

# New foundations for the construction sector?

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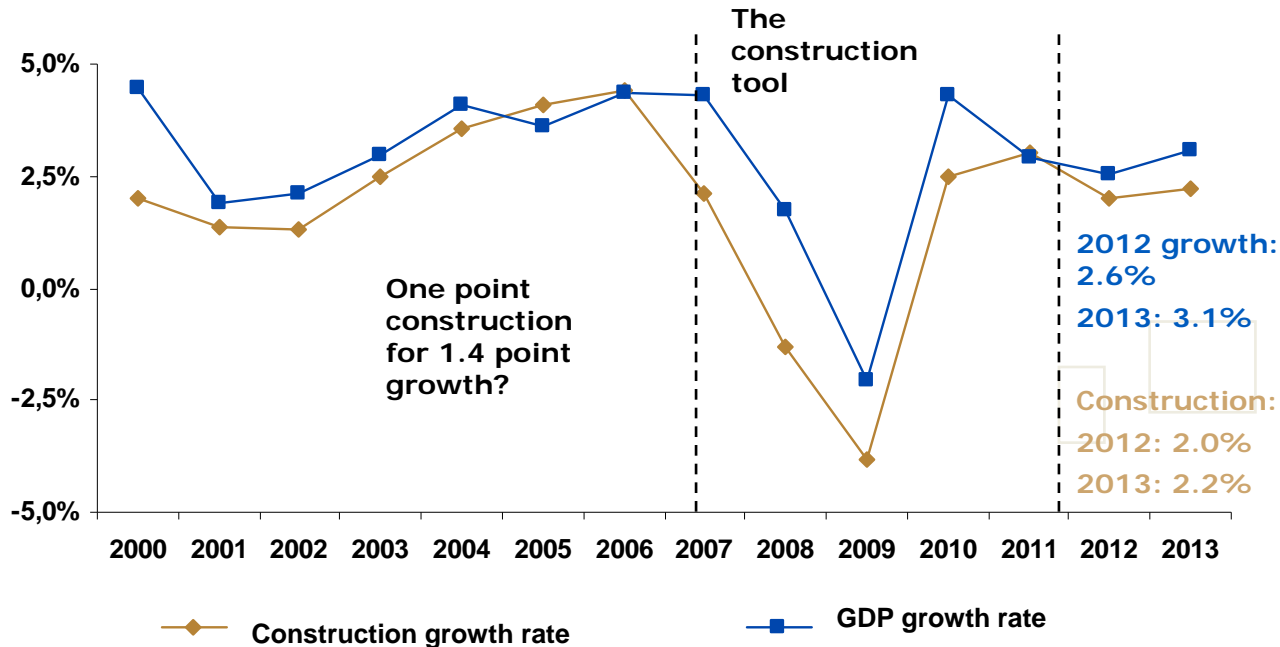
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- 1. Can construction growth revive?**
- 2. Without growth, what is left for the construction sector?**
- 3. Erosion of profitability for sector companies**
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# Can construction growth revive?



## Evolution of GDP and construction at global level



Sources: GlobalInsight, IMF, Euler Hermes

- Existence of a structural link between the construction sector and economic growth: myth or reality?

- If so, how?

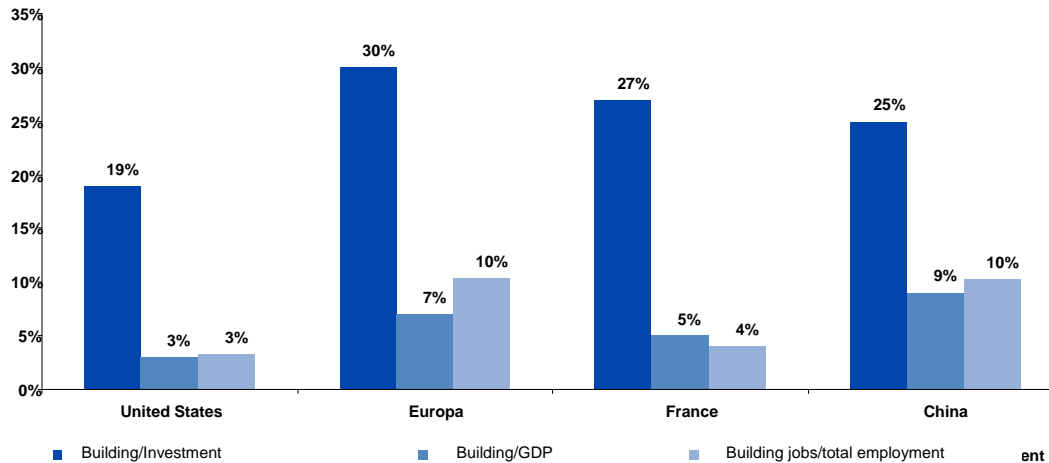
- No direct answer, but an intuition?

