Atradius
Managing risk, enabling trade

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market monitor

Focus on construction sector performance and outlook

Disclaimer

In this issue...

On the following pages we indicate the general outlook for each sector featured using these symbols:

Elevated credit risk remains

There are certain issues and patterns that construction industries have in common in any country, regardless of their performance in individual markets: n high level of competition, low profit margins, the fact that public buyers generally pay late and that there is a higher than average proportion of business failures. Long payment duration and cash flow problems/weak financials of smaller construction players are an issue in almost every market. After the major shake-up of the global construction industry caused by the 2008 financial crisis a return to economic normalcy has become visible, however, the rebound in some countries like Belgium, France, Italy and Spain remains modest compared to pre-crisis levels, as the decline in building activity during the recession was very steep. The recent sudden failure of a major British construction company highlights again the elevated credit risk level for businesses in the construction industry, where thousands of smaller businesses are typically at the back of the queue for payment.

Belgium

- The rebound is set to continue
- Bank financing remains an issue
- Stable outlook for payment delays and insolvencies

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months		✔			
Development of non-payments over the coming 6 months			✔		
Trend in insolvencies over the last 6 months				✔	
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance		✔			
Overall indebtedness of the sector		✔			
Willingness of banks to provide credit to this sector				✔	
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months		✔			
General demand situation (sales)		✔			

Source: Atradius

In 2017 the Belgian construction sector continued its rebound after bottoming out in 2013. The value added growth rate was 3.1% in 2017 and growth of 1.3% is expected in 2018. Working volumes continue to show a positive trend, and the industry has also benefitted from the comprehensive rebound of the Dutch construction market.

Residential construction is expected to benefit from low interest rates and increased demand in anticipation of E40 (S31) energy-efficiency requirements. Current building activities shows a clear preference for flats/apartments over single-family houses, due to scarcity of space, demographic development and investors' focus. The Flemish regional government is currently revising the registration tariffs for existing houses, which could result in procrastination in the renovation of larger houses.

Commercial construction activity is expected to increase along with the improved economic environment. Public construction-related businesses had difficult times over the past few years, but since 2017 this segment has recorded increasing orders, benefitting from increased infrastructure work in the run-up to the October 2018 municipal elections. While another decrease in public construction activity in 2019 cannot be ruled out, there is some hope that Aquafin and other utility companies will maintain a high investment level. The large infrastructure work in relation to the Oosterweel link (a construction project intended to complete the Antwerp Ring Road) should help to sustain infrastructure construction activity.

Construction businesses profit margins remain low, but have improved somewhat in 2017, and further improvement is expected in 2018. Currently it seems that due to the rebound larger construction companies have less leverage than in the past to play off smaller subcontractors on price, pass on price pressure and/or impose longer payment terms on them as a cheap source of financing. This is currently an issue for larger businesses that

Belgium: construction sector

	2017	2018f	2019f
GDP growth (%)	1.7	1.6	1.5
Sector value added growth (%)	3.1	1.3	1.4

Sector share in the national economy (%)	5.1
Average sector growth over the past 3 years (%)	3.3
Average sector growth over the past 5 years (%)	1.9
Degree of export orientation	very low
Degree of competition	very high

Sources: Macrobond, Oxford Economics, Atradius

negotiated their current order portfolios in more difficult times (and consequently for a lower price).

The overall indebtedness in the sector and dependence on external financing remain high, while banks remain rather unwilling to provide credit to construction businesses. Working capital needs of companies are very high, as advanced payments are not common in Belgium, while the administration (approval of works) and payments by the Belgian government are very slow. In general, payment terms tend to be long in the sector, i.e. "60 days end of month" is very common.

Payment experience has been bad over the past two years, however the number of non-payment notifications in the sector, while remaining high compared to other industries, has decreased in 2017 and is expected to remain stable in 2018. Construction insolvencies increased by more than 10% in 2017 (a 7.6% increase for all Belgian businesses). However, this major increase was also largely due to changes in the legal system, especially in the Brussels Capital region. In 2018 construction insolvencies are expected to level off.

Our current underwriting stance on the construction industry is neutral (e.g. not overly cautious or overly open) for all subsectors. In order to sustain our risk appetite, it is necessary to identify the most affected companies/subsectors and to contact buyers for up-to-date financial information and performance outlooks. Given the improvements in business performance and credit risk seen in 2017 and the stable outlook for 2018. we have upgraded the trade sector performance rating from "Poor" to Fair".

