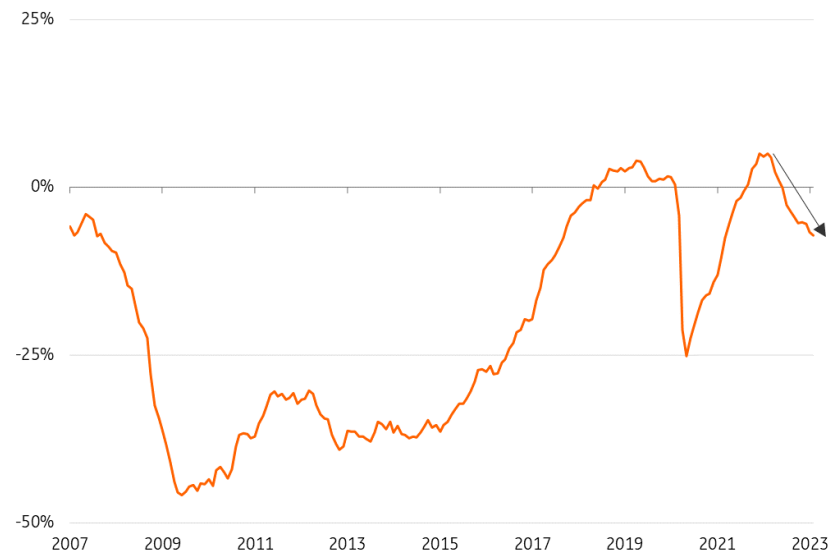
Source: Eurostat, ING Research

Less satisfied with order books

Due to the uncertain economic situation, some orders are somewhat less certain than previously thought. In addition, the increased costs of materials have made it more difficult for businesses in the building industry. As a result, profit margins are regularly lower than previously calculated. As a result, EU builders have in recent months become less satisfied with the quality of the orders they hold. On balance, they are not positive about the work they have in the pipeline.

Quality of order books for EU construction companies is declining

Evolution of order books in the EU construction sector (SA, latest data point February 2023)



Source: European Commission, Eurostat & ING Research

The prices of many building materials have been decreasing lately

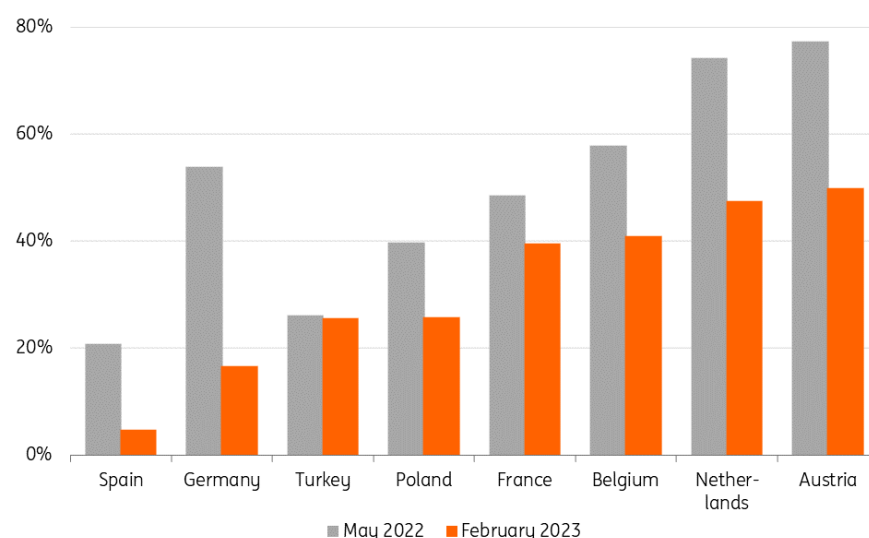
The prices of many building materials (eg. timber and metals) peaked during the summer of 2022 and have fallen steadily since. The reasons for this are the diminishing supply chain disruptions and weakening demand as forecasts for economic development in many countries have been lowered. The normally stable price of concrete, cement and bricks increased steadily in 2022 due to rising energy prices as the production processes of these materials are very energy intensive. Despite decreasing energy prices, prices for these energy-intensive building materials were still increasing at the beginning of 2023. [We expect](#) that it will take another one or two months before these prices gradually decline as well.