## ▶ The structural link between construction and GDP

# Can construction growth revive?



## Construction to support growth



Source: Comptes de la Nation, Euler Hermes

- **Construction is a source of investments**
- **Construction creates wealth and jobs**

### Recovery plans:

**France: 1.8 billion Euros**

**China: 12 billion Euros**

**United Kingdom: 2.1 billion Euros**

### Investment plans:

**Brazil 2001/2014: 660 billion Euros (road network, energy production)**

**India: 100 billion Euros over 5 years (rail network, bridges)**

### Measures to support the residential sector:

**Tax allowances, low-interest loans (France: zero-interest loan).**

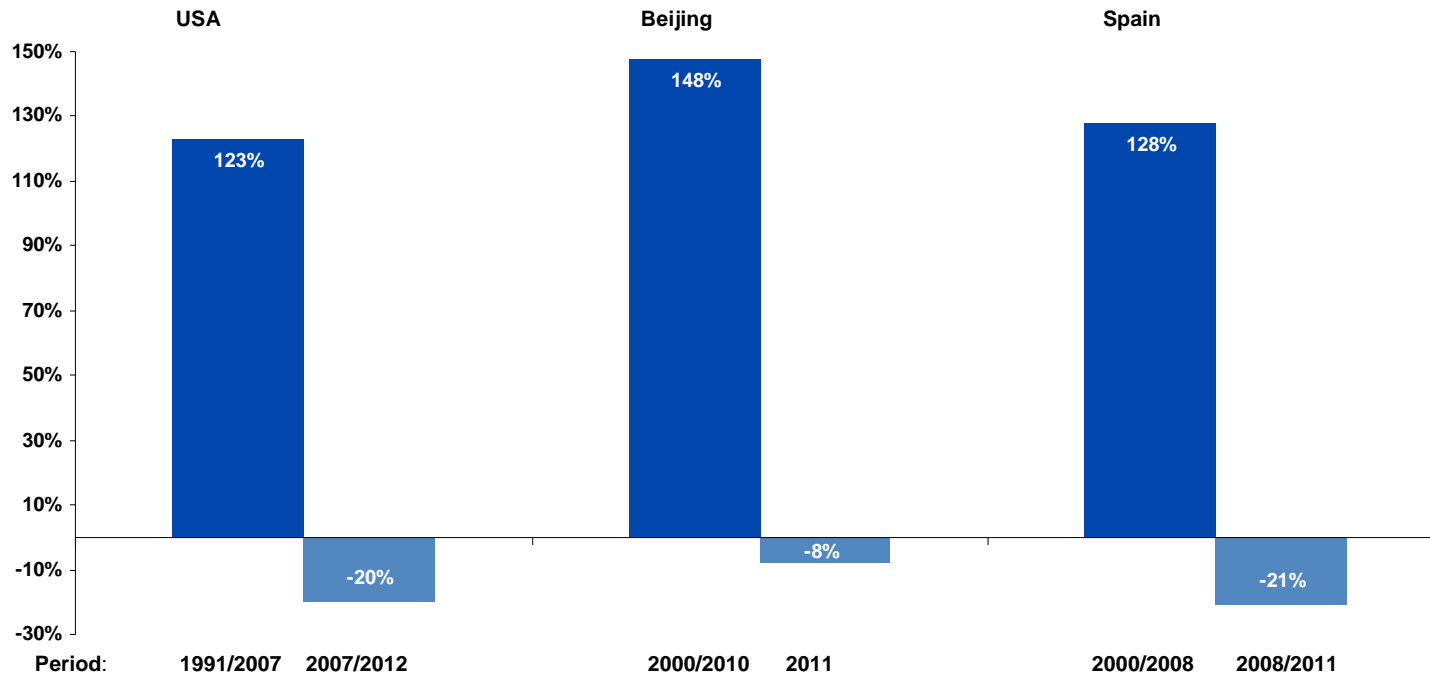
**Extending credit periods (USA: 30 years, Spain and Portugal: 40 to 50 years)**

