

A deteriorated outlook for construction

The situation for the construction sector has remained generally favourable in 2022 but a number of indicators point to a loss of momentum since the spring. Supply-side difficulties have persisted this year and are coupled with negative signals for demand in this sector.

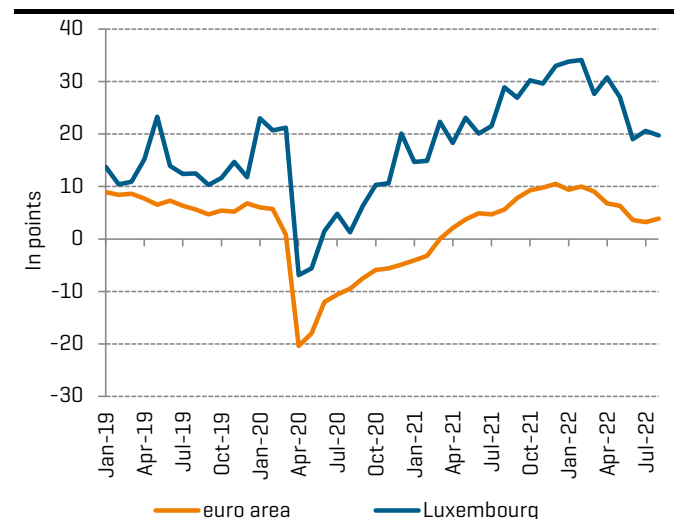
Construction output recovered sharply in 2021. The previous year was affected by the consequences of the health crisis [including a full month of shutdowns on all construction sites]. It returned to pre-crisis levels by mid-2020 and broadly stabilised thereafter. However, the upturn in output was more marked for building and civil engineering companies than for specialist activities such as roofing, carpentry, technical installations and finishing.

Construction contractor confidence peaked in the first quarter of 2022. This indicator is based on two questions in STATEC's business survey, firstly on the order books and secondly on the employment outlook for the next three months. However, both elements of the confidence indicator deteriorated in the second quarter [order books dropped sharply in June] and stabilised in July and August [latest available data]. Output data gathered in the meantime reveals that output declined in the second quarter [-4.2% over a quarter]. Despite the recent decline in construction sentiment, it remains at a historic high. These trends in Luxembourg's construction sector are very similar to those observed in the euro area over the same period.

Supply issues were already apparent in 2021: despite healthier order books [which indicates growing demand], output was relatively stable. These supply issues were due to two factors. Firstly, there were supply difficulties for some materials, a global phenomenon due to the strong recovery in demand after the pandemic [creating shortages and disruptions in logistical chains]. This pushed up input prices sharply [and hence prices of construction services] and lengthened the time required to complete work. Secondly, recruitment difficulties have increased [according to companies' responses in business surveys on whether labour shortages are affecting their output].

These supply-side issues have persisted in 2022 [and have even intensified in the case of recruitment] and the latest trends mentioned above seem to indicate that demand could also be affected. The economic environment [which is marked by high inflation] and the business outlook for this and next year have deteriorated significantly, weighing on household and business confidence. These are very negative signals for consumption and investment [and thus also for construction demand].

CONFIDENCE INDICATORS IN CONSTRUCTION



Sources: European Commission, STATEC (seasonally adjusted data – last point: August 2022)

Upward pressure on prices

Producer prices in construction rose almost 15% year-on-year in Luxembourg in the second quarter of 2022 [a record high replicated across many euro-area countries over the same period]. This increase in the price of construction services may well act as a brake on consumer and business demand, already experiencing a sharp rise in general inflation and energy bills. Rising interest rates have also weighed on borrowing capacity and demand for mortgages in Luxembourg and the euro area has fallen in recent months.¹

