

2021 European Construction Outlook: Output to recover by 4%

The construction sector in the Eurozone has been hit hard, but not to the same extent as hospitality and aviation. In 2021 we expect a rebound, especially in those countries that had stringent lockdowns like Spain and France but given the uncertainty and weakening financial positions, growth is unlikely to fully compensate for the fall seen in 2020



House construction in Orleans, France

For 2021 we expect eurozone construction output to recover by 4%. The countries that had the most stringent lockdowns are likely to see strong rebounds this year but the recession is likely to leave its mark.

Permits for new dwellings - a strong indicator of future production, plunged in France and Spain in 2020, which may hinder the completion of new dwellings in the coming years, even as the pandemic abates and the demand for housing recuperates. Infrastructure companies are receiving fewer orders and expect price levels to decline too.

Due to high uncertainty and the weakening financial position of many firms, investments in commercial building are expected to decline in 2021 as well.

4%

Eurozone construction output in 2021

Forecast (volume % yoy)

French construction hit hardest during the first wave of the pandemic

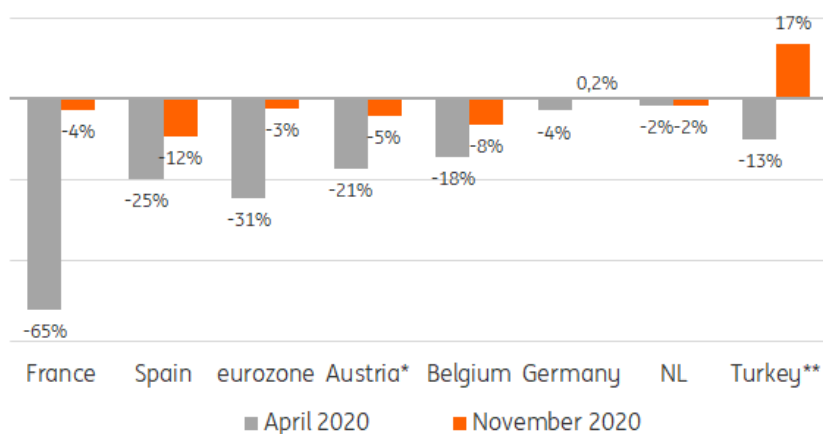
During the first lockdown, the construction sector was modestly affected in comparison to other sectors like hospitality and aviation.

In April 2020, eurozone construction output decreased by approximately 30% in comparison to January of 2020. However, differences between countries were huge. France experienced the biggest contraction in production volumes since many French construction sites closed down.

However, in Germany and the Netherlands, there was almost no decline because construction sites remained open, although, there were some delays, for instance in renovation works in the health sector as hospitals and care institutes were reluctant to welcome construction workers into buildings because of contamination risk.

Biggest construction decline in France during first lockdown

Development production volume Construction sector
(In comparison with January 2020, Seasonally adjusted)



Source: Eurostat, Turkstat and ING Sector Research

* Austria: October data, ** Turkey Turnover data

Strong recovery in many countries

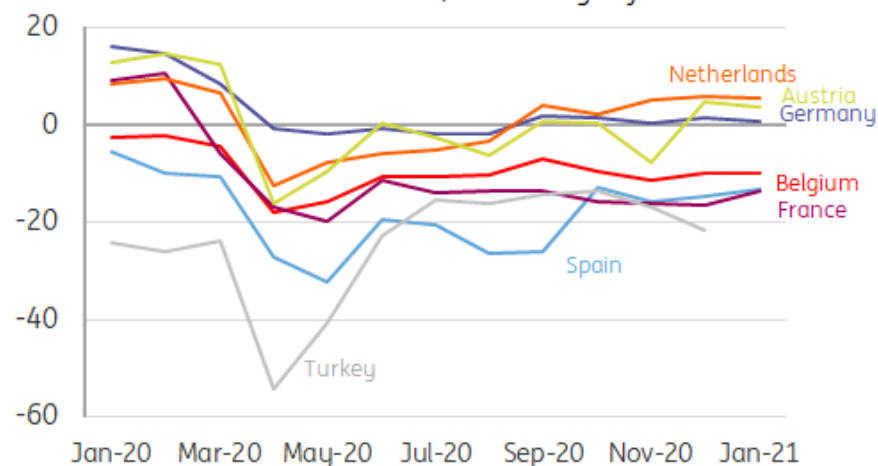
When the first lockdown measures eased and construction sites reopened, production volumes bounced back in almost all countries. For example, French construction sector production was only 5% lower in October 2020 in comparison to January 2020.