Construction represents key element of the economy

# Can construction growth revive?



## Evolution of real estate prices in the USA, China and Spain



- No continent has been spared the real estate bubble
- Absorbing the housing inventory available for sale will take several years

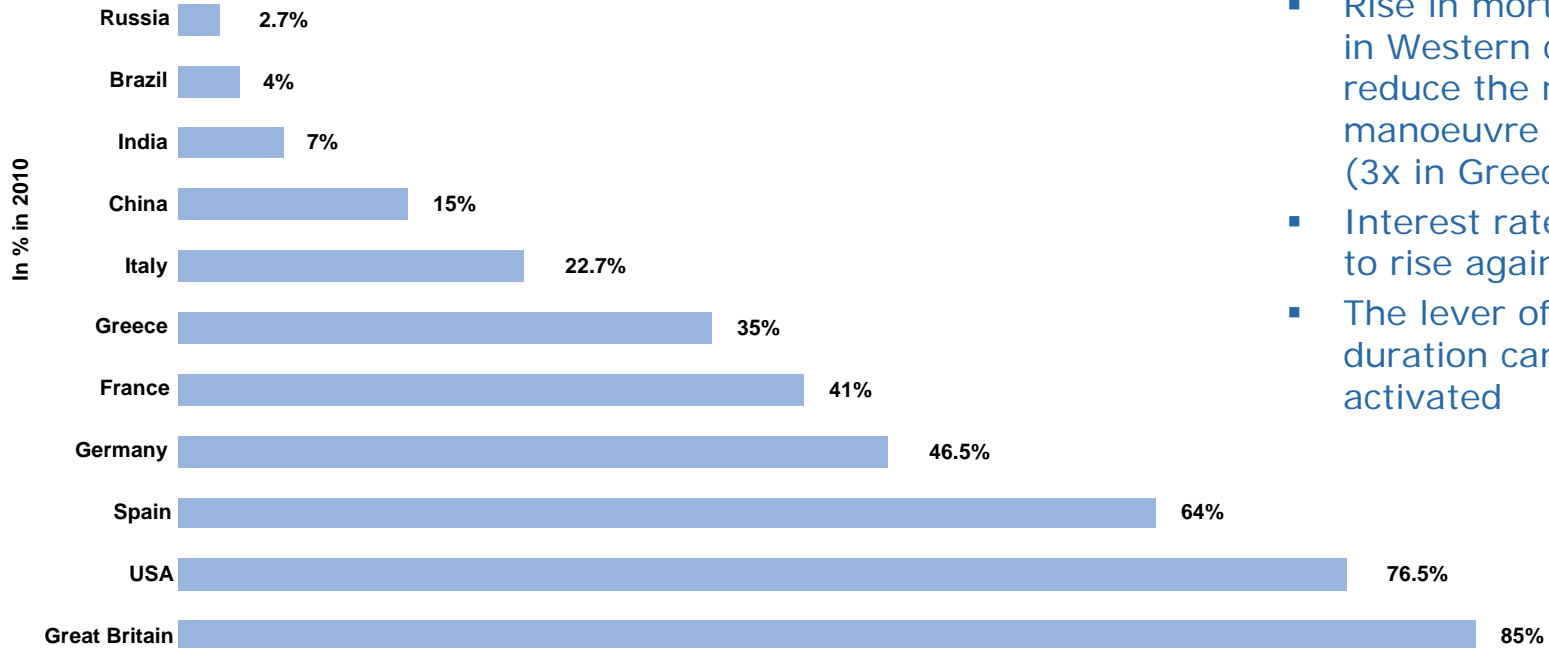
Source: Euler Hermes

▶ Real estate bubbles have followed successively on all continents

# Can construction growth revive?



## Household mortgage debt/GDP



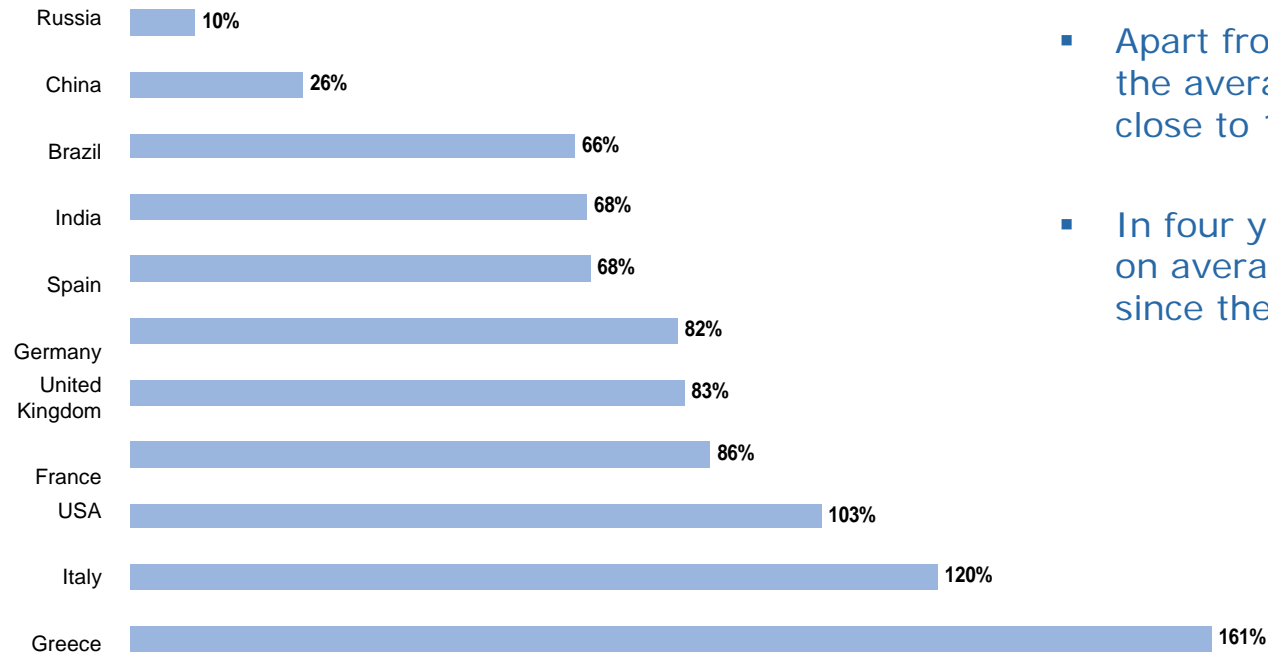
- Rise in mortgage debt ratio in Western countries will reduce the room to manoeuvre for several years (3x in Greece in 10 years)