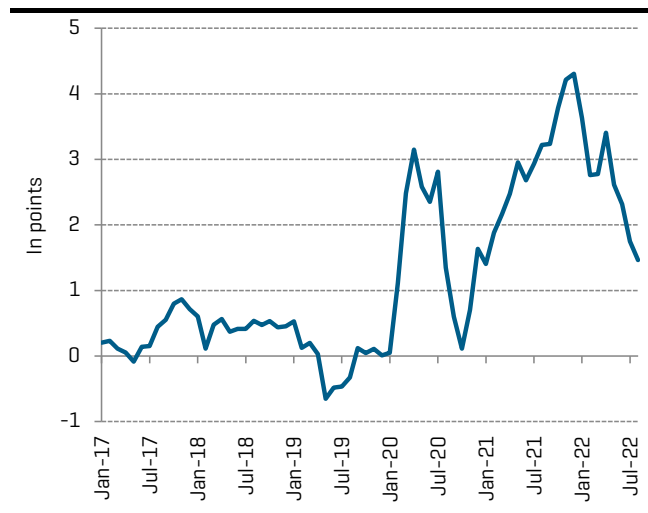
Some manufacturers in Europe – notably in the glass and steel sectors – have already announced their decision to suspend production during the coming winter due to rising energy prices. This could potentially increase the supply difficulties for some materials used in the construction sector.

¹ See page 2, Conjoncture Flash of August 2022

<https://statistiques.public.lu/en/publications/series/conjoncture-flash/2022/08-22-conjflash.html>

International 1/2

GLOBAL SUPPLY CHAIN PRESSURE INDEX



Source: Federal Reserve Bank of New York

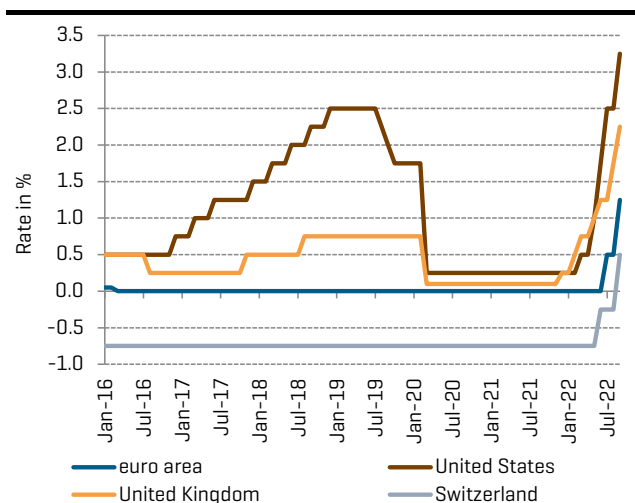
Pressure on supply eases

Worldwide supply difficulties remain but seem to be gradually easing. This finding is based on the Global Supply Chain Pressure Index drawn up by the New York Federal Reserve and published since spring 2022. This index is based on sea and air freight cost indicators and Purchasing Manager Indices (PMI) surveys on delivery times, backlogs and purchased stocks.

After soaring in early 2020 at the outbreak of the COVID-19 pandemic, the index then subsided when restrictions were lifted. It rose sharply throughout 2021 due to new waves of infections (and lockdowns) and to the strong recovery in demand for goods (particularly in the US), which created bottlenecks in the production and logistics chains. It fell in 2022 (but rose briefly in April due to lockdowns in China and rising energy prices after the outbreak of war in Ukraine), but in August it was still above its long-term average (equal to 0).

International 2/2

KEY INTEREST RATES



Source: Macrobond

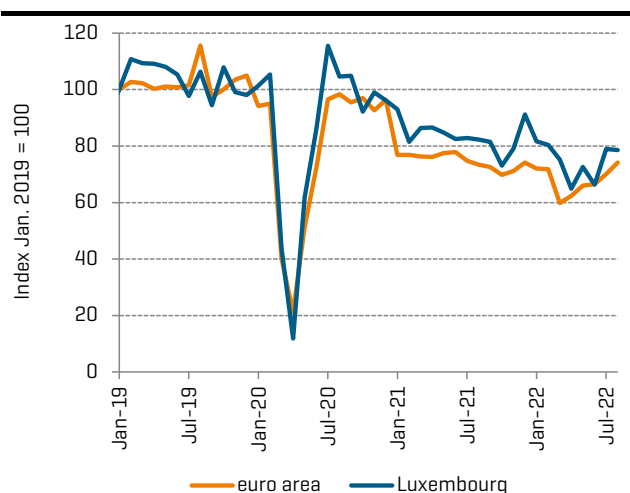
Key interest rates set to rise faster

High inflation, expected to remain well above the 2% target for some time, is prompting central banks to tighten monetary policy more quickly by raising policy rates more sharply. In September, the European Central Bank (ECB) raised its three key interest rates by a historic 75 basis points. The Bank of England, one of the first to raise rates at the end of 2021, increased rates by 50 basis points for the second consecutive time (the seventh hike since last December). The US Federal Reserve raised rates 75 basis points three times in a row.