Fewer contractors expect to increase their sales prices

Fewer contractors have to increase their sales prices due to the lower costs of some building materials. This has been especially the case in Austria and The Netherlands. In May 2022, a record percentage of approximately 75% of the companies in these countries replied in a survey that they were scheduling a sales price increase. This percentage decreased to almost 50% in February 2023. In Germany, there was an even larger decline from 54% to 17% over the same period. In addition, decreasing demand for construction works due to higher interest rates and the uncertain economic situation can also result in fewer companies expecting to increase their sales prices due to increasing competition.

Diminishing price increases for construction companies

Balance of construction companies that expect to increase -/- decrease output prices (over the next three months)



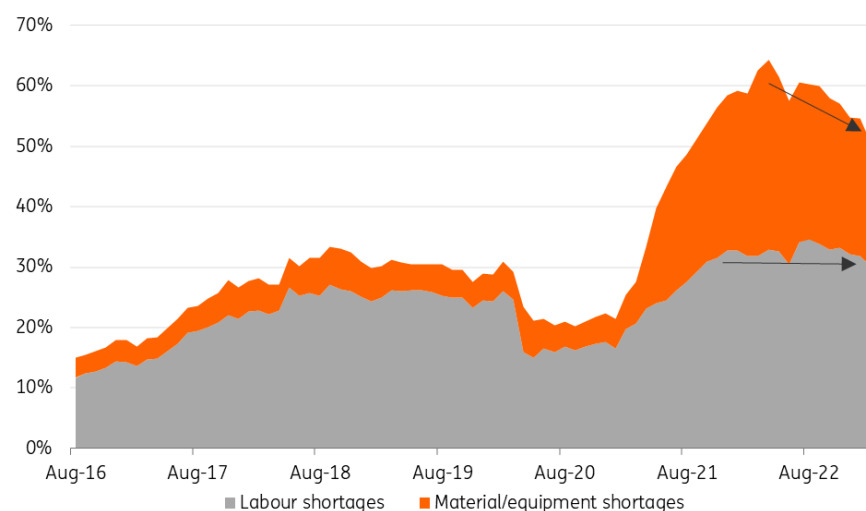
Source: European Commission, Eurostat & ING Research

Diminishing material shortages

In February 2023, a fifth of all EU contractors indicated lower production due to a lack, or delayed delivery, of building materials. The shortages are abating due to the easing of supply chain problems in the economy. Shortages are still the highest in Poland and France, although they are decreasing in these countries as well, while there are almost no construction firms that mention a shortage of building materials in Spain. One of the main reasons for this is the decreasing construction output levels in the country which limits the demand for building materials.

Shortage of labour is a structural problem. Shortage of materials is temporary

% of EU construction firms that have to limit production because of (cumulative):