- Interest rates have started to rise again.
- The lever of extending loan duration can no longer be activated

Sources: European Mortgage Federation, Eurostat, Euler Hermes

▶ Household debt has eroded their financial position

# Can construction growth revive?

## National debt as a % of GDP



- Apart from emerging countries, the average national debt ratio is close to 100%
- In four years, it has risen by 35% on average, after being stable since the beginning of the decade

Sources: IMF, Eurostat, Euler Hermes

▶ The cost of reviving construction is very high

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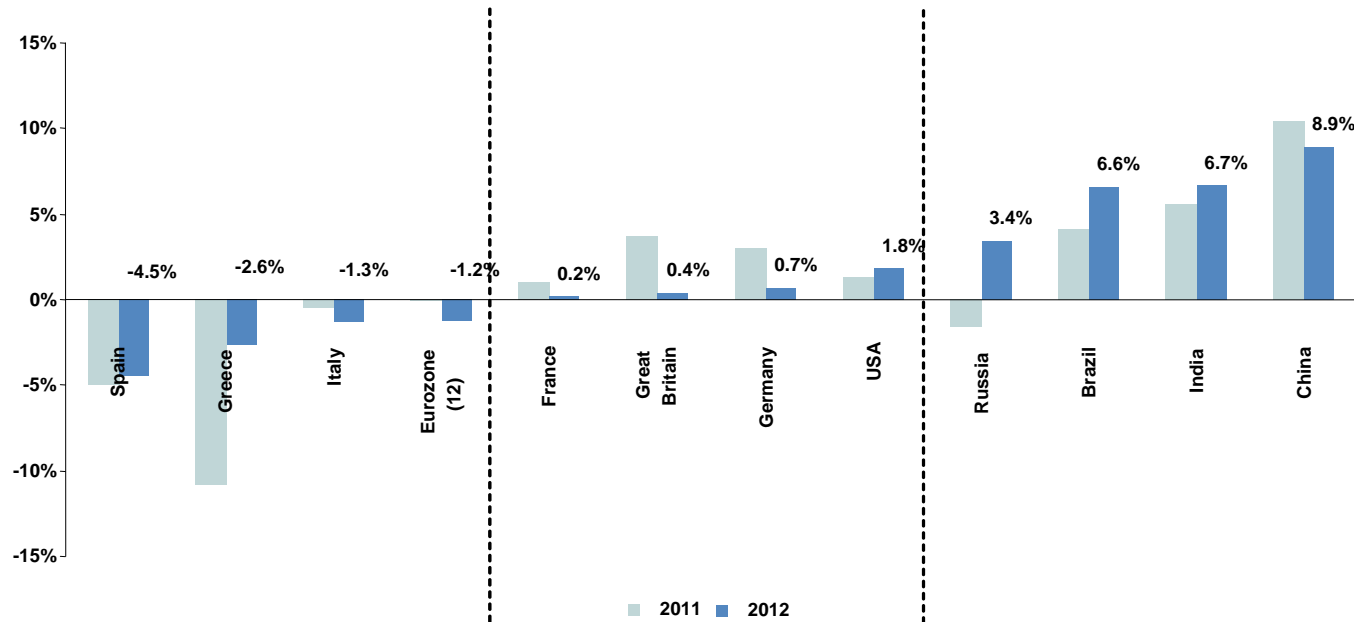