Belgian construction sector

Strengths	Demographic evolution
	Aged real estate stock, coupled with insufficient infrastructure investments in the past
	Low interest rates
Weaknesses	Price sensitive public tendering
	Cyclical trend in public spending and long time between tender and actual execution of public works
	High labour costs and availability of skilled workers

Source: Atradius

France

- Growth expected to slow in 2018
- Insolvencies have decreased, but remain on a high level
- Smaller players still face financing issues

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months			✔		
Development of non-payments over the coming 6 months			✔		
Trend in insolvencies over the last 6 months		✔			
Development of insolvencies over the coming 6 months		✔			
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance		✔			
Overall indebtedness of the sector		✔			
Willingness of banks to provide credit to this sector				✔	
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months			✔		
General demand situation (sales)		✔			

Source: Atradius

The rebound of the French construction sector observed in 2016 accelerated last year as, according to the French Builders Association FFB (Fédération Française du Bâtiment), in 2017 French construction activity grew 4.7% in volume, after a 1.9% rise in 2016. Growth was driven by new residential construction activity: in September 2017 new housing starts amounted to 414,000 units over the previous 12 months, compared to 380,000 in December 2016. This surge was mainly spurred by tax exemptions aimed at fostering real estate investment and supporting first-time buyers.

In 2018 construction activity growth is forecast to slow down to 2.4%, as the effect of tax exemptions will expire. At the same time rising real estate prices will affect household purchasing power, despite low interest rates. Renovation activity is expected to remain stable while public construction activity will remain low due to public budget spending constraints. That said, French construction contractors are currently more optimistic than in the past as revenues are growing, employment is picking up, backlogs are recovering and the production capacity utilization rate remains over its long-term average.

Despite the ongoing recovery, construction still suffers from fierce competition, with prices and profitability remaining at a low level. Margins of many businesses have not yet benefited from the recovery, while major players keep putting pressure on their subcontractors. Despite the current upturn, banks still remain very selective with their loans to construction businesses, making access to short-term credit difficult. Due to the ongoing difficulties in accessing short-term credit facilities - in a recovery period where buyers have to finance their growth - cash management remains a major issue for many, mainly smaller, construction businesses.

France: construction sector

	2017	2018f	2019f
GDP growth (%)	1.8	1.9	1.7
Sector value added growth (%)	1.6	1.8	1.8

Sector share in the national economy (%)	4.5
Average sector growth over the past 3 years (%)	-0.1
Average sector growth over the past 5 years (%)	-1.5
Degree of export orientation	very low
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

After a decrease in 2016 non-payment notifications only levelled off in 2017, therefore remaining at a high level, and no substantial decrease is expected in 2018. At least construction insolvencies continued to decrease in 2017 (down 12% year-on-year in the period of January-September 2017). This positive trend is expected to continue in 2018, with business failures expected to decline by about 7%. However, compared to other industries the share of construction insolvencies and protracted payments is expected to remain high.

Despite the current recovery we remain cautious in our underwriting stance, but we continue to provide cover to our customers whenever it is reasonable and prudent to do so. We closely monitor and review buyers to anticipate potential risks to our customers.

We continue to scrutinise the public construction subsector due to weak demand and very high regional disparities. Despite a modest recovery in 2017 and a stable performance outlook in 2018 we continue to pay attention to the furnishing segment (insulation, plastering, joinery installation, plumbing, roof covering).

We also closely monitor the construction materials wholesaler business, which suffered in 2017 as customers took advantage of fierce competition in this segment by putting pressure on sales prices.

We focus on the cash situation and loan facilities available to buyers, especially smaller and mid-sized companies. Several key financial indicators must be analysed: the level of activity, margins and ability to fund working capital requirements. High financial costs are a key indicator of potential pressure on cash. We also try to assess the ability of construction businesses to manage bigger projects than usual, as we often notice that smaller enterprises cannot cope with financial distress due to insufficient pricing and allocation of resources.

French construction sector

Strengths	Structural lack of housing due to demographic developments (growing population)
	Low interest rates
	Government support through tax emptions
Weaknesses	Feeble economic growth and measures taken to curb the high public deficit
	High unemployment
	Costs rising faster than prices

Source: Atradius

Italy

- **Low spending capacity and tight credit conditions**
- **A modest rebound is underway**
- **High insolvency level remains**

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months			✔		
Development of non-payments over the coming 6 months			✔		
Trend in insolvencies over the last 6 months			✔		
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance	✔				
Overall indebtedness of the sector	✔				
Willingness of banks to provide credit to this sector				✔	
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months			✔		
General demand situation (sales)			✔		

Source: Atradius

While Italy´s construction sector continued to grow in 2017 the industry is still far away from a real rebound, as construction investments in Italy shrank by more than 35% between 2007 and 2016. According to the Italian construction association ANCE, construction investment increased just 0.2% in 2017, driven by restorations (up 0.5%) and non-residential building activity (up 0.6%), while the new residential building segment continued to contract (down 1.5%).

In 2018, the modest recovery in construction investment is expected to continue improving 1.5%, with positive growth anticipated across all subsectors (investments in new houses and restorations up 1%, commercial constructions up 0.7% and growth in public construction up 4%). According to the Italian government EUR 100 billion is earmarked for public construction spending over the next 15 years, and an additional EUR 3.3 billion is earmarked for rebuilding activities in certain regions affected by earthquakes.

