CONJONCTURE FLASH

Economy and prices

MONTHLY PUBLICATION ON THE STATE OF LUXEMBOURG'S ECONOMY– **NOVEMBER 2023**

DOWNTURN IN CONSTRUCTION

Falling demand on the real estate market is having a negative impact on construction activity. Economic indicators for this sector show a clear deterioration, with construction of buildings experiencing a particularly sharp downturn.

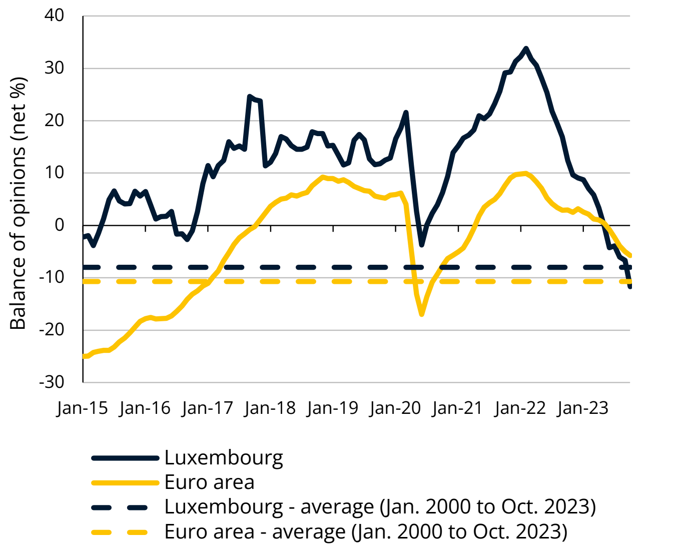
Morale in the construction industry has continued to weaken severely in recent months. Since August 2023, the confidence indicator has fallen below its long-term average and also below the low point reached during the Covid pandemic. The decline was more pronounced in Luxembourg than in the euro area as a whole.

The confidence indicator is based on business owners' perceptions of their order books and on their outlook for employment. Both of these components have been trending downwards since spring 2022, with a more pronounced deterioration of order books in both Luxembourg and the euro area. Business surveys show that among neighbouring countries, Luxembourg and Germany are the most affected by the downturn in construction activity and this is confirmed by many other construction and real estate indicators.

Gross value added (GVA) in real terms in Luxembourg's construction sector fell by 6% year-on-year in the first half of 2023 (latest data available) – whereas it increased slightly by 0.4% in the euro area over the same period. The current difficulties in the sector concern certain areas of activity in particular. Construction of buildings saw GVA fall almost 12% year-on-year in the first half of the year, while the decline was only around 2.5% for both civil engineering and specialised construction activities.[1] The "construction of buildings" sub-sector, which includes structural work and property development, has been particularly hard hit by the drop in new building projects (whereas specialised activities, such as heating engineers or painters, continue to benefit from renovation projects).

Payroll employment in construction began to slow at the start of 2022 and has been falling since the spring of 2023. Employment fell 2.7% year-on-year in October 2023, even more sharply than in 2009 during the financial crisis. As with GVA, the biggest fall was in construction of buildings (-6% year-on-year in August 2023). Employee numbers in specialised construction activities stopped rising in the first half of 2023 and have since fallen back slightly. Luxembourg is one of only four countries in the euro area (along with Italy, Lithuania and Estonia) where employment in the construction industry fell year-on-year in the second quarter of 2023 (latest figures available). The number of construction job seekers registered with ADEM has also risen sharply (+45% year-on-year in October 2023), while the stock of job vacancies is falling, reflecting lower demand for labour.

CONFIDENCE INDICATORS IN CONSTRUCTION



Sources: European Commission, STATEC (data smoothed over 3 months)

Housing to be held responsible

Investment in construction fell 3% year-on-year in the first half of 2023 (compared with around -1% in the euro area), due to falling residential investment (-16% year-on-year in the first half of 2023), while investment in other buildings and civil engineering structures continued to grow (+2.5%).

Falling demand on the real estate market, caused in particular by sharp rises in interest rates, led to a decline in property transactions. The number of transactions in the first half of 2023 fell sharply compared with the previous year, by almost 50% (and even by 70% for apartments under construction). As transactions fell, property prices began to adjust and are now down for the third consecutive quarter[2] (falling 2.7% quarter-on-quarter and 6.4% year-on-year in Q2 2023). New mortgages still fell slightly in Q3, and banks do not expect any turnaround before the end of the year[3], indicating that the difficulties in the construction sector seem set to continue, at least for the remainder of 2023.

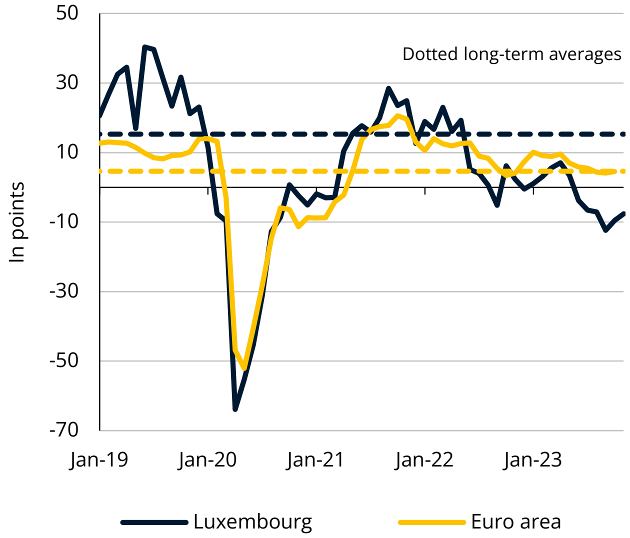
[1] Mainly finishing and technical installation activities.

[2] For more details on price trends and property transactions in Luxembourg and internationally, see the October 2023 Conjoncture Flash.

[3] See below in this Flash

Activity

CONFIDENCE INDICATOR IN NON-FINANCIAL SERVICES



Sources: European Commission, STATEC

Confidence remains low despite some positive signals

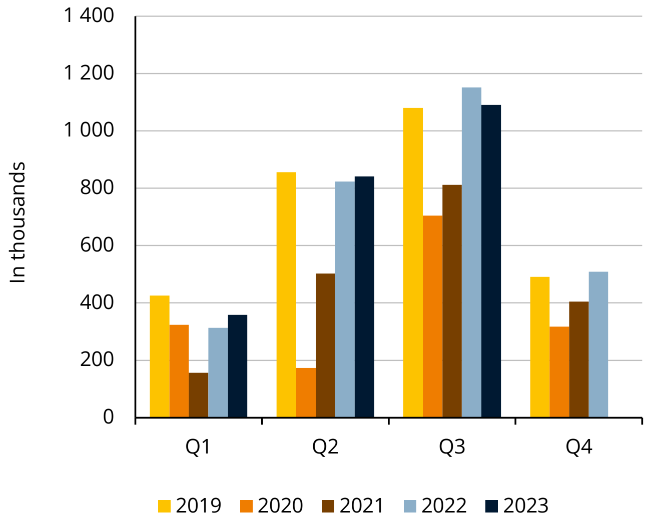
Morale among Luxembourg's non-financial services companies deteriorated significantly in 2022 and declined further in the spring and summer of 2023. Since then, it has been well below its long-term average, while in the euro area it is more or less back up to par.

However, the confidence indicator improved slightly in October and November in Luxembourg (the November results are not yet available for the euro area), with an upturn in opinions on recent demand and the short-term outlook for demand. This modest upturn in optimism came particularly from transport, post and courier activities, accommodation, advertising and market research and, to a lesser extent, legal and accounting services.

The outlook for employment, however, shows no such signs of recovery, and remains on a downward trend (although this does seem to have eased somewhat in recent months).

Tourism

OVERNIGHT STAYS IN TOURIST ACCOMMODATION



Source: STATEC

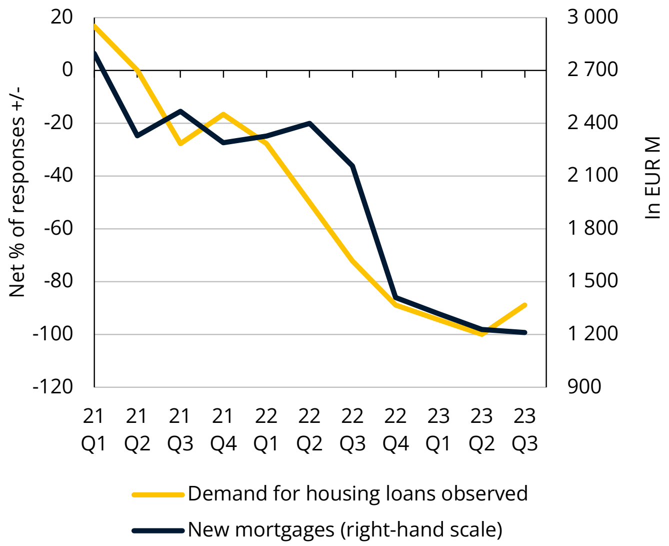
Less favourable weather conditions in Q3?

Over the first 9 months of 2023, the number of overnight stays in tourist accommodation establishments in Luxembourg was stagnant compared to the same period in 2022. The results over the first two quarters were better than last year but performance was down over the summer (-5.3% year-on-year in Q3). Campsites in particular (-7.3%) saw their customer numbers fall, no doubt due to the unfavourable weather. Traditionally the peak months for tourism, July and August this year were marked by relatively cold temperatures and much higher than normal rainfall. The numbers of Dutch tourists in particular, a key customer group for Grand Duchy campsites, declined sharply in Q3 (-12% year-on-year).

On the other hand, the number of arrivals rose 5.7% over the first nine months (given the stagnation in overnight stays, this indicates that average stay length has fallen) but this is around half the increase seen elsewhere in the euro area, where southern countries posted the best results.

Real estate

MORTGAGE APPLICATIONS IN LUXEMBOURG



Sources: BCL (loans to non-promoter residents, seasonally adjusted data), European Commission (bank lending survey, moving average over last three quarters)

Demand for mortgages remains weak

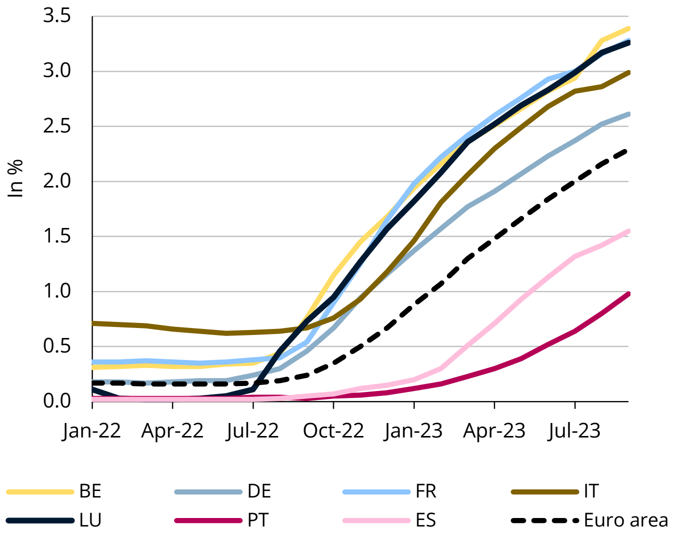
According to the bank lending survey, demand for mortgages fell again in Q3 due to the worsening outlook for the property market and deteriorating household confidence. Banks do not expect any improvement in the final quarter of 2023.

New mortgages granted to