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# What is left for construction?

## Evolution of construction activity indices in volume



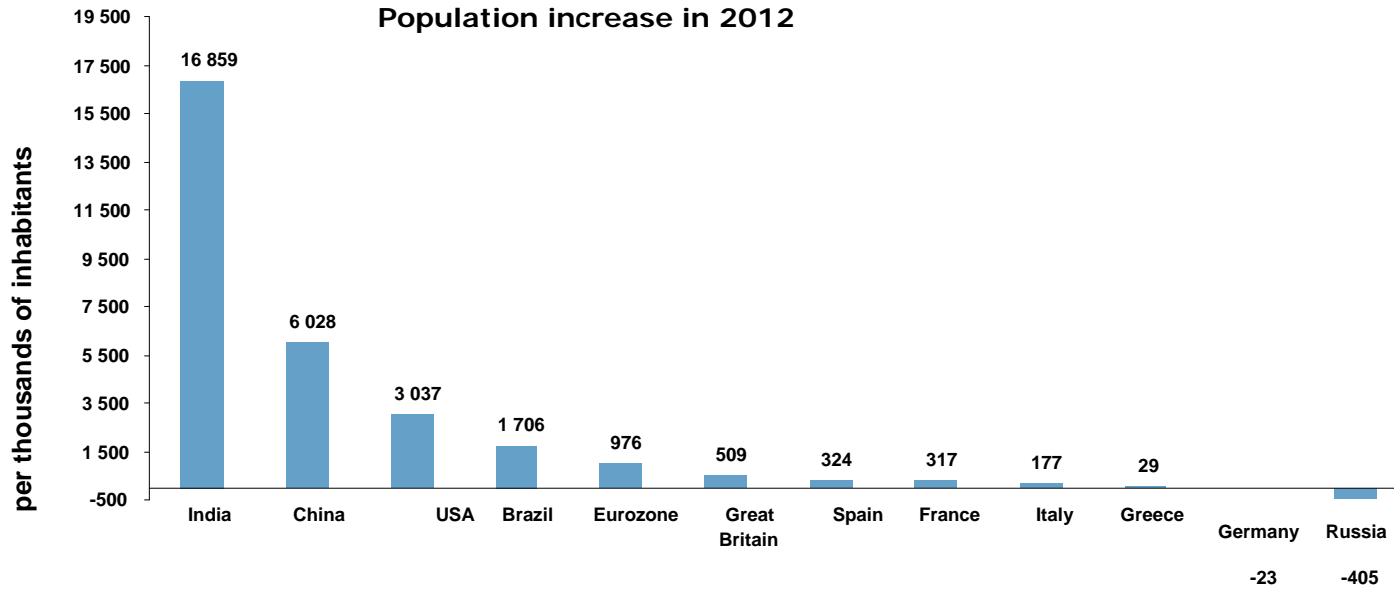
- USA: a gradual exit from crisis for the first country to enter it
- Spain: continuing impact from the collapse of the real estate bubble
- Eurozone hampered by the Mediterranean countries

Sources: GloballInsight, IMF, Euler Hermes

▶ The activity (+2.0% in 2012) is driven by the emerging countries

# What is left for construction?

## Population increase (in thousands) and urban development rates (in %)



## Urban development rates by country in 2011 (in % of the population)

30.9%   49.2%   82.1%   84.2%   73.0%   79.5%   77.3%   85.2%   68.2%   61.2%   73.8%   73.7%