Next to the still low spending capacity, tight lending conditions set by banks remain the main reason for the still subdued performance of construction, exacerbating the fact that many Italian construction businesses remain highly geared. New loans for construction businesses decreased 68% in value between 2007 and 2016, but in 2017 some signs of stabilization were seen.

Loans granted to local municipalities have sharply deteriorated (EUR 651 million in 2016 compared to EUR 6.3 billion in 2000). Therefore it comes as no surprise that late payments from public bodies have also contributed to market difficulties. According to ANCE, in H1 of 2017 about 70% of the construction companies recorded late payments from public entities (paying after 156 days on average, compared to 60 days required by EU laws). At least it can be said that average payment delays have shown an improving trend in recent years, down from 160 days in 2013 and 112 days in 2016 to 96 days in H1 of 2017.

Italy: construction sector

	2017	2018f	2019f
GDP growth (%)	1.6	1.4	1.1
Sector value added growth (%)	2.0	2.5	2.2

Sector share in the national economy (%)	4.1
Average sector growth over the past 3 years (%)	0.3
Average sector growth over the past 5 years (%)	-2.0
Degree of export orientation	very low
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

While the profitability of many Italian construction businesses remains low, at least no deterioration is expected in 2018. Non-payment notifications remain at a high level in 2018, but no major increase is expected. The same accounts for construction insolvencies, which remain at an elevated level.

Given the on-going issues our underwriting stance remains restrictive, especially for small and medium-sized construction businesses as well as cooperatives and consortiums focused on residential construction and/or dependent on public construction (new buildings shrank by more than 63% between 2008 and 2016). The only exceptions are businesses active in renovation work supported by government incentives (up 20% between 2008 and 2016).

While larger, more export oriented construction players have proved to be more resilient so far, we have recently taken a more prudent underwriting approach on businesses with substantial business in countries with elevated economic and political risk (such as Algeria and Venezuela).

Italian construction sector

Strengths	Larger players benefit from export demand
Weaknesses	Still weak domestic demand
	Restrictive bank lending
	Smaller businesses lack financial resilience

Source: Atradius

United Kingdom

- **The recent failure of a major contractor will have a major knock-on effect**
- **Insolvencies are expected to increase by about 4%-5% in 2018**
- **Brexit will have an impact on construction performance**

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months				✔	
Development of non-payments over the coming 6 months				✔	
Trend in insolvencies over the last 6 months			✔		
Development of insolvencies over the coming 6 months				✔	
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance		✔			
Overall indebtedness of the sector		✔			
Willingness of banks to provide credit to this sector				✔	
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months		✔			
General demand situation (sales)			✔		

Source: Atradius

According to the Office of National Statistics (ONS) construction performance weakened towards the end of 2017, as output in the period September to November 2017 decreased 2.1% compared to the period June to August 2017. Previous decreases in new orders, particularly in the commercial and public non-housing segments, now appear to be filtering through into lower volumes of work.

In 2018 the residential construction sector is expected to grow, as the government announced an additional housing stimulus package worth GBP 15.3 billion over the next five years, bringing total support for housing to at least GBP 44 billion over this period. Public spending on infrastructure is expected to expand, and some big projects such as Crossrail 2, Thameslink, HS2 and Hinkley Point should ensure improved performance in 2018. That said, the outlook for commercial construction remains more muted, as uncertainty over the outcome of Brexit negotiations has a dampening effect on British businesses investments.

Legacy contracts have been a serious issue for the construction industry over the past 3-4 years, as many businesses pursued an aggressive accounting strategy by sealed risky contracts which proved unprofitable. Problems have been exacerbated by rising raw materials and labour costs. In 2017 four out of the top 10 construction companies in the UK issued profit warnings, and in January 2018 Carillion, the 2nd largest construction company in the UK and one of the government's biggest contractors, filed for voluntary liquidation, struggling under GBP 1.5 billion of debt including a pension shortfall of GBP 587 million.

The subsequent knock-on effect is expected to be huge, as it is anticipated that between 25,000 and 30,000 suppliers and subcontractors are owed around GBP 2 billion. This will surely cause substantial financial distress for thousands of suppliers along the value chain.

United Kingdom: construction sector

	2017	2018f	2019f
GDP growth (%)	1.5	1.5	1.6
Sector value added growth (%)	1.4	0.9	1.5

Sector share in the national economy (%)	4.9
Average sector growth over the past 3 years (%)	2.7
Average sector growth over the past 5 years (%)	0.9
Degree of export orientation	low
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Average payment in the British construction industry is 75 days, and the level of protracted payments and payment delays remains high. After increasing in 2017, the level of non-payment notifications is expected to increase further in H1 of 2018, additionally fuelled by the Carillion liquidation. For many smaller construction businesses problems further up the supply chain regarding delays in payments will only intensify the issues they already have and drain them of their “lifeblood” of cash, which could have serious repercussions on their performance. With the problems experienced by tier one contractors in 2017 and the Carillion liquidation, access to bank finance remains difficult, especially for smaller construction businesses and companies in sectors such as support services, particularly those with feeble balance sheets.