At the beginning of 2021, construction confidence indicators were positive in Germany, Austria and The Netherlands again. Many construction companies (especially larger ones) work on long-term projects which they picked up again immediately after the first lockdown.

Likewise, in the eurozone order books showed only a small decrease from 8.4 months of ensured work at the beginning of 2020 to 8.0 months in January 2021.

Construction confidence indicator positive in Germany, Austria and The Netherlands in January 2021

Construction confidence indicator, Seasonally adjusted



Source: Eurostat (No January 2021 data available for Turkey)

Second wave of lockdowns less harsh for construction

We expect the second wave of the pandemic to have a moderate impact on the European construction sector given more construction sites remain open this time, particularly in France.

In addition, production levels in winter are often lower in some countries due to the Christmas break and poor weather conditions. But workers are also now more used to social distancing measures at the construction sites which is likely to lead to fewer delays.

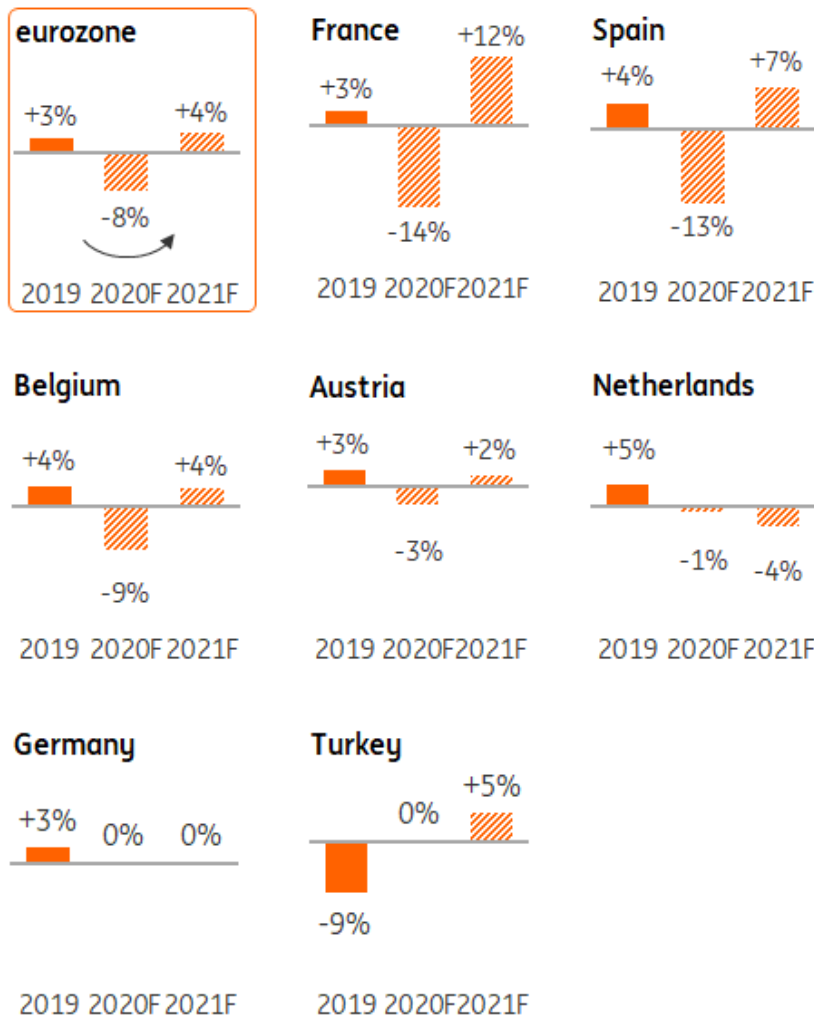
Recovery in 2021

In 2021 we expect eurozone construction output to recover. There will be a strong rebound, especially in the countries that had a strict lockdown in 2020 (e.g. Spain and France). However, we don't expect a rebound in Germany and The Netherlands, where construction sites didn't close during the first lockdown.

