Atradius
Managing risk, enabling trade

February 2017

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:

Excellent Good Fair Poor Bleak

Challenges and opportunities

Construction remains a cyclical sector, i.e. the performance of building companies is strongly related to a country's economic growth and investors´ sentiment as well as business and consumer confidence. Therefore, it comes as no surprise that construction activity diverges significantly in many countries. However, even in markets where construction growth has been very robust in recent years the fact remains that competition is high, profit margins slim, public buyers generally pay late and the proportion of business failures remains higher than in most other industries. Those seem to be reoccurring issues in the construction industry, regardless of performance.

Despite its cyclical nature and 'traditional' issues, from a global perspective, there are new opportunities and challenges ahead. For example, technology increasingly has a tremendous impact on construction. The rapid emergence of augmented reality, drones, 3D printing, Building Information Modelling (BIM), autonomous equipment and advanced building materials –will profoundly change the sector in the future.

Additionally, demographic shifts have started to play a major role in construction. The population of the world's urban areas continues to increase, which will drive demand for housing as well as social transportation and utility infrastructure. At the same time, many societies particularly in the West, but also in Japan and China face aging populations, which will lead to changing real estate investment patterns.

Belgium

- **Business margins remain under pressure**
- **Slight increase in public construction investment**
- **Level of payment delays and insolvencies remains high**

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 Belgian construction sector is very fragmented, mainly consisting of small and medium-sized businesses. Subcontracting is very common, but subcontractors are generally more vulnerable than larger businesses, which tend to pass on the price pressure to the next level. Larger companies also benefit from higher margins in private-public co-operation projects and are increasingly looking for business opportunities abroad.

In 2016 the Belgian construction sector continued its slow rebound after bottoming out in 2013. The recovery is supported by increasing work volumes (larger order portfolios with a longer time horizon), triggered by low interest rates, tighter environmental regulations and insufficient infrastructure investments in the past. Due to the upcoming municipal elections in 2018, an increase in infrastructure works and/or works for utility companies is expected. However, due to budget constraints, this surge in public works will be less pronounced than in the past.

A full-scale rebound of the Belgian construction sector is hampered by the still difficult economic climate, with rather low annual GDP growth rates of around 1.5%, government budget constraints (with a very price-sensitive public tendering) and the fact that banks remain restrictive in providing loans to construction businesses. Additionally, Belgian construction businesses still suffer from high labour costs, especially when compared to construction businesses from Eastern Europe active in Belgium. As a result, margins and profits of many businesses remain under pressure.

Construction companies´ working capital needs 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. Quite often construction businesses are forced to accept

Belgium: construction sector

	2015	2016	2017f
GDP growth (%)	1.5	1.3	1.4
Sector value added growth (%)	-2.0	1.1	1.4

Sector share in the national economy (%)	4.9
Average sector growth over the past 3 years (%)	-1.3
Average sector growth over the past 5 years (%)	1.0
Degree of export orientation	very low
Degree of competition	very high

Sources: IHS, Atradius

unfavourable payment terms. Larger businesses tend to impose longer payment terms on their subcontractors as a cheap source of financing. As construction companies are regularly confronted with project delays, this has an adverse impact on profitability, not only because turnover is lower than expected, but also due to volatile raw material prices and unfavourable price index revision clauses.

Given all those constraints, it comes as no surprise that we observed an increase in payment delays in 2016. Due to the difficult market conditions, the number and amount of notifications of non-payment is expected to remain high. That said, we expect business failures to decrease further in 2017. However, the overall level of construction insolvencies remains high, given the steady increases seen in the years 2008-2013.

Our prudent underwriting stance should allow us to maintain our current level of engagement. 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. We are more restrictive in underwriting vulnerable segments such as erection of roof covering and frames, joinery installation, floor and wall covering, demolition and wrecking of buildings, earth moving, plumbing and civil engineering works.