Due to all this and a general concern over the overall state of the UK economy the level of insolvencies in the construction sector will remain high and is expected to increase further in 2018, by about 4%-5% year-on-year.

Beside the current market shake-up caused by the Carillion liquidation the Brexit issue will undoubtedly have an impact on the construction market, as the industry is very susceptible to shifts in investor confidence. If the coming months fail to deliver greater clarity about the conditions under which the UK will leave the EU, the commercial and infrastructure segments in particular could struggle.

As more than 60% of building materials are imported from the EU, any increase in tariffs or limits on quantities imported after leaving the EU could lead to higher costs for British construction businesses and a shortage of building materials. Once the UK leaves the Single Market it is likely that the current issue of skill shortage will worsen, especially if there are no follow-up agreements with the EU on the free movement of people. This could result in even higher pressure on wages, causing construction firms to face considerably higher project costs. Additionally it could reduce the capacity of the industry to deliver new houses to meet the government’s housing targets, and therefore further deepen the current housing shortage, especially in London.

Currently the UK construction sector still benefits from having access to the European Investment Bank (EIB) and the European Investment Fund (EIF), which have invested EUR 7.8 billion in major infrastructure projects in the UK and provided loans worth more than EUR 500 million to smaller British construction businesses. A loss of that financial support could significantly impact the ability of businesses to deliver big infrastructure projects such as High Speed 2 and reduce development opportunities for start-ups.

We continue to underwrite cautiously, with risks considered on a case-by-case basis, while the failure of Carillion has increased vigilance. Even more than in the past the need for up to date regular financial information supported by visits, meetings and conference calls is essential to be able to provide the most informed underwriting decision. The speed at which seemingly good performing construction businesses can deteriorate requires extra scrutiny on order books, margins and contract details.

British construction sector

Strengths	Housebuilding is set to grow further
	Larger projects Crossrail, Thameslink, HS2 and Hinckley Point to help sustain volumes during the year
	Increased spend in the regeneration of major cities such as Birmingham and Manchester
Weaknesses	Looming uncertainty due to the Brexit decision
	High level of payment delays, risk of further increase in insolvencies
	Legacy issues still remain in contracting businesses. Also lack of funding affecting businesses that may need to resume investment
	Knock-on effect of the Carillion collapse

Source: Atradius

Market performance snapshots

Romania

- **Insolvencies increased in 2017**
- **Subdued investment in infrastructure works**
- **Access to bank loans remains restricted**

The volume of construction work decreased 10.3% year-on-year between January and October 2017 – a decline mainly caused by poor financing of infrastructure works. At the same time growth of private investments in the residential and commercial sector (retail and offices) has continued to support activity in the industry, which is expected to record 2.2% value added growth in 2018.

Investment in public construction is still insufficient given the overall market potential, mainly hampered by underfunding of local infrastructure. This also constrains a potential surge in commercial construction activities, while residential construction remains positive, partly compensating the reduction in engineering and non-residential work. In the construction materials subsector many companies generate only small profit margins while there is a need to provide high quality products and services in order to expand the business.

Due to the current lack of government investments/projects competition has become fiercer. However, a number of construction companies that typically focus on public projects are offsetting the reduction with residential and commercial projects.

Many construction businesses are heavily indebteded., The main financing sources are suppliers and banks. However, banks are rather cautious in providing loans to the industry due to the large number of insolvencies and generally volatile market demand situation.

Payment duration in the industry is 90-120 days, on average, and the level of protracted payments remains high. As construction projects usually take an extended amount of time to be completed, buyers rely heavily on protracted payments, which is increasing the risk in the value chain. At the same time public bodies are paying slower than private companies.

In H1 of 2017 construction insolvencies increased 6% year-on-year, accounting for 17% of all business failures in Romania. It is expected that there will be no major construction insolvency increase in 2018, however this depends on a stable economic environment with no major decrease in government investments.

Due to high risk and elevated insolvency numbers our underwriting stance remains restrictive for all construction subsectors. For larger requests we require constantly updated financial information and payment experience. In the public construction segment the state is generally slow to pay for completed work, which is putting pressure on the liquidity of related buyers. Therefore we take extra care reviewing the financing conditions of public projects.

Spain

- The rebound continues, but long payment terms remain an issue
- Insolvencies expected to decrease by more than 5%
- Still low activity in the public segment

The Spanish construction sector continued its rebound, that started in 2015, with an estimated value added growth rate of 4.2% in 2017, mainly due to Spain´s economic recovery and increased foreign investments. However, it must be said that the current construction recovery comes from a very low level following years of severe recession, as domestic production had decreased by more than 50% in the period 2007-2014.