Given that the uncertainty regarding the duration of the pandemic is very high and the financial position of many firms is weakening, private and public investment is expected to be lower in 2021. As a result, eurozone construction output growth is unlikely to fully compensate for the decrease of 2020 this year alone.

Construction volume eurozone expected to rebound in 2021

Development Construction output (volume value-added in % yoy)



Source: Oxford, Economics, Euroconstruct and ING Sector Research

✔ Non-residential building sector

A sharp decline in new dwelling permits in France and Spain

Permits for new dwellings - a strong indicator for future production, plunged in France and Spain in 2020 because both countries implemented strict lockdowns and civil servants had difficulties processing applications whilst working from home.

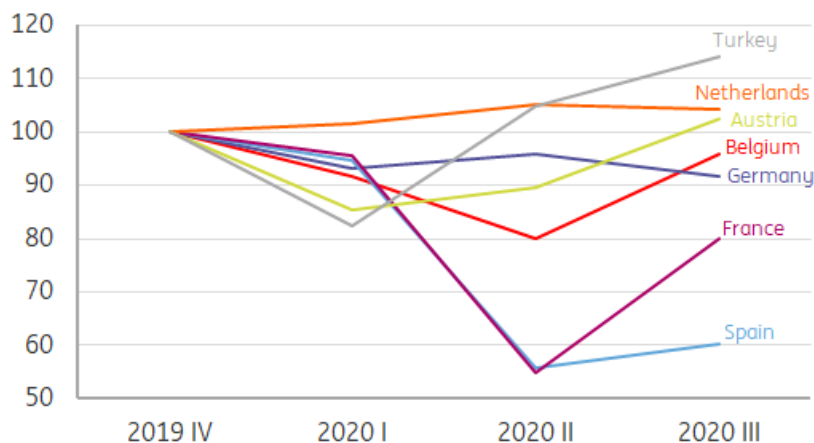
In France, there was a strong improvement in the third quarter but the number of issued permits was still 20% below pre-pandemic levels. Like France, Spain saw a similar decline in the second quarter but not the sharp increase afterwards. These low numbers of permits are likely to hinder the completion of new dwellings this year and in 2022, even as the pandemic abates. In Belgium, the reduced VAT rate of 6% for demolition and reconstruction might support the residential sector in 2021.

Some believe that lockdowns have encouraged people to move to the countryside, however, the

evidence isn't clear but there certainly an effect on the purchase of second homes.

Number of Spanish permits for new dwellings plunged

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



Source: Eurostat, ING Sector Research

More new dwelling permits for The Netherlands and Turkey

In the first three quarters of 2020, the number of newly issued dwelling permits increased in Turkey, the Netherlands and Austria.

For the Netherlands, this could be explained by the fact that working from home was already very common, which resulted in less productivity loss for permit issuing departments during the lockdowns. Also, another factor at play in the Netherlands was the reduced number of permits issued in 2019, due to new restrictive rulings that were brought in for nitrogen emitting activities in construction. Although these regulations were eased last year, applicants were accustomed to coping with these new measures.

On the other hand, after a small dip at the beginning of 2020, Turkey saw an increase in the number of dwelling permits issued. However, the level is still far below that of 2017 before the Turkish financial shock, when it was about four times as much.