Source: European Commission, Eurostat & ING Research

Structurally not enough staff

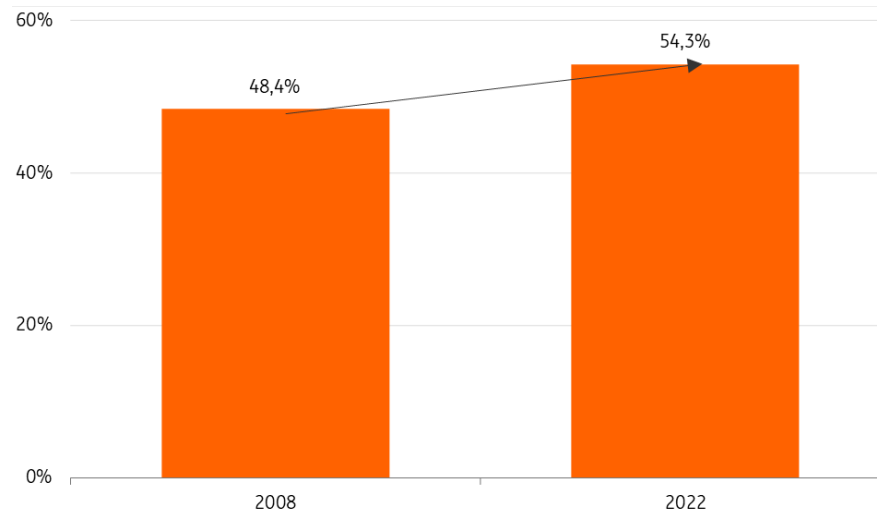
Another factor limiting production, but with a more structural nature, is the availability of sufficient labour. In the European Commission survey, a quarter of the EU contractors cite this as problematic, particularly firms in Austria, France and Germany. Companies can do several things to try to solve this problem. For instance by increasing [labour productivity](#) through industrialisation and digitalisation, attracting skilled workers from abroad, or investing in education for younger employees and trying to commit them to the company for a longer period.

Share of R&M increases

The renovation and maintenance market (R&M) is often overlooked in the construction sector. It is composed of small, fragmented firms and often lacks (reliable) data. It is also deemed less glamorous than new construction. However, the share of the R&M market has slowly increased in the last 15 years. In 2008, 48% of EU production volume consisted of R&M works. This has gradually increased to more than 54% in 2022. We expect that this share will increase further as the need for energy efficiency measures (eg. insulation, [hybrid] heat pumps and solar panels) increases due to high energy prices and sustainability measures and legislation, such as the upcoming [Energy Performance of Buildings Directive \(EPBD\)](#) that aims to ensure a higher sustainability rate.

Share of renovation increases slowly in the building sector

Renovation share of total building production



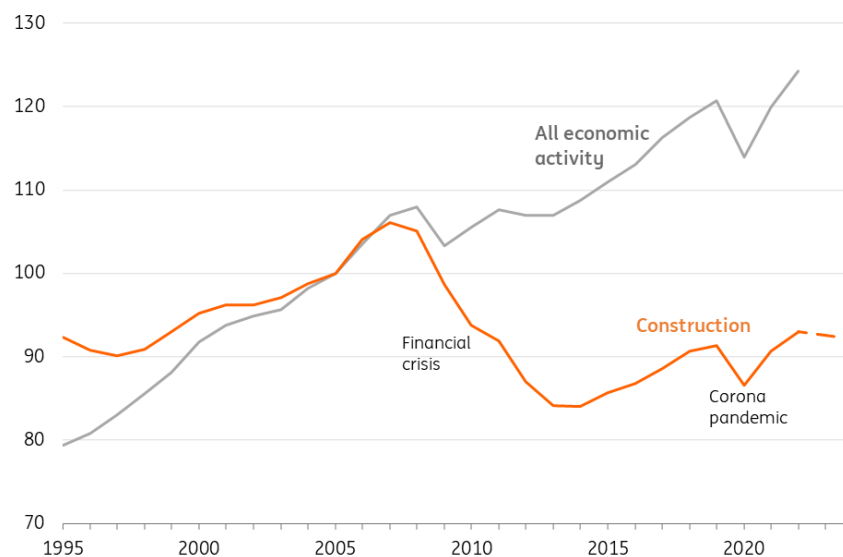
Source: Euroconstruct, ING Research

R&M market is less volatile

Although there is a strong demand in many countries for more houses, new building projects are often complicated due to land shortages and complex and long (juridical) procedures. In addition, the market for new buildings is volatile and very dependent on the economic cycle. The need for R&M is, however, an ongoing process and is therefore less susceptible to fluctuations in the economy. Furthermore, the demand for R&M may even increase during an economic crisis. For instance, during an economic downturn, homeowners may not be able to sell their homes and may choose to improve their current living spaces to accommodate their needs. This results in an increase or at least sustains the demand for R&M.