In 2018 value added construction growth is expected to increase again by about 2.5%-3%, mainly driven by residential and commercial construction, while growth in the public construction/civil engineering segment is expected to be subdued.

Competition in the industry has dropped off significantly, as a large number of players have left the market since 2008 and there is a high degree of specialisation among the remaining players. Profit margins have increased in 2017 and are expected to improve further in H1 of 2018. However, the profit and loss accounts of businesses active in energy-intensive subsectors (e.g. cement and ceramics) are negatively affected by elevated electricity and gas costs.

Spanish construction businesses are highly dependent on bank funding and other sources of external financing. In this respect, conditions for external financing have continued to improve in 2017 due to the robust performance of the Spanish economy. However high leverage still remains a serius issue for many Spanish costruction businesses.

The contruction sector maintains a record of frequent and long payment delays. Despite the fact that the average payment period has improved in recent years, it continues to be high, at 93 days on average. Late payment of mainly larger players continues to negatively affect the working capital management of many smaller players. It is expected that construction payment delays will level off in H1 of 2018.

Construction insolvencies have shown annual decreases since 2014, as the remaining businesses are more resilient. It is expected that construction insolvencies will decrease further in 2018, by 5%-9% year-on-year, due to the satisfying growth outlook and the lower indebtedness of many businesses.

Due to the ongoing rebound, our underwriting stance for the construction sector has become less restrictive than in previous years, with an open stance for larger businesses and international groups. However, we are still prudent with smaller businesses as the market has not yet fully consolidated, many companies are still highly indebted and lending conditions have not yet fully eased. We are also more cautious when underwriting businesses dependent on the public construction sector, as the activity level in civil works remain low due to constrained spending by the Spanish government (fiscal consolidation in order to reduce the public deficit).

United States

- **The robust performance is set to continue in 2018**
- **The outlook for infrastructure investment growth remains uncertain**
- **Payments take 38 days on average**

In 2017 the US construction industry continued to expand, with a value added sector growth rate of 2.3%. It is estimated that private residential construction spending increased more than 7% and non-residential construction about 4%, while public construction spending decreased 4%-6%.

US construction expansion is set to continue in 2018, underpinned by robust economic growth, with building businesses profit margins expected to remain stable, as price increases are offset by higher costs. Construction starts are expected to increase about 5% in 2018 with commercial construction forecast to pave the way with a double digit growth rate. Construction spending is expected to increase 7%, mainly due to a surge in the private residential segment.

However, despite repeated announcements by the US administration that it will invest in infrastructure improvements, a public construction spending increase remains uncertain, as political gridlock and shifting priorities have so far stifled promises to boost infrastructure spending. At the same time a combination of rising prices and higher interest rates (the Federal Reserve tightened its monetary policy in December 2017, and additional interest rate hikes are expected in 2018) may dampen the housing market in 2018, particularly in the first time home buyers segment, which has been expanding since 2011.

Both construction businesses leverage and dependence on bank financing are generally high. Companies that show consistent profitability, healthy balance sheets and prompt payment trends are generally able to obtain lines of credit, while viable and promising projects continue to be attractive to lenders in the growing market. However, the volatile nature of the construction sector continues to bottleneck financing options for companies with liquidity issues.

Payments in the US construction industry take 38 days on average, while 60 day and even 90 day terms are not uncommon. Over the last two years, payment experience in the construction sector has been decent, and the overall number of late payment notifications received in 2017 increased only slightly compared to 2016. No insolvency increase is expected in 2018.

Due to several years of stable growth we have continued to increase our risk appetite for the industry throughout all major segments (residential, commercial, public construction and construction materials). However, caution is advised with smaller construction businesses, which still show higher bankruptcy rates than their peers in other industries.

When available, financial statements are to be reviewed annually with supplemental soft credit information reviewed more frequently. Trading experience will be used to gain a better comfort level in gauging the relationship between our customers and their buyers. Reduction or withdrawal of cover is considered if the buyer shows significantly worsening results, including losses, heavy debt levels, problems with working capital, cash flow, liquidity or deteriorating payment trends.

Market performance at a glance

Australia

- Construction is a significant contributor to the Australian economy, accounting for approximately 9% of GDP. 2017 is expected to be the final year of contraction in non-residential and engineering construction before modest growth returns in 2018.
- While mining-related activity could decline further this year, the prospects for growth in other parts of engineering and non-residential construction are improving and expected to outweigh any further contraction in mining related work. Engineering construction output – particularly infrastructure-related projects for road and rail, largely located on the east coast – is forecast to increase about 3.5% in 2018.
- Residential construction growth is expected to level off or slightly contract in 2018, as lenders are tightening terms and conditions for borrowers, particularly investors. An increase in the number of apartments and decrease in Chinese buyers is also playing a part in the slow price growth.
- The “two speed economy” is supported by the differences in performance and outlook of the construction market in the various Australian regions. Queensland, Western Australia and the Northern territory are all considered to be so-called “mining states” and are forecast to account for about AUD 7 billion decrease in construction activity in 2018. On the other hand, the South Eastern regions are forecast to maintain the present levels of activities.
- Payments in the construction sector take 30-60 days on average, and the level of non-payment notifications remains high. The number of credit insurance claims is expected to remain elevated in 2018.
- Our underwriting approach remains cautious, particularly for small businesses, the mining-related segment and the Western Australia and Queensland markets generally. Overall, construction sector performance still needs to be closely monitored given its volatility.