Key interest rates are being raised in a growing number of countries and are expected to continue to rise in the coming months "to dampen demand and guard against the risk of a persistent upward shift in inflation expectations" according to the ECB. Monetary tightening will nevertheless weigh heavily on growth in advanced economies by curbing demand.

Consumption

NEW REGISTRATIONS OF PRIVATE CARS



Sources: SNCT, ACEA, STATEC [seasonally adjusted data – last updated in August 2022]

Vehicle sales remain low

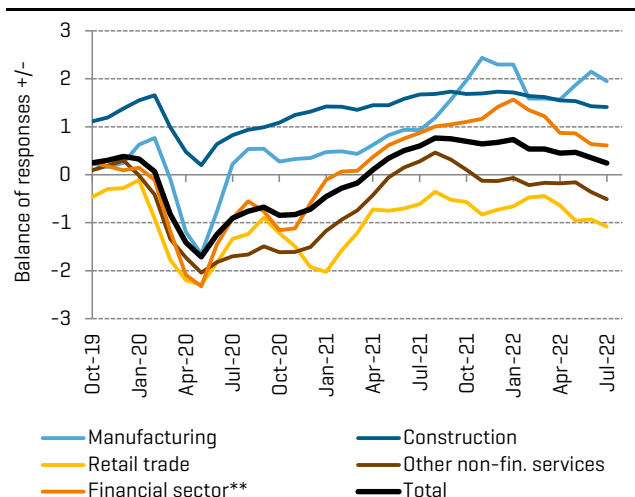
The industry is facing its third consecutive year of declining passenger car sales. In the first eight months of 2022, new registrations in Luxembourg were down by 11% year-on-year, very close to the result for the euro area [-12% over the same period].

Based on seasonally adjusted data, car registrations have recently started to recover (after a low point in March for the euro area and in April for Luxembourg), but the recovery is still timid – around 20% below pre-COVID levels. At the same time, output in the automotive industry in Europe has recovered [+20% between March and July 2022], although this is not uniform across the various Member States (fairly marked in Poland, the Czech Republic and the Netherlands but much more moderate in Italy and Spain).

New commercial vehicle registrations are falling again this year (after rebounding in 2021). However, the decline is less marked in Luxembourg [-15% over one year for the first eight months] than in the euro area [-20%].

Labour market

EMPLOYMENT PROSPECTS OF LUXEMBOURGISH COMPANIES*



Sources: STATEC, European Commission (business surveys)

* standardised and smoothed three-month series, ** euro area

Employment prospects deteriorate

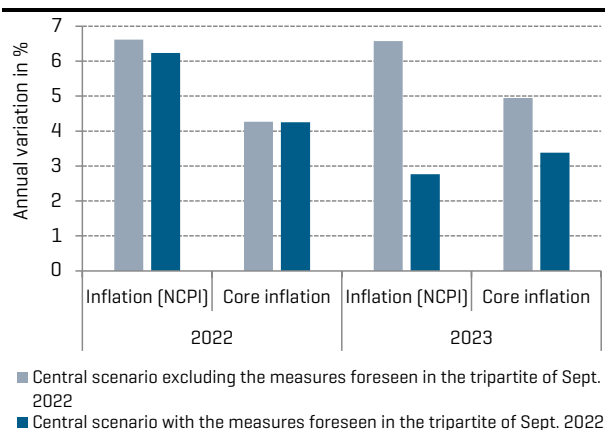
While employment remained very strong up to Q2 2022 in the euro area [+0.4% quarter-on-quarter] and in Luxembourg [+0.8%], the outlook has been deteriorating since the beginning of the year.

All sectors in Europe are affected, despite a slight pick-up in August [the latest available data], particularly in construction. In Luxembourg, on the other hand, recruitment intentions in manufacturing remained relatively high up to August 2022. In non-financial services (which account for one third of total employment), the bleakest prospects were in advertising and market research, post and courier activities, publishing and computer programming and consultancy services.

The initial figures available for August point to slowing employment [+3.4% year-on-year after +3.6% in Q2 and +3.7% in Q1] and rising unemployment [4.8% of the labour force, after stabilising at 4.7% from March to July].