Belgian construction sector

Strengths	Demographic evolution
	Aged real estate stock, need for infrastructure improvements (schools, hospitals, roads)
	Currently low interest rates
Weaknesses	Competition from foreign builders
	Low level of government investment
	High labour costs

Source: Atradius

France

- **Construction activity finally picked up in 2016**
- **Still a high level of payment delays**
- **Larger players put pressure on subcontractors**

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 has finally gained momentum. According to the French Builders Association FFB (Fédération Française du Bâtiment), in 2016 French construction activity grew 1.9% in volume, after eight years of decline. The recovery was mainly driven by new residential construction activity, which increased 7.4% in 2016. In 2017 construction activity is forecast to increase 3.4%, driven by higher residential and commercial construction output. The on-going recovery is helped by tax exemptions for real estate investors, financial support for first-time buyers and persistently low interest rates. That said, the rebound remains fragile for the time being, as household purchasing power remains constrained and activity in the public building segment remains low due to public budget spending constraints.

Given the poor construction performance and low demand in previous years, it comes as no surprise that French construction businesses still face many difficulties. Competition is still fierce and prices and profitability remain low, although profit margin levels are expected to stabilise in 2017 due to the increased demand. However, major players keep putting pressure on their subcontractors, and despite the current upturn, banks still remain very selective with their loans, making access to short-term credit difficult. Due to the on-going difficulties in accessing short-term credit facilities, cash management remains a major issue for many mainly smaller construction businesses.

While non-payments in the construction sector have decreased in 2016, the level of NNPs remains fairly high, and payment experience over the past two years has been rather bad. Insolvencies finally decreased in 2016 after several years of yearly increases, and this positive trend is expected to continue in 2017, in line with increasing building activity. However, compared to other French industries the share of construction insolvencies remains high.

France: construction sector

	2015	2016	2017f
GDP growth (%)	1.2	1.2	1.2
Sector value added growth (%)	-2.7	0.8	1.4

Sector share in the national economy (%)	4.8
Average sector growth over the past 3 years (%)	-1.7
Average sector growth over the past 5 years (%)	-1.2
Degree of export orientation	very low
Degree of competition	high

Sources: IHS, Atradius

Despite the current rebound 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 especially scrutinise construction businesses active in the public building subsector and the furnishing works segment (insulations works activities, plastering, joinery installation, plumbing, roof covering). Furnishing has suffered heavily during the downturn and still remains vulnerable despite the current increase of new housing, as furnishing work usually occur at the final stage of building activities.

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.

French construction sector

Strengths	Structural lack of housing due to demographic developments (growing population)
	Still low interest rates
Weaknesses	Feeble economic growth and measures to curb the high public deficit
	High unemployment
	Costs rising faster than prices

Source: Atradius

Germany

- Growth expected to accelerate in 2017
- Poor payment behaviour of public buyers remains an issue
- Interior work-related segments show higher vulnerability

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 2016 the German construction sector continued its solid performance. The outlook for 2017 remains positive, mainly driven by another surge in residential construction. According to the German Builders Association, turnover growth will increase 5% in 2017, to more than EUR 112 billion. Residential construction is expected to increase 7%, driven by a high employment rate, low interest rates and the need to provide new housing for the large number of refugees and asylum seekers. Public construction is expected to increase 5% due to increased investment in infrastructure, while commercial building output is forecast to grow 3%.

However, despite continued growth during the last ten years and the benign outlook, the level of building activity seen in the 1990s has not been reached again. The sector´s share in the national economy has decreased to about 3%, down from more than 6% in the mid-1990s.

Within the industry, 90% of companies are small businesses (less than 20 employees) accounting for 45% of total construction turnover. 45% of sector turnover is realised by companies with 20 to 100 employees, and the remaining 10% is generated by large companies with more than 100 employees. Small companies are mainly focused on residential construction (about 70% of operations), while large building companies generate most of their turnover abroad.