Construction sector in more gradual territory

Development production (volume value added) EU, Index 2005=100



Construction less volatile than in the past

An increasing share of R&M in the construction sector could make the total construction sector less volatile as the share of the choppy new building subsector decreases. During the financial crisis, EU construction decreased by almost 20% (2007-15). Since then we have only seen a gradual increase, except for the temporary dip during the first wave of the Covid-19 crisis. Construction volumes have also increased at a slower pace than EU GDP. Therefore, it doesn't look like there is a new bubble (as during the financial crisis) in the construction market. That being said, the construction sector is often hit late in the economic cycle due to long lead times.

Modest decline expected in the EU construction sector

Taking everything into account, higher interest rates and a weaker economy are currently causing home buyers and firms to be more hesitant to invest in new residential and non-residential buildings. Moreover, although some building material prices have decreased in recent months, the increased costs of new investments have made new buildings more expensive. Nonetheless, EU construction firms still have a healthy backlog of work, with nine months of guaranteed projects as of the beginning of 2023. While the EU construction confidence indicator declined in the first half of 2022, it has since stabilised around a neutral level. We therefore stick to our [previous forecast](#) (from January 2023) and expect only a very slight decrease (-0.5%) in total EU construction volumes in 2023. We expect the same modest decline in 2024.

A quick overview of the various EU construction markets










Germany: two consecutive years of contracting building volumes and a third to come

In 2022, German construction output declined by 1.5%, after a 1.6% decrease in 2021. This is the first time since 2008-10 we have seen two consecutive years of contraction. While order books in the first quarter improved a bit, they are lower than a year ago. The building industry suffers from

the [weak German economy](#). German contractors are still facing significant challenges due to labour shortages. Material shortages are decreasing but the current water levels have hit a new low for this time of year, posing a risk of causing new supply chain disruptions as many heavy building materials (such as sand and gravel) are transported by barges. In January, construction activity bounced back (+13% month-on-month) after a strong (perhaps mainly technical) fall in November and December 2023. Nevertheless, for the whole of 2023, we forecast a moderate contraction of the largest construction market in the EU.

EU Construction Forecast

Volume output construction sector, % YoY

| | | 2021 | 2022* | 2023* | 2024* |
|---|----------------|-------|-------|-------|-------|
|  | Austria | 7.7% | 3.4% | -1.0% | 0.0% |
|  | Belgium | 4.2% | 1.5% | 0.5% | 1.0% |
|  | France | 13.8% | 2.5% | -0.5% | -0.5% |
|  | Germany | -1.6% | -1.5% | -1.0% | -0.5% |
|  | Netherlands | 2.7% | 2.9% | -0.5% | -1.0% |
|  | Poland | 1.5% | 8.2% | -1.0% | 1.0% |
|  | Spain | -6.2% | -7.2% | -3.0% | 0.0% |
|  | European Union | -5.0% | 2.6% | -0.5% | -0.5% |
|  | Turkey | -0.6% | -3.0% | -1.0% | 1.0% |

Source: Eurostat & ING Research; *Estimates and Forecasts

Spain: construction sector faces its fifth consecutive year of contraction

Our projections indicate that Spain's construction volumes will continue to decline this year, marking the fifth consecutive year of contraction for the sector. At the end of 2022, the production level was almost 25% lower compared to the end of 2019. Unlike contractors in other EU countries, who are still mainly experiencing material and labour shortages, Spanish building firms are grappling with insufficient demand. In fact, more than half of all Spanish builders noted in February that inadequate demand is the primary factor limiting their production. Despite this, order books are improving and the EU recovery funds' investments in the Spanish construction sector will generate some positive outcomes. Consequently, we foresee a stabilisation of volumes in 2024.