Inflation

INFLATION FORECASTS WITH AND WITHOUT "TRIPARTITE" MEASURES



Source: STATEC

Note: The measures include a one percent reduction in VAT (standard, intermediate and reduced rates), a freeze on electricity prices in 2023, gas price rises limited to +15% of current levels and a reduction of 15 cents per litre in the price of heating oil.

Inflation forecasts lowered after tripartite measures

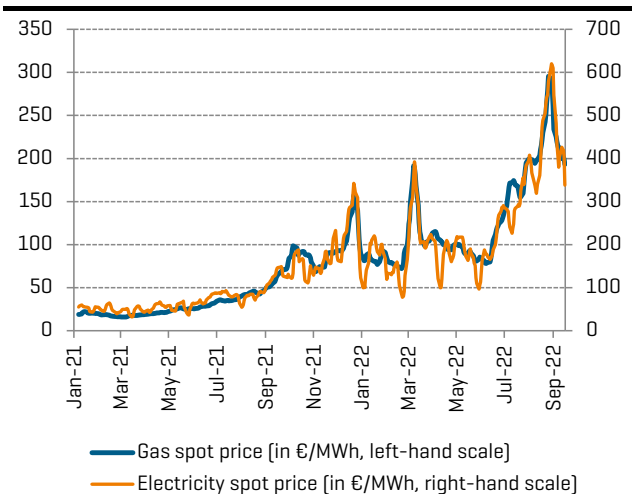
STATEC has updated its inflation forecasts to include the impact of the recent boom in energy markets and the new measures decided following the Tripartite negotiations.

These measures will temporarily remove the uncertainty surrounding energy prices in Luxembourg and will help slow consumer prices.

The latest forecasts predict inflation of 6.2% in 2022 [6.6% in early September forecasts] and 2.8% in 2023 [compared to 6.6%]. Core inflation is expected to reach historically high levels in 2022 [4.3%] but is set to slow slightly in 2023 [3.4%] due to the capping of electricity prices and the VAT cut. The forecast anticipates that the wage indexation threshold will be breached next in the first quarter of 2023.

Energy

CORRELATION BETWEEN GAS AND ELECTRICITY PRICES



Source: Macrobond (moving averages over one week)

Gas prices drove up electricity prices

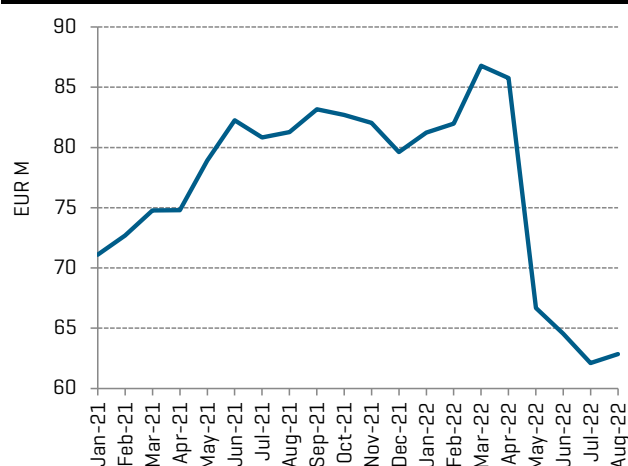
One observes a strong parallelism between gas and electricity prices on energy markets. This is due to the way the electricity market works. Particularly the merit-order mechanism, where prices are determined by the generation plant with the highest marginal costs. In response to the renewed disruption of gas flows from the Nord-Stream 1 pipeline in late August, the spot price of gas rose to unprecedented levels, driving up the price of electricity at the same time.

The European Commission is currently looking at a reform of the European electricity market to decouple electricity from gas prices.

In Luxembourg, energy suppliers announced that starting October, basic gas rates were to go up between 85% and 115%. As a reaction, during the tripartite negotiations in September, the government committed to cap gas increases at 15% until the end of 2023. Electricity prices are frozen at September 2022 levels – basic rates and network charges for electricity would both have increased without this intervention.