On average, payments in the German construction sector take around 45-50 days. After decreasing in 2015, instances of payment default remained stable in 2016, and this trend is expected to continue in H1of 2017. With demand increasing and profit margins improving, construction insolvencies have decreased in recent years (down 2% in 2016) and are expected to remain stable or show a modest decline in 2017. Construction businesses´

Germany: construction sector

	2015	2016	2017f
GDP growth (%)	1.7	1.9	1.3
Sector value added growth (%)	-0.7	4.3	3.8

Sector share in the national economy (%)	3.3
Average sector growth over the past 3 years (%)	0.5
Average sector growth over the past 5 years (%)	0.6
Degree of export orientation	low
Degree of competition	high

Sources: IHS, Atradius

dependence on bank finance is not overly high, given that payments in advance or instalment payments by investors are a major source of financing.

However, despite the generally benign situation, we still consider the construction sector to be riskier than other industries. The proportion of insolvencies in the construction sector is higher than in other German trade sectors. According to Creditreform, in 2016 there were 94 insolvencies per 10,000 firms in the construction industry, compared to 42 per 10,000 in the manufacturing sector overall. Construction insolvencies still account for about 16% of all business failures in Germany.

The poor payment behaviour of public buyers remains an issue, as it puts a strain on suppliers' liquidity. Many construction companies – especially smaller ones – traditionally have weak equity ratios (the proportion of equity used to finance a company's assets) and limited financial scope, which makes them vulnerable to payment delays and defaults.

We have observed higher claims in some segments related to interior work, such as building installation, plastering, painting and glazing. Such activities are usually due at the final stage of building projects, and are therefore more susceptible to budget constraints of the awarding authority. Another reason could be the lack of commercial skills in those mainly very small businesses.

Due to the good performance of the German construction and construction materials sector in the last couple of years and the promising business outlook for 2017, our underwriting stance for the industry remains quite relaxed. In general, when assessing buyer risk we take into account operating results, equity, liquidity and financing (e.g. the ratio of work in progress/advanced payments) and orders in hand.

However, we are more cautious with the above-mentioned interior work-related segments and businesses that are mainly active for public customers (road and railway and other infrastructure construction). Those often face delayed payments by their clients, which could put a strain on their liquidity. With less background information to work with, we are naturally very cautious when assessing the creditworthiness of construction/construction materials businesses that have operated for less than one year, unless they are part of, or a spin off from, a larger group.

German construction sector

Strengths	Solid performance since 2010 helped by a robust German economy
	Significant amount of specialisation, mainly in construction services
	Strong in technical innovations especially in the area of energy-efficiency
	In general, businesses are not heavily indebted
Weaknesses	Very large number of small companies
	Limited access to international capital markets
	Many smaller companies have weak equity ratios and limited financial scope

Source: Atradius

The Netherlands

- The rebound continues
- Margins remain under pressure
- Decreasing order books in the infrastructure segment

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 line with the overall Dutch economic performance the construction industry continued to grow in 2016, which also benefitted related segments like construction materials and engineering. The strong growth in the housing market provides an additional stimulus for private consumption.

In Q3 of 2016 construction was the fastest growing trade sector in the Netherlands, and turnover and gross added value have increased for the past eight quarters in a row. Home prices have further increased, and the sentiment of many construction companies remains positive, with businesses expecting further revenue increases in 2017.

In 2015 the recovery in the Dutch construction market was rather one-sided, driven mainly by growth in the residential construction segment, while the non-residential subsector, especially utility construction segments, still faced modest demand. Residential construction continued its increase in 2016 and is expected to grow further in 2017, although below 2008 pre-crisis levels. Meanwhile demand for non-residential construction picked up in 2016. Civil and utility construction have shown robust growth in 2016, and production even increased 13.4% year-on-year in Q3 of 2016. However, utility is a very diversified subsector, where developments in single regions also vary: demand for offices and hotels as well as brick-and-mortar shops is higher in Amsterdam than in less central communities. Despite the upturn, pressure on businesses' margins remains in this segment.

The infrastructure segment has also partly benefitted from improving market conditions and government spending in 2015 and 2016. However, infrastructure expansion has lost steam in H2 of 2016, with production decreasing 4.5% year-on-year in Q3. Roads, tunnels and railroad builders reported a 5.8% decline, and it seems that the infrastructure-related expansion has ended for the time being.