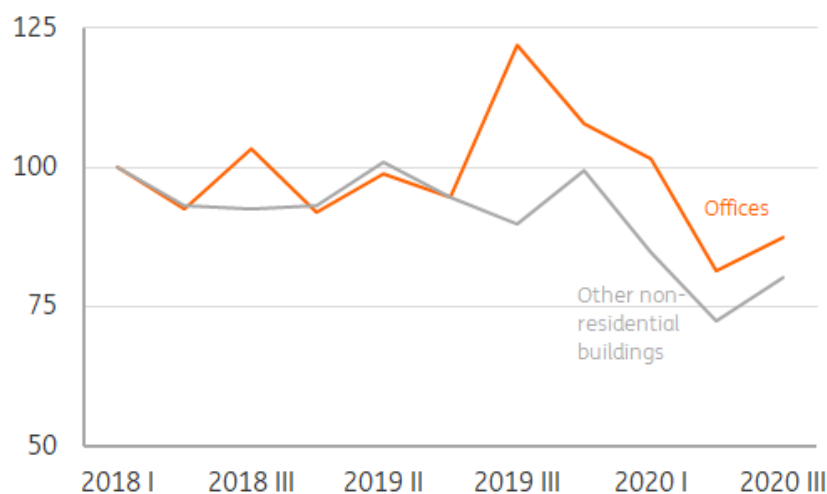
Non-residential permits on a downward slope

In the non-residential market, we see a comparable fall in building permits in 2020. Issued permits for offices peaked at the end of 2019 but declined in 2020.

The decline was the largest in Spain, followed by Belgium and France. Permits for non-residential buildings such as factories, warehouses, schools, stores and hospitals declined as well in the eurozone. After the lockdown, there was a modest increase in 3Q20.

Sharp decline non-residential building permits

New residential buildings permits in m2 excluding offices eurozone, (index 2018 Q1 = 100, Seasonally adjusted)



Source: Eurostat, ING Sector Research

Investments in offices are particularly risky

Due to the pandemic, many offices are partially vacant, as most staff work from home and a reduced workforce leads to less requirement for office space.

In the long term, the question is to what extent is the trend to work-from-home permanent and how much demand will there be for office space?

However, in the non-residential categories, the extreme increase in e-commerce due to Covid-19 has increased the demand for new logistics centres, and therefore a surge in demand is to be expected.

☑ Infrastructure

The infrastructure sector isn't immune from the pandemic either.

Infrastructure activities more often than not take place outside, which makes working with social distancing measures less complicated. However, during the first lockdown production volumes also plunged in the countries where construction sites were closed.

But given that many construction sites have remained open during the second wave, we expect less impact this time around.

Recovery plans can only do so much for infrastructure

Governments are trying to support their economies with large recovery plans.

During a "normal" economic crisis, new infrastructure projects are almost always a part of these plans as they stimulate the domestic economy in the short-run (more local jobs), and the long run via better infrastructure, however, this time appears to be somewhat different, as it is not certain

whether we will return to the same traffic congestion as before.

This is because an increasing number of people will probably continue to work from home and fewer people going on business trips.

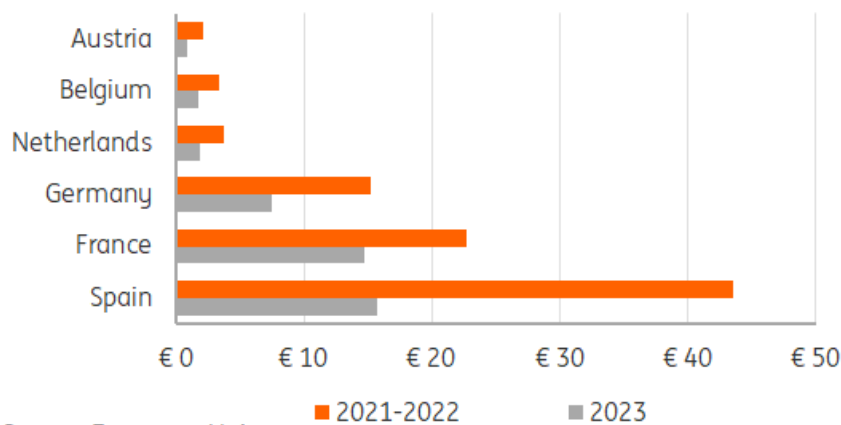
European recovery fund

Economic recovery schemes for the pandemic are focusing on other investment categories than just infrastructure.