Sources: OECD, United Nations, Euler Hermes

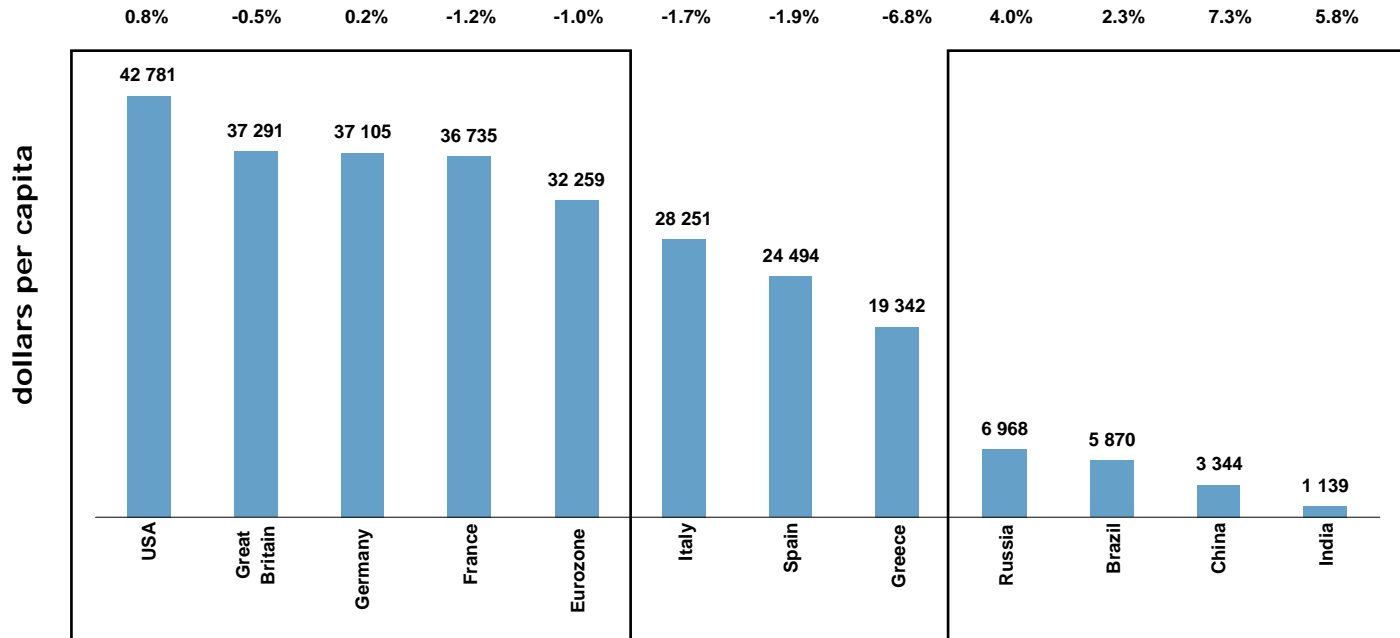
- Dual demographic effect in India
- High urban development potential
- Brazil to rebuild urban housing
- Housing shortage:  
France: 500 000  
Brazil: 10 million  
India: 24 million

## The dual effect of the demographic variable

# What is left for construction?

Per capita GDP change in 2012 (in \$ and in %)