The Netherlands: construction sector

	2015	2016	2017f
GDP growth (%)	2.0	2.0	1.7
Sector value added growth (%)	9.8	2.7	2.4

Sector share in the national economy (%)	4.9
Average sector growth over the past 3 years (%)	3.0
Average sector growth over the past 5 years (%)	1.1
Degree of export orientation	very low
Degree of competition	very high

Sources: IHS, Atradius

After a steep increase during the crisis years, a decrease in non-payment notifications and credit insurance claims has been recorded since 2015, and it is expected that non-payments and insolvencies will further decrease in H1 of 2017. Compared to 2015 loan policies of banks towards construction companies eased last year. However, the on-going strong competition in the market indicates that many Dutch construction businesses remain affected by price wars, leading to on-going pressure on margins. There is still overcapacity in the market, and a consolidation has yet to take place.

Given the robust performance in 2016, decreased insolvencies and the positive outlook for 2017 we relaxed our underwriting stance last year. However, more attention is currently given to businesses active in the infrastructure segment because of shrinking order books.

When assessing a buyer's creditworthiness, we require up-to-date financial information, and details of their 2016 order book and payment experience. Additionally, we seek details on a company's financing (covenants/securities) and the maturity dates of bank loans. Our aim is still to maximise the insurance cover we can give our customers, and in this respect third party securities, if available, can help.

Dutch construction sector

Strengths	Robust economic growth
	Less restrictive bank lending
	Demographic development
Weaknesses	Overcapacity and pressure on margins remain
	Infrastructure building has lost steam

Source: Atradius

United Kingdom

- **Market uncertainty has increased after the Brexit decision**
- **Contract issues and underperformance are concerns**
- **High level of payment delays**

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

After a weak performance in Q3 of 2016 (the first three months following the Brexit vote), the British construction sector recorded a rebound in Q4, mainly driven by residential construction. That said, commercial construction activity remained affected by subdued investment spending and heightened economic uncertainty.

Skills shortages remain an issue within the industry, particularly in the London building market. This has caused cost pressure and has subsequently dampened the impact of improved tender margins. Legacy contracts have also caused issues, as during the downturn construction companies took on contracts at conditions that were no longer sustainable after 2014, mainly due to raw material price increases and higher labour costs. As many construction businesses have worked on such low margin legacy contracts, losses on contracts have been relatively frequent until recently, despite improving order books. However, it seems that this effect has started to abate towards the end of 2016, as many of those projects have been completed and tender margins for new projects have improved.

Despite increased demand since 2014, contract issues and underperformance remain constant problems in the construction industry, as many businesses have been tempted by larger contracts with attractive margins. At the same time, access to bank finance remains difficult, especially for many smaller construction businesses. For growing businesses with light balance sheets, the risk of those contracts becoming unsustainable intensifies - especially if there are not sufficient reserves available to fund payment delays associated with disputes or contract delays. This has led to several insolvencies in 2015 and 2016, often of businesses experiencing high levels of growth and appearing to perform reasonably well at first sight.

While no major increase in business failures is expected in 2017, the level of insolvencies in the construction sector will remain

United Kingdom: construction sector

	2015	2016	2017f
GDP growth (%)	2.2	2.0	1.3
Sector value added growth (%)	2.9	4.1	2.3

Sector share in the national economy (%)	6.5
Average sector growth over the past 3 years (%)	3.6
Average sector growth over the past 5 years (%)	1.1
Degree of export orientation	low
Degree of competition	high

Sources: IHS, Atradius

high. The same accounts for protracted payments and the level of non-payment notifications, which are expected to increase in H1 of 2017.