For instance, the €672.5 billion the EU will make available in the recovery and resilience facility, aims to make European economies and societies more sustainable, resilient and better prepared for the challenges and opportunities of the green and digital transitions. The EU mainly supports regions that are most affected by the pandemic like Spain.

EU facility to help countries to come out of the corona crisis

Grants allocation Recovery and Resilience Facility per country (in € billions)



Source: European Union

Construction sector profits indirectly

Flagship areas for EU investment plans are clean technologies, sustainable transport, broadband services and digitalisation. However, big infrastructure projects aren't mentioned but that doesn't mean that the facility doesn't favour the construction sector.

For instance, installation companies can profit from more investments in electric vehicle charging stations. Cable and pipelayers will benefit from the construction of fibre-to-the-home (FTTH) for broadband connectivity, and smaller building companies will see an increase of sustainability projects for the existing building stock.

But local investments will probably shrink

Central governments are unlikely to skip or postpone infrastructure projects, but local governments might.

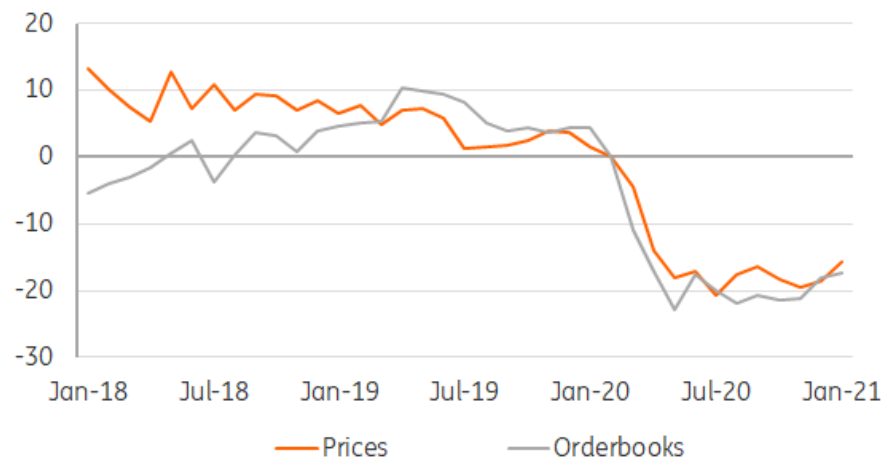
Due to the pandemic, local governments are experiencing a decrease in income (e.g. less tourist tax and parking fees) and an increase in social expenditures. To make ends meet they will probably postpone road maintenance or other small infrastructure projects like investing in new

roundabouts, particularly impacting small and local mid-sized infrastructure companies that depend on the flow of these smaller regional projects.

To keep a flow of infrastructural public projects Austria has, for instance, eased procurements procedures until the end of 2022. Public Austrian projects of up to € 1 million may be awarded directly, in a non-public process to ensure quick and non-bureaucratic procurement.

Infra sector: Lower prices and diminishing order books

Development Infrastructure sector eurozone over the next 3 months, Balance (in %-points) of the positive & negative answers, Seasonally adjusted



Source: European Commission

Lower prices and diminishing order books

As a result of diminishing investments by local authorities and moderate investments by central governments, infrastructure companies are receiving fewer orders and expect price levels to decline. Lower prices are likely to be the result of the decrease in demand, as well as a drop in the oil price as oil is an important raw material (e.g. asphalt)

Nevertheless, differences among European countries remain substantial. For instance, at the beginning of 2021, French civil engineering companies were very pessimistic about their order books as were companies in Turkey and Belgium. Dutch companies were also gloomy about their sales but this has been the case for a while due to the local nitrogen regulations.

✓ Building material

The building material industry is more volatile than the construction sector

The developments in the building material industry are closely related to the construction sector, but this industry is more vulnerable to economic shocks for two reasons.