Growth rate of per capita GDP 2012/2011



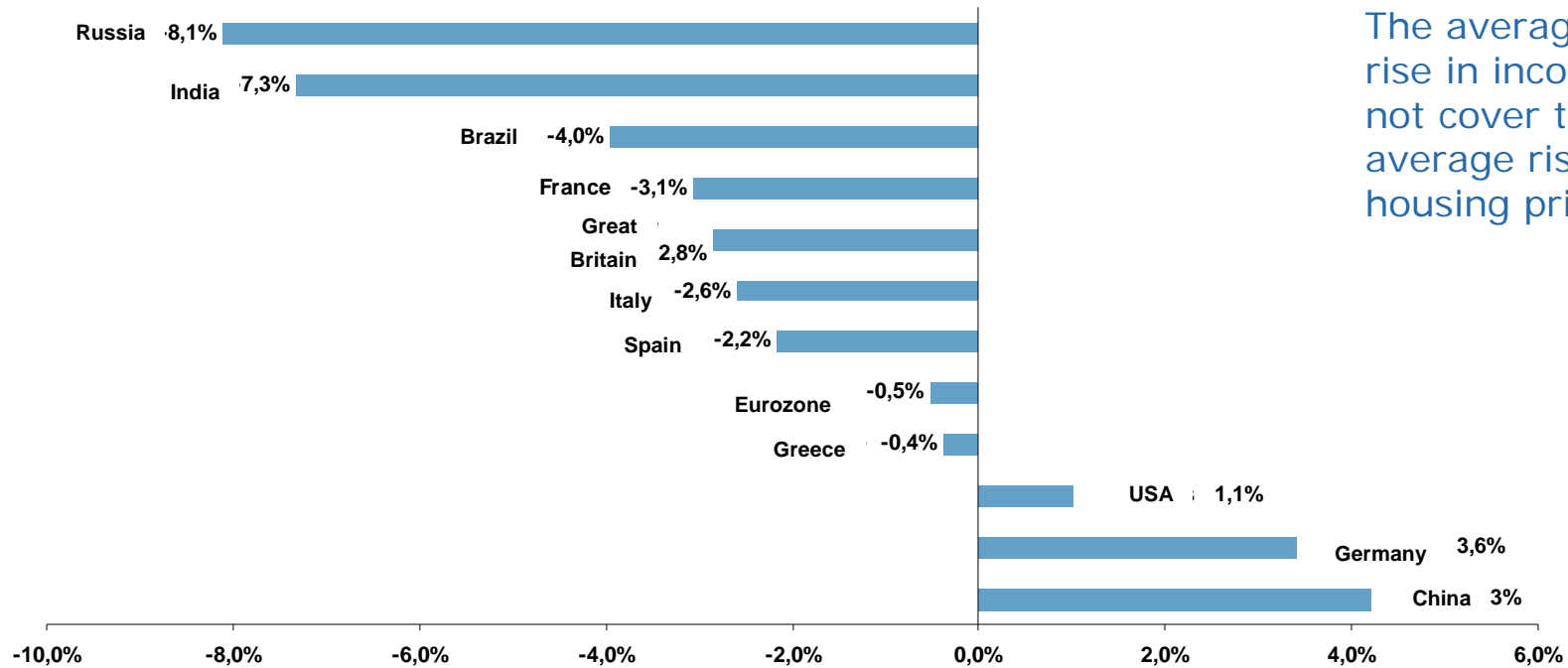
Sources: GlobalInsight, World Bank, Euler Hermes

- High levels of wealth in Western countries
- Faster growth in the emerging countries, despite persistent inequalities
- Tense situation in less wealthy Western countries that are experiencing the crisis

▶ Two worlds with two measurements of wealth

# What is left for construction?

## Differential between the growth rate of income and housing prices since 2000



The average annual rise in income does not cover the annual average rise in housing prices

Sources: World Bank, National statistics offices, Euler Hermes

▶ But the disparity between prices and income is general

# What is left for construction?

## New growth opportunities

**Environmental standards for energy savings and lower CO2 emissions: 550 billion dollars**

**Additional cost of an HEQ and BBC building: 10% to 15% more**

**Prospects for the renovation sector: 80% of buildings do not meet environmental standards**

**75% of existing buildings in Russia and 40% in Poland**

**Commercial and office investment:  
office real estate is driving corporate investment in Western Europe:  
+7% in the first quarter 2012**

**External events:  
2014: World Cup in Brazil  
2016: Olympic Games in Brazil  
2014: Winter Olympic Games in Russia**

Source: Euler Hermes

► **Some potential for growth exists in the world**

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# Erosion of company profitability

## Profitability of large global groups

| Net income/Turnover | 2010 | 2011 | 2012 |
|---------------------|------|------|------|
| China               | 1.9% | 2.1% | 2.2% |
| Europe              | 5.0% | 3.7% | 3.6% |
| USA                 | 4.3% | 4.9% | 4.8% |

Sources: Companies, Euler Hermes

- Low profitability of Asian groups, despite a very gradual improvement
- European and American groups lead, despite eroding profits

▶ Large European groups caught by the crisis: -1.4 point in two years

# Erosion of company profitability

## French companies' profitability

| France              | 2010 | 2011  | 2012 |
|---------------------|------|-------|------|
| Turnover trend      | 0.8% | 1%    | 0.5% |
| Net income trend    | -9%  | +0.5% | -3%  |
| Net income/turnover | 3.6% | 3.6%  | 3.4% |

- Business stagnation
- Pressure on prices
- Scissor effect on raw materials:
  - Steel:**  
*August 09/April 12: +22%*
  - Cement:**  
*+3% per year since 2010*
- Deterioration of profitability

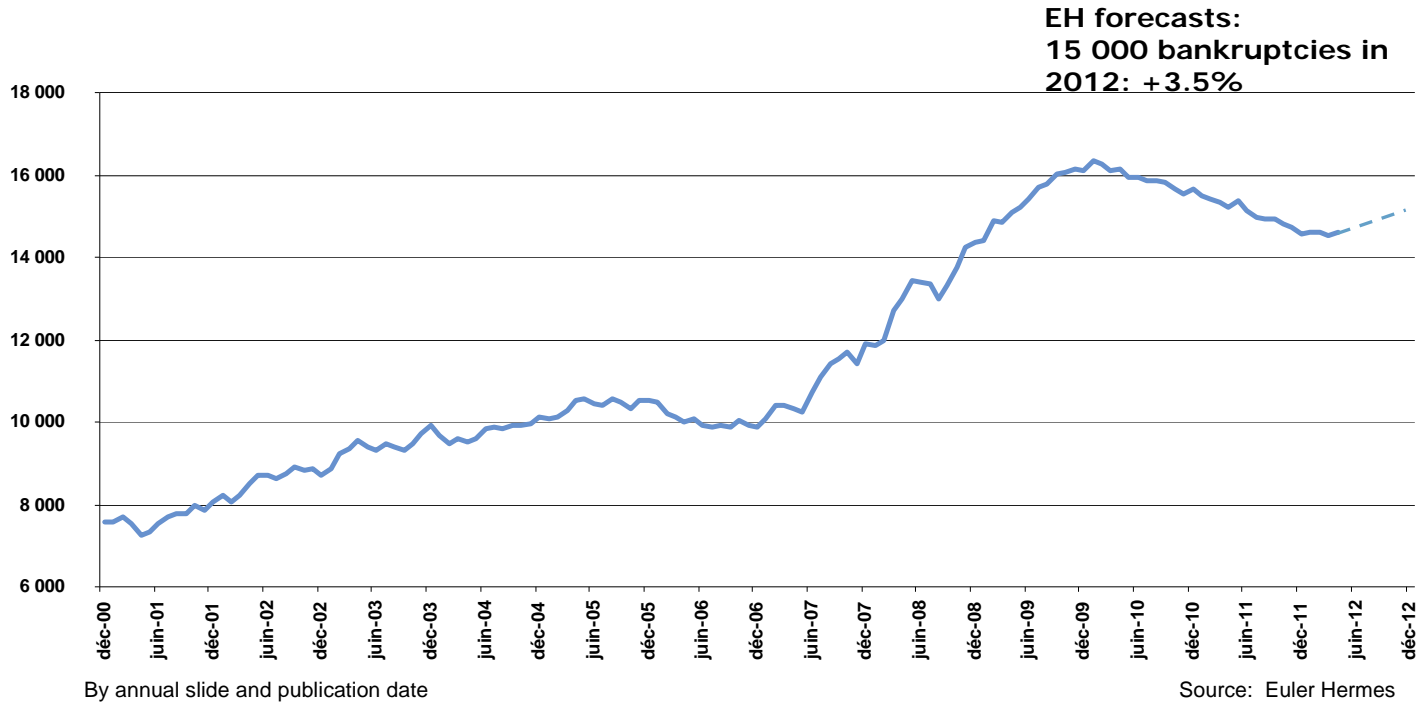
Source: Sample of 125 000 companies, Euler Hermes

▶ 3% profitability drop expected in 2012



# Erosion of company profitability

## Bankruptcies in Building & Public Works in France



Building & Public Works in France: 25% of bankruptcies in France

Bankruptcy rate: 3.2% in 2011 (vs. 1.7% on average in France)

2012 outlook: High level of bankruptcies, and a further 3.5% increase

## Fragility of French small business network

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# Conclusion

- **The historically established correlation between construction and growth encourages recovery policies that focus on construction to exit the crises.**
- **These policies are hard to implement given the levels of private and public debt. They can prove costly in the short and medium term, despite the visible effect on employment.**
- **Given debt and costs factors, and a lack of economic growth, construction must go back to basics, or seek new growth areas.**
- **Against this backdrop, the sector will continue to face serious difficulties in 2012 and 2013, and company profitability will continue to decline.**



# Thank you.

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