So far, the implications of the June 2016 Brexit decision on the British construction sector have been limited. Cost pressures have increased due to the depreciation of the British pound, as suppliers passed on higher costs of imported raw materials, and uncertainty remains in the market. However, many contractors still have 1-2 years of secured order books prior to the Brexit decision (particularly in the London market), which serve as a short-term buffer. Additionally, there are major public infrastructure schemes in the pipeline, such as HS2 (a high speed rail network connecting the North and South of England), Hinkley Point (a nuclear power station) and Crossrail 2 (a railway serving London and the wider South East).

That said, it seems quite probable that in the medium- to long-term the Brexit decision will adversely impact construction, i.e. slower GDP growth and lower consumer, business and investor confidence will most probably put downward pressure on building performance. Uncertainty in the market is expected to grow in the coming years, especially as a 'hard Brexit' seems to be a possibility.

After increasing our risk appetite in 2014, our underwriting stance has again become more restrictive since early 2015, when construction business failures started to increase again. For the time being, we continue to underwrite cautiously, with risks considered on a case-by-case basis. With legacy issues having been an issue for a number of years, and some seemingly healthy construction businesses rapidly deteriorating due to contract issues and underperformance, there is a need to receive the most updated management accounts from buyers. Close contact to buyers and regular provision of management accounts enables us to make a more informed decision on credit limit applications and ensures that decisions are as current as possible.

While Brexit will undoubtedly have an impact on the construction market, for the time being the extent of this impact is unclear. But it looks more and more likely that Article 50 will be invoked in March 2017 and that there will be a 'hard Brexit'. Therefore, we will monitor things closely with a 'business as usual' approach, and adapt our underwriting stance as the situation progresses.

British construction sector

Strengths	Sector has rebounded, as output grew in 2015 and 2016
	Secured order books for the coming two years
Weaknesses	Looming uncertainty due to the Brexit decision
	Still high level of payment delays
	Lack of funding affects businesses that may need to resume investment

Source: Atradius

Market performance snapshots

Italy

- **Construction investments expected to decrease again in 2017**
- **Lack of bank financing remains a major issue**
- **High insolvency level remains**

Deterioration in the Italian construction sector started to slow at the end of 2014, as the economy rebounded modestly. However, construction performance is still far away from a real rebound. Italy´s GDP growth remains feeble in 2017 (up 0.7%) after growing just 0.8% in 2016, which will hamper construction growth. After a weak 0.3% increase in 2016, construction investments are expected to decrease 1.2% in 2017, with new housing investments down 3% and public works investments decreasing 3.5%.

Next to subdued spending capacity, tight lending conditions set by banks are the main reason for the poor performance of the construction sector. Given the current problems in the Italian financial sector, it seems that there will be no improvement in the restrictive loan policy anytime soon. Many businesses in the construction sector remain highly geared. Bank loans for residential building decreased from EUR 30 billion in 2007 to less than EUR 8 billion in 2015, and for non-residential construction from EUR 20 billion to EUR 10 billion.

Late payments from public bodies have also contributed to market difficulties. The average payment term stands at 5.5 months, compared to two months set by law. Average payment delays are still long, but have at least decreased since 2014 (from 146 days in H1 of 2014 to 117 days in H1 of 2015 and to 108 days in H1 of 2016). Non-payment notifications are expected to remain at a high level in 2017, but at least no major increase is expected. The same accounts for construction insolvencies, which should remain at an elevated level.

Not all businesses are equally affected by the difficult market situation. Large construction companies have proved to be resilient due to portfolio diversification and export orientation, which makes them less dependent on the domestic market. Large export oriented players (mainly active in African and Middle Eastern countries) are expected to achieve positive results.

In contrast, construction cooperatives and consortiums focused on the domestic residential construction market and dependent on public works have been severely hit by deteriorating demand, decreased bank loans and late payments. Finally, small and medium-sized businesses focused on residential construction are most severely affected, due to decreased investment in private housing (new buildings shrank by more than 60% between 2008 and 2015) and restricted bank loans. The only exceptions have been businesses active in renovation works supported by government incentives (up 19% between 2008 and 2015).

Given the on-going problems, our underwriting stance remains restrictive. However, underwriting is more open for construction players who are export-oriented and less dependent on the domestic public sector.