Hungary

- The demand situation in the Hungarian construction sector remains good, with 3.4% value added growth in 2017 and a 110% year-on-year increase of in orders received by the end of 2017.
- Profit margins of construction businesses are low, mainly due to substantial competition in the market and contracts being made at low price levels.While margins have increased in 2017 a decrease is expected in 2018 due to rising raw material prices and higher labour costs.
- Both gearing and dependence on bank financing are high in the Hungarian construction industry. Many smaller businesses are undercapitalized and require external financing, but only a small share of them are really creditworthy. Although banks have increased their willingness to provide loans since 2016, lending conditions remain tight. While interest rates of residential property loans have declined, banks still prefer office space projects to residential ones.
- Payments in the construction industry take 60-120 days on average and the payment behaviour has been rather bad over the past two years, with a high level of protracted payments. Non-payment notifications increased in 2017, and further increases are expected in 2018, as many small businesses show weak financials and struggle with low contractual prices and increasing labour costs.
- The number of insolvencies is very high compared to other Hungarian industries and many small companies active in the construction sector have a very short lifespan. Smaller players often lack the ability to make efficiency-enhancing investments necessary to survive in the market. It is expected that construction insolvencies will increase by 5%-10% in 2018.
- Despite the sector’s positive performance in 2017 and turnover growth estimated at 10% in 2018 our underwriting approach remains generally restrictive, as many small and undercapitalized businesses are active in the market.
- In the residential construction segment property price inflation and increasing operating expenses pose a risk, while uncertainty about a potential VAT increase on housing construction (from 5% to 27% as of 2019) remains. However, we are less restrictive in the public construction segment. After a low level in 2016, public procurement tenders partly funded by the EU (road, railroad, civil engineering) have recently surged again.

Mexico

- 2017 was a difficult year for the Mexican construction industry as the public construction segment suffered from low investment, while private investment in residential and commercial construction remained stable at least. Overall construction output value contracted 3.8% year-on-year in Q3 of 2017. A the same time the construction materials segment has been negatively impacted by increased price volatility (mainly steel and cement).
- The outlook for 2018 remains subdued and the (already low) profit margins of many construction businesses are expected to deteriorate further in H1of 2018, mainly due to ongoing low building investment by the government and lower market activity ahead of the July 2018 presidential and general elections. Additionally, uncertainty over the outcome of the ongoing NAFTA renegotiations has an impact on building investments in Mexico.
- In general banks are not restrictive in providing loans to the construction sector. However, the currently high interest rates are an issue for lenders.
- On average, payments in the construction industry take 45-120 days. It is common for buyers in this sector to pay slowly, especially in the public infrastructure segment. Due to the subdued demand situation it is expected that non-payment notifications will increase in 2018.
- While keeping a neutral underwriting stance for businesses active in the residential and commercial construction segments, we are restrictive on public construction and construction materials.

Poland

- Construction turnover increased in 2017 compared to 2016, and value added growth rose 4.7%. In 2018 2.9% a growth rate is expected. However, the average annual margin in the industry decreased from 28,6% in 2016 to 26,8% in 2017. It is expected that businesses margins will decrease further in the coming months due to a significant price increase for subcontractors, transport and construction materials.
- While competition in the Polish construction market remains high, due to high demand no price wars were observed in 2017. The average revenue-weighted debt ratio in the industry was 78% in 2017, while the level of debt in the construction materials segment is much lower. The willingness of banks to lend to the construction industry is at the same level as with other Polish industries. The risk that funding costs adversely affect businesses financial condition or operational results is limited.
- Payment duration in the industry is 60-90 days on average (in some cases up to 120 days), and the level of non-payment notifications is high, with no major decrease expected in 2018. In 2018 it is expected that construction insolvencies will increase by more than 10%, as the construction market has expanded and the number of active businesses is growing.
- Our current underwriting approach is neutral to restrictive. While the market is still growing, especially in the infrastructure segment, increasing costs (construction materials, transport, price increase for specialist work) weigh on the performance of construction businesses.