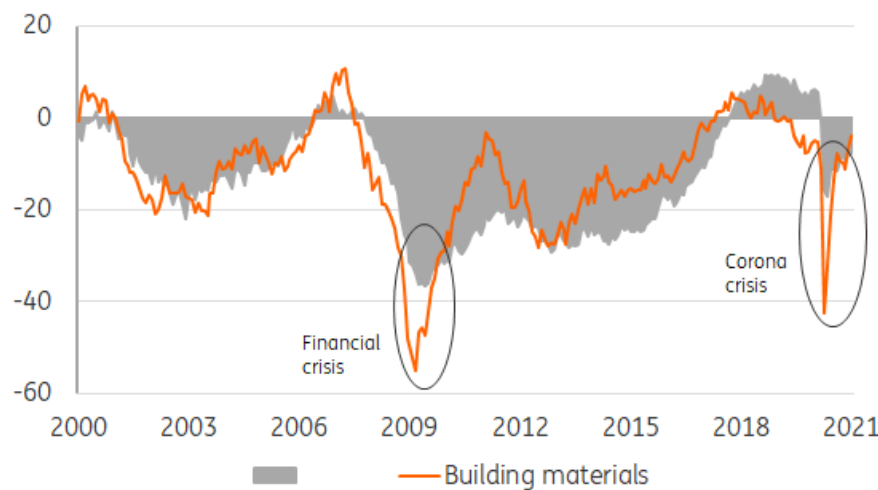
Firstly, in general, building material companies have higher fixed costs as they have invested more in machineries and factories than construction companies. This makes building material companies less agile and therefore they have more difficulties scaling down during an economic downturn.

Secondly, building materials deliver relatively more supplies for the construction of new buildings

and to a lesser extent for renovation. In general, the construction of new buildings is more volatile than renovation. Consequently, building material firms were more pessimistic at the beginning of the pandemic (and during the financial crisis) than construction companies. As soon as they saw, in May and June 2020, that the impact of the crisis was relatively limited on the construction sector their confidence improved.

Confidence building material sector more volatile than construction sector

Producer Confidence indicator eurozone, Seasonally adjusted (monthly)



Source: Eurostat & European Commission

Production building materials recovered

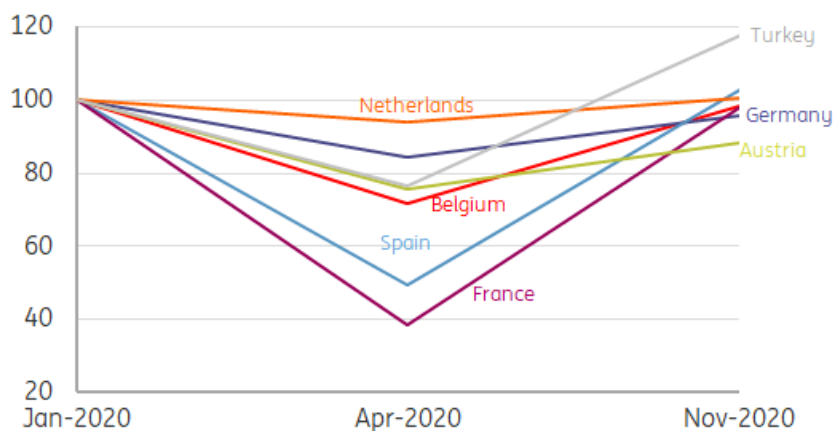
The production of building materials declined substantially during the first lockdown. And like the construction sector, Spain and France saw dramatic declines. But by November 2020, production levels were restored in most countries to pre-pandemic levels.

In Spain, there were slightly more building materials produced than in January 2020 while in Turkey, the level increased by almost 20%. For 2021, we expect similar production development to the construction sector, which means Spain and France will experience further recovery.

In addition, we expect a modest decline in Germany and The Netherlands that did not experience a sharp decrease in construction in 2020 due to milder lockdowns.

Production volumes building materials industry recuperating

Volume production building materials
(Index Jan 2020 =100, Seasonally adjusted)



Source: Eurostat, ING Sector Research

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