United States

- The robust performance is expected to continue in 2017
- Payments take between 30-60 days on average
- Still many foreclosures in some states

In 2016 the US construction industry continued its rebound that started in 2012, with value added sector growth up 5.3%, and another 2% increase is expected in 2017. Residential construction is forecast to remain robust through 2019. Foreclosures have decreased 11% over the past 12 months, however, some states (especially in New England) still recorded increased foreclosures. Non-residential construction is expected to expand 5.6% in 2017, with hotels, offices, and amusement/recreation venues expected to drive the expansion. The unemployment rate in the construction sector declined to almost 5%, just slightly above the national unemployment rate.

US construction growth in 2017 could get an additional boost if, as announced, the new US administration invests heavily in infrastructure improvements. After the US Federal Reserve raised interest rates in December 2016 further increases are expected in 2017, which could result in accelerated buying activity in the housing segment.

Banks are principally willing to lend to the construction industry, but only for viable and promising projects. As the commercial and residential development markets strengthen, the construction sector´s financing climate is improving. However increasing salaries, healthcare costs for staff and miscellaneous expenses continue to weigh on the already tight margins of many US construction businesses.

Payments in the US construction industry still take 30-60 days on average, while 90 day terms are not uncommon. Over the last two years payment experience in the construction sector has been rather good, and the overall number of late payment notifications we received in 2016 levelled off. US construction insolvencies decreased in 2016, and are expected to level off in 2017. Small businesses in the industry are generally still paying later and have higher bankruptcy rates and delinquent debt than other industries.

Due to the positive development, we have continued to increase our risk appetite for the industry over the past few years. But caution is still advised, especially with smaller construction businesses. 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 or liquidity or deteriorating payment trends.

.

Market performance at a glance

Australia

- In 2016 the Australian construction sector continued to suffer from subdued investment in mining and related projects. However, the industry saw significant increases in residential building activity, as the economy shifts away from its strong focus on mining.
- Residential building activity is expected to increase further in 2017 before slowing down and decreasing in 2018-2019, with an anticipated decline of 6%.
- Modest recovery is forecast in the non-residential segment due to stronger private demand and activity picking up in the infrastructure and commercial sectors. Engineering construction is also expected to increase, driven largely by the telecommunications sector due to rising National Broadband Network (NBN) related investment, as well as road, major rail and light rail projects.
- It is important to take into account regional differences, e.g. while higher housing investment is projected for New South Wales from 2017-2018 onwards, there are weaker growth prospects for Queensland, Western and South Australia.
- Payments in the construction sector take between 90-120 days on average, and the level of non-payment notifications remains high.
- Our underwriting approach remains cautious, particularly for small businesses, the mining-related segment and the Western Australia and Queensland markets generally.

Saudi Arabia

- Construction demand in Saudi Arabia is expected to remain subdued in 2017. Due to the sharp decrease in oil prices since the end of 2014 the Saudi government, as the largest sponsor of construction acitivities, suffered a deterioration of its fiscal position.
- Due to the deterioration in demand competition has increased, as builders have begun to operate on lower margins in order to obtain the remaining available business, which is leading to price wars. As a consequence, construction business profits will deteriorate further in 2017.
- For construction businesses banks are the primary sources of funding. While banks were pursuing a very open loan policy strategy in the past, now lending has turned very restrictive due to the difficult economic situation and increasing default rates. This, together with the deterioriated demand situation, has strained the management of working capital and the cash flow position of most construction businesses, especially for smaller players.
- Payment duration in the industry is 120-180 days on average. Payment experience has been bad over the past year, and non-payment notifications and insolvencies increased in 2016 due to the squeeze on working capital and reduced demand and prices. Both payment delays and protracted defaults are expected to increase by about 30% in the coming six months.
- Due to the deteriorated business performance and credit risk situation, our underwriting stance has become restrictive for all construction subsectors.