Singapore

- Singapore's construction sector value added shrunk in 2017 (down 6.1%) due to a subdued performance in private construction, steming from continued lower demand, less favourable economic conditions and bigger supply of already completed private housing projects and offices. SME contractors continue to suffer from tight cash flow and deteriorating margins due to a lack of projects, increasing competition, and higher labour and rental costs.
- Public construction accounted for about 70% of building activity in 2017 (60% in 2016), following the government's higher spending on infrastructure and civil engineering contracts (worth between SGD 20 billion and SGD 24 billion, up from SGD 15.9 billion in 2016). In order to support the industry and give a boost to troubled smaller contractors the government announced it will spend SGD 1.4 billion over the next two years to upgrade walkways and renovate community centres, sports halls, police stations, etc.
- Singapore´s construction businesses are heavily reliant on banks for loans and project funding. Despite a more difficult outlook for the Singaporean banking sector as a result of lower growth in China and a less favourable domestic economic outlook, bank lending remains non-restrictive to the construction sector for the time being.
- Payment duration in the industry is 60-120 days on average. Payment morality slowly deteriorated in 2017, and this negative trend is expected to continue in H1 of 2018. According to the Singapore Commercial Credit Bureau (SCCB) construction is the only sector that registered a year-on-year rise in the number of slow payments (up from 50.82% in Q3 of 2016 to 53.3% in Q3 of 2017).
- The protracted default rate in the construction industry remains high. At least the number of businesses under liquidation has decreased year-on-year by about 15%, as banks are more prone to accept restructuring options as opposed to resorting to liquidation.
- In 2018 the decline is expected to ease on the back of continuous public investment in the sector. While our underwriting stance is generally open for businesses related to public sector construction we are more cautious about the private building segment and SME contractors in general.

Thailand

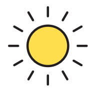
- Construction accounts for about 8% of Thailand´s GDP, with the public sector accounting for about 60% of activity. There are about 80,000 construction companies registered in Thailand, of which 1% qualify as large-scale operators, holding 75% of market share. The sector is expected to have high growth rates over the next five years, mainly due to large infrastructure projects driven by the government.
- Due to lower construction material prices (e.g. low steel prices caused by oversupply from China) businesses profit margins have improved in 2017. However, as China is reducing its steel production steel prices are expected to increase again in the coming years. Higher input prices could pose a risk for smaller players, which are more exposed to construction work demand volatility and price-cutting by large operators, affecting their payment capability.
- Payment duration in the industry is 90-120 days on average, depending on the size of individual projects. Payment experience has been average over the past two years, with a slight increase in non-payment notifications in 2017, mainly caused by smaller players.
- Our underwriting stance is generally open for commercial construction (due to a strengthening economy) and public construction (due to high demand and progress of government-sponsored mega-projects). However, our underwriting is more restrictive for businesses active in residential construction, as there are indications of oversupply in the low-to-medium price residential building segment.
- In all subsectors we are more selective with small and medium-sized construction businesses, as many of them are highly geared and dependent on bank financing, while financing conditions like covenants are quite tight for them. The assets of smaller players are often limited, which hampers their ability to undertake larger projects.

Industries performance forecast per country

February 2017

	Agriculture	Automotive/ Transport	Chemicals/ Pharma	Construction Const.Mtrls	Consumer Durables	Electronics/ ICT	Financial Services
Austria	⛅	🌧	⛅	⛈	☁	☁	☀
Belgium	☁	⛅	☀	☁	☁	⛅	☁
Czech Rep.	⛅	⛅	⛅	🌧	☁	☁	⛅
Denmark	⛈	☁	⛅	☁	🌧	☁	☁
France	🌧	☁	☀	🌧	☁	☁	⛅
Germany	☁	☁	☀	☁	☁	☁	⛅
Hungary	☁	☁	⛅	☁	☁	☁	☁
Ireland	☁	☁	⛅	☁	☁	☁	⛅
Italy	⛅	⛅	⛅	🌧	⛅	⛅	⛅
The Netherlands	⛅	☁	☀	⛅	☁	⛅	⛅
Poland	☁	🌧	☁	🌧	🌧	🌧	⛅
Portugal	☁	☁	🌧	🌧	☁	☁	🌧
Russia	🌧	☁	🌧	🌧	☁	🌧	☁
Slovakia	☁	⛅	⛅	🌧	☁	☁	⛅
Spain	☁	⛅	⛅	🌧	☁	☁	☁
Sweden	⛅	☁	⛅	☁	⛅	⛅	⛅
Switzerland	⛅	☁	⛅	🌧	☁	☁	☀
Turkey	⛅	⛅	☁	🌧	☁	🌧	⛅
UK	⛅	☁	⛅	🌧	☁	☁	☁
Brazil	☁	🌧	☁	🌧	⛈	⛈	⛅
Canada	☀	☁	☁	☁	☁	☁	☀
Mexico	☁	⛅	☁	🌧	☁	☁	⛅
USA	☁	⛅	⛅	☁	☁	⛅	⛅
Australia	⛅	🌧	☁	🌧	☁	⛅	⛅
China	☀	☁	☁	🌧	☁	☁	☀
Hong Kong	N/A	☁	☁	☁	☁	⛅	⛅
India	☁	☁	⛅	🌧	☁	☁	☁
Indonesia	☁	☁	☁	☁	☁	☁	⛅
Japan	⛅	☁	☁	☁	☁	⛅	⛅
New Zealand	⛅	🌧	⛅	⛅	🌧	⛅	⛅
Singapore	⛅	🌧	☁	🌧	☁	☁	⛅
Taiwan	N/A	🌧	☁	☁	⛅	⛅	☁
Thailand	☁	⛅	☁	☁	☁	☁	☁
United Arab Emirates	⛅	☁	☁	🌧	🌧	🌧	☁