The Netherlands: slight contraction in the construction sector in 2023/24

Growth in Dutch construction output has been declining steadily in recent years. However, in the last quarter of 2022, Dutch construction volumes increased (surprisingly) by 2.3% compared to the previous period. Yet we don't expect this will last. A decreasing number of building permits in the residential sector, the increase in construction costs and a reluctant consumer will reduce new residential construction in 2023 and 2024. At the beginning of November 2022, the Council of State

also decided that the exemption for construction works for [nitrogen emissions was no longer valid](#). This is a setback for construction companies although it doesn't make new housing projects impossible. High energy prices create additional demand for energy-saving construction works in the installation and maintenance market. We therefore only expect a modest contraction in the Dutch building volume this year and next.

Belgium: low growth for the construction sector in 2023

The Belgian construction confidence index has been hovering around a neutral level for several months, despite an increase in building production volumes in 2022. However, the issuance of building permits for both residential and non-residential buildings has decreased over the same period. [Belgian contractors](#) are facing greater wage hikes than their counterparts in neighbouring countries, in addition to the higher cost of building materials. This has led to an increase in salaries by approximately 10% over the past year, due to automatic wage indexation. Although [Belgian house prices](#) are expected to decline slightly, they are anticipated to rise again in 2024, potentially allowing for some price increases for new buildings in the same year. The government's stimulus plans include funding to improve the energy efficiency of existing buildings, a reduction in the VAT rate for demolition and reconstruction, and funds to rebuild 38,000 homes damaged by the floods in 2021. Overall, we predict that the Belgian construction sector will experience a growth rate of around 0.5% in 2023 and 1% in 2024.

Poland: promising building start in 2023 but contraction ahead

[Polish contractors started 2022](#) with an impressive growth rate of 7% (month-on-month) in January. The relatively mild weather could be one of the reasons. The outbreak of war in Ukraine caused heightened tensions in the construction labour market due to shortages. This is because some Ukrainian males who had been previously employed left Poland to fight for their homeland, while the refugees who arrived mostly consisted of women and children who are unlikely to be able to fill the vacancies. The Polish civil engineering sector can receive a boost from an ambitious investment programme, including the EU Recovery Fund (which is still frozen due to a judiciary dispute with the EU). However, demand for new houses has deteriorated strongly, due to the high increase in interest rates and the general deterioration in household sentiment. Building permits for residential buildings have decreased by almost 13% in 2022. Therefore, we anticipate that Polish construction output will contract in 2023.

France: contractors facing enormous labour shortages

Construction output in France experienced growth of 1.7% quarter-on-quarter in the final quarter of 2022, after declines in the second and third quarters. The building sector in France is still facing significant challenges due to shortages of materials and labour, as well as price increases. In February, more than half of French contractors mentioned shortages of staff as a limiting production factor. Shortages of materials are declining but are still high. The construction of new houses is under pressure. In 2022, the number of building permits for new residential buildings contracted by more than 10%. On the other hand, government measures such as MaPrimRénov support renovation and sustainability activity. The French construction confidence index (EC Survey) is dwindling but remained positive in February (+2), and order books are still well filled with a stable eight months of work in the first quarter. Overall, a minor decline of -0.5% is expected in the French construction sector for the whole of 2022, which means that construction output in France will still fall short of its pre-Covid level.

Turkey: uncertainty in the construction sector

Due to persistently high inflation, the devastating earthquake and the presidential elections, Turkey's prospects are uncertain. The issuing of building permits for new residential buildings decreased in 2022. In February, the Turkish construction confidence indicator (EC survey) showed a negative reading of -10. Order books sharply decreased in the first quarter of 2023. Contractors are affected by high building material costs and a lack of demand due to the resulting high prices. We now forecast a continued decline in Turkish construction output in 2023, marking six consecutive years of declining building output in Turkey. The expectation is that reconstruction efforts in the form of higher public investment should generate growth in the construction sector in the longer term.

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