Singapore

- Singapore's public construction segment, which accounts for more than 60% of building activity, will continue to expand in the coming years, supported by government investment in transport infrastructure. However, private building projects are expected to deterioate, due to less favourable economic conditions and an increased supply of already completed private housing projects and offices. In this segment competition is expected to increase, and players will try to maintain their top lines by lowering margins.
- Mainly small and medium-sized businesses active in the private construction sector are already suffering from profit margin contraction due to lower demand, coupled with higher labour and rental costs. In 2017 companies will struggle to meet working capital requirements as margins are continuously squeezed.
- 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 the slowdown 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 experience has been bad over the past year, with non-payment notifications mainly coming from Malaysian construction businesses active in Singapore. In contrast, non-payments from Singaporean businesses are less of a problem.
- The protracted default rate in the construction industry is above average. It is expected that insolvencies in the construction sector will increase by about 5% in 2017. Last year the number of businesses in Singapore liquidated after encountering financial trouble was the highest in 11 years, mainly due to slower economic growth of the city state. At least it seems that local banks are more prone to accept restructuring options available, as opposed to resorting to liquidation.
- While our underwriting stance is generally open for businesses related to public sector construction , we are more cautious about the private building segment.

Spain

- The Spanish construction sector continued to rebound in 2016, with a value added growth rate of 3%, mainly due to Spain´s economic recovery, increased foreign investments and a return of business confidence. Lower commodity prices also had a positive impact. 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 2017 value added construction growth is expected to increase again by about 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 ceased, as a large number of players have left the market since 2008. Profit margins were stable in 2016, and are expected to remain so in 2017. Spanish construction businesses are highly dependent on bank funding. In this respect, conditions for external financing have improved since 2015 due to lower interest rates and better growth prospects for the Spanish economy.
- The payment experience has been good over the past two years, and there has been a low number of defaults. This is mainly because financially weak players left the market during and immediately after the downturn, while the remaining businesses are more resilient. It is expected that construction insolvencies will level off or even decrease slightly in 2017 after major decreases in 2015 and 2016.
- Due to the on-going 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. On-going fiscal consolidation could adversely affect the performance of businesses in the civil engineering segment.

Sweden

- In 2015 and 2016 the Swedish economy grew by more than 3%, which has helped to support domestic construction demand, especially in the residential construction segment. Construction performance has also been sustained by low interest rates and government subsidies. Value added construction growth increased 2.6% in 2016, and is expected to grow 2.7% in 2017.
- However, due to fierce competition in the construction market many players - especially smaller players - have low margins. Gearing in the construction industry is not overly high, and banks are generally willing to provide loans to businesses. Both non-payments and insolvencies in the construction sector have been stable in 2016, and are expected to level off in 2017.
- Our underwriting stance is generally open, with no restrictions for any subsectors. However, closer monitoring of small and medium-sized construction companies is required.

United Arab Emirates

- The decrease in oil prices since the end of 2014 has had a negative impact on construction activities in the UAE. The government, as the largest sponsor of construction activities (especially infrastructure), suffered a deterioration of its fiscal position due to decreasing oil revenues.
- Commercial and residential construction are facing headwinds due to reduced demand and a cooling down of the real estate market. In 2016 delivery of residential units in Dubai decreased to approximately 10,000 units compared to the 40,000 units originally planned.
- Decreasing demand, payment delays and strong competition have led to an erosion of businesses´ profitability - both in terms of reduced margins as well as increased provisions towards bad debts.
- Construction businesses are largely dependent on banks to fund their working capital requirements. However, banks have become very restrictive on lending due to the low demand situation and the fact that many construction businesses are already highly geared.
- Payments to suppliers and subcontractors are usually made when receivables are collected from end clients, who currently tend to delay payments. This has a knock-on effect on the trade cycle, with many smaller players struggling to meet their payment commitments. After rising in 2016, non-payments are expected to increase further in the coming six months. Business closures are also on the rise since 2016.
- Due to the currently challenging business environment, we have decreased our risk appetite in all construction subsectors. We are especially cautious on large buyers with sizeable exposure to government projects, buyers operating in the infrastructure segment, and businesses operating in oil field support services.