Public finances

EXCISE DUTIES ON PETROLEUM PRODUCTS



Sources: Customs and Excise Agency, STATEC (seasonally adjusted data)

Fuel rebate scheme ends

Following the tripartite agreement in March 2022, the government temporarily dropped autonomous excise duties, reducing retail prices for diesel and petrol by EUR 7.5 cent per litre. From mid-April to late August, autonomous excise duties were reduced to zero on unleaded petrol and fell sharply from EUR 90.5 to EUR 26.4 per 1000L for diesel used for fuel. Oil excise receipts fell sharply over this period [-19% over one year], as did service station revenue [-17% over one year in July].

Luxembourg and Germany discontinued fuel rebates in September. In Belgium, the EUR 0.175 rebate will remain in force until the end of 2022. In France, it rose from EUR 0.18 to 0.30 in September and will be lowered to EUR 0.10 in November. These different measures erode the price gaps with France and Belgium, which will weigh on the amount of fuel sales in Luxembourg (which already fell by 15% year-on-year in July for petrol and 21% for diesel). The prices observed in the week of September 19 in Luxembourg were higher than the average price in France [difference of EUR 0.09], but lower than in Belgium [-5 cents for petrol, -15 for diesel].

Trend chart

	Dec-21	Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Average over the last three months	Same period previous year
Annual variations in %, except where otherwise indicated											
Activity											
Industrial output per working day, in volume	8.1	1.3	2.9	-3.2	-0.6	-1.4	-2.2	...	...	-1.4	23.9
Construction output per working day, in volume	-5.8	5.8	5.7	-1.8	-4.0	3.2	-4.4	...	...	-1.9	23.3
Turnover by volume of total retail trade	4.9	6.6	-6.2	0.5	-6.0	-1.7	-4.1	-1.3	...	-2.4	4.9
Prices, wages											
Consumer price index (NCPI)	4.1	3.6	6.6	6.1	7.0	6.8	7.4	6.8	6.8	7.0	2.3
Underlying inflation	2.3	1.4	4.2	3.5	4.2	4.5	4.8	4.7	5.1	4.9	1.2
Oil product index	46.9	48.7	51.7	56.9	59.2	49.7	56.3	43.6	36.0	45.2	28.9
Industrial producer price index	26.3	25.7	24.4	24.9	30.3	32.9	30.1	25.3	...	29.4	6.1
Construction price index ¹	9.3	11.6	11.6	11.6	13.9	13.9	13.9	...	...	13.9	5.2
Average wage bill, per person (National accounts)	5.2	7.0	7.0	7.0	...	...	...	...	...	7.0	1.6
Foreign trade											
Exports of goods (volume)	2.0	1.7	2.2	-0.5	-8.2	0.8	-2.9	-9.4	...	-3.9	10.2
Imports of goods (volume)	1.7	4.7	4.5	7.6	6.9	4.2	2.6	4.5	...	3.8	14.6
Employment, unemployment											
Domestic number of employees	3.7	3.8	3.6	3.7	3.6	3.6	3.5	3.6	3.3	3.5	3.0
National employment	2.8	3.0	2.9	2.8	2.6	2.5	2.5	2.8	2.7	2.6	2.3
Unemployment rate [% of working population, seas. adj.]	5.1	4.9	4.9	4.7	4.7	4.7	4.7	4.7	4.8	4.7	5.6

Source: STATEC

¹ Estimations based on half-yearly data

Indicators

	Quarterly variation in %					
	2021 Q1	2021 Q2	2021 Q3	2021 Q4	2022 Q1	2022 Q2
Eurozone - real GDP growth (European Commission)	-0.1	2.0	2.2	0.5	0.7	0.8
Luxembourg - real GDP growth (STATEC)	2.0	0.6	-0.3	1.7	0.7	-0.5
	Annual variation in %					
	2018	2019	2020	2021	Forecast 2022	Forecast 2023
Luxembourg - real GDP growth (STATEC)	1.2	2.3	-0.8	5.1	2.0	4.0
GDP at current prices 2021: EUR 72 295 million						
Minimum monthly salary (since 01/04/2022): EUR 2 313.38	Consumer price index (08/2022) - base January 1 st 1948: 961.10					
Current account balance (2022 Q2): EUR 610 million	Half-yearly average of the index linked to base as at January 1 st 1948 (08/2022) : 954.51					
Resident population (01/01/2022): 645 397	Estimated deadline for next salary indexation: 2023 Q1					

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