Food	Machines/ Engineering	Metals	Paper	Services	Steel	Textiles
Good	Good	Fair	Fair	Good	Poor	Poor
Good	Good	Fair	Poor	Poor	Good	Poor
Good	Fair	Fair	Fair	Fair	Fair	Poor
Good	Fair	Fair	Bleak	Fair	Poor	Poor
Fair	Fair	Fair	Poor	Fair	Fair	Poor
Fair	Good	Fair	Poor	Good	Fair	Poor
Fair	Good	Poor	Fair	Good	Poor	Poor
Good	Fair	Fair	Bleak	Fair	Fair	Poor
Good	Excellent	Fair	Fair	Fair	Fair	Poor
Excellent	Good	Good	Fair	Good	Fair	Fair
Fair	Poor	Fair	Fair	Good	Fair	Fair
Fair	Fair	Poor	Fair	Good	Poor	Fair
Fair	Bleak	Fair	Fair	Poor	Fair	Fair
Good	Good	Fair	Fair	Fair	Fair	Poor
Good	Fair	Poor	Poor	Good	Fair	Poor
Good	Good	Poor	Fair	Fair	Poor	Poor
Good	Good	Fair	Fair	Good	Poor	Fair
Good	Fair	Bleak	Poor	Poor	Fair	Poor
Fair	Fair	Fair	Poor	Fair	Fair	Poor
Good	Poor	Poor	Fair	Fair	Poor	Poor
Good	Fair	Fair	Poor	Good	Fair	Bleak
Good	Fair	Poor	Good	Good	Poor	Poor
Good	Fair	Fair	Poor	Good	Fair	Poor
Good	Fair	Poor	Poor	Fair	Poor	Poor
Good	Fair	Bleak	Poor	Good	Bleak	Poor
Excellent	Fair	Poor	Fair	Good	Poor	Fair
Good	Fair	Poor	Good	Good	Poor	Fair
Good	Fair	Poor	Fair	Fair	Poor	Fair
Good	Fair	Fair	Fair	Good	Fair	Poor
Fair	Fair	Fair	Poor	Poor	Poor	Poor
Good	Fair	Fair	Fair	Good	Poor	Fair
Excellent	Fair	Poor	Fair	Good	Poor	Fair
Good	Fair	Fair	Fair	Fair	Poor	Bleak
Poor	Fair	Poor	Fair	Good	Poor	Poor


Excellent


Good


Fair


Poor


Bleak

Industry performance

Changes since December 2017

Europe

Belgium

Construction/Construction Materials

Up from Poor to Fair

See article on page 5

Czech Republic

Automotive/Transport

Down from Excellent to Good

The market is saturated, together with higher labour costs and declining margins. Recently established small companies have become more vulnerable to default, while currency appreciation has reduced exporters´ price competitiveness.

The Americas

United States

Metals

Up from Poor to Fair

Steel

Up from Poor to Fair

The production rebound in the Oil Country Tubular Goods (OCTG) segment, a continued stable performance in the automotive sector and improved conditions in construction (especially in residential construction), have supported steel and metal sector performance.

Asia/Oceania

Indonesia

Automotive/Transport

Up from Poor to Fair

In 2018 car sales are expected to increase to about 1.1 million units. Commercial vehicle sales will benefit from a recovery in the mining industry and the increase in infrastructure projects. Robust economic growth supports passenger car sales.

Financial Services

Up from Fair to Good

Indonesian banks are in general well-regulated and capitalised, having sufficient liquidity to serve the higher credit demand as economic growth picks up. The Indonesian banking industry adheres to the Basel III standard as a whole.

Thailand

Automotive/Transport

Up from Fair to Good

In 2018 and 2019 car exports are expected to increase 3%-5% year-on-year (to more than 1.2 million units per year). In the transport segment the aviation subsector is set to grow further helped by increasing tourism, while the whole industry benefits from high public investment in infrastructure projects.

Consumer Durables

Up from Poor to Fair

The industry is expected to rebound in 2018 after a more difficult period in the past, mainly due to increasing exports. Despite the fact that consumers purchasing power is affected by a high debt per capita, the retail segment is expected to grow 4%-4.5% in 2018.

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