TABLE OF CONTENS
FULL REPORTS
MARKET PERFORMANCE SNAPSHOTS
MARKET PERFORMANCE AT A GLANCE
OVERVIEW CHART
INDUSTRY PERFORMANCE

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	Fair	Poor
Fair	Fair	Fair	Fair	Fair	Poor	Poor
Good	Fair	Fair	Bleak	Fair	Poor	Poor
Good	Fair	Fair	Poor	Fair	Fair	Poor
Fair	Good	Fair	Poor	Good	Fair	Poor
Fair	Good	Poor	Fair	Good	Poor	Poor
Good	Fair	Fair	Bleak	Poor	Fair	Poor
Good	Good	Poor	Poor	Good	Poor	Poor
Good	Fair	Poor	Fair	Good	Poor	Poor
Fair	Poor	Fair	Fair	Good	Fair	Fair
Fair	Fair	Poor	Fair	Good	Poor	Fair
Fair	Poor	Fair	Fair	Poor	Fair	Fair
Fair	Good	Fair	Fair	Fair	Poor	Poor
Good	Fair	Poor	Poor	Good	Poor	Poor
Good	Good	Poor	Fair	Fair	Poor	Poor
Good	Good	Fair	Bleak	Good	Poor	Fair
Good	Fair	Bleak	Poor	Poor	Fair	Poor
Fair	Fair	Poor	Poor	Fair	Poor	Poor
Good	Poor	Poor	Fair	Fair	Poor	Poor
Good	Fair	Fair	Poor	Good	Fair	Bleak
Good	Fair	Poor	Good	Good	Poor	Poor
Good	Fair	Poor	Poor	Good	Poor	Poor
Good	Fair	Poor	Poor	Fair	Poor	Poor
Fair	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	Fair	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 2016

Europe

Belgium

Financial Services

Down from Good to Fair

Some larger payment default and insolvency cases have hit the sector in recent months.

Machines/Engineering

Up from Fair to Good

Payment default and insolvencies in the industry have decreased further, and business performance is improving due to increased orders.

Denmark

Chemicals/Pharma

Down from Excellent to Good

The performance of pharmaceutical manufacturers remains strong, but the industry faces intensified price controls in its key market, the US.

Italy

Automotive

Up from Fair to Good

Machines/Engineering

Up from Fair to Good

Both industries performed well in 2016, as a weaker euro helped to sustain export growth while domestic demand increased.

Poland

Agriculture

Down from Good to Fair

Several cases of avian flu registered in Poland since the end of 2016 have negatively affected the large poultry farming segment.

Portugal

Automotive

Up from Fair to Good

Automotive has benefitted from increasing car sales and an upward trend in the automotive components subsector in recent years. In 2016 new investments by international players have been announced, which should further improve the sector's prospects for the near future.

Russia

Steel

Up from Poor to Fair

In line with the general improvement of the Russian economy (a strengthening rouble, better liquidity situation, growing demand for capital goods) the local steel market has rebounded. Payment behaviour in the steel industry has improved in H2 of 2016.

Slovakia

Agriculture

Up from Fair to Good

The default rate has decreased and financial conditions in the market have improved.

Asia/Oceania

Indonesia

Construction/Construction materials

Up from Fair to Good

The sector benefits from a large amount of new projects initiated by the government in order to build new infrastructure and public facilities/premises.

If you've found this report useful, why not visit our website www.atradius.com, where you'll find many more Atradius publications focusing on the global economy, including more country reports, industry analysis, advice on credit management and essays on current business issues.

On Twitter? Follow @Atradius or search #marketmonitor to stay up to date with the latest edition

Connect with Atradius
on Social Media

@atradius Atradius atradius

Atradius N.V.
David Ricardostraat 1 · 1066 JS Amsterdam
Postbus 8982 · 1006 JD Amsterdam
The Netherlands
Phone: +31 20 553 9111

info@atradius.com
www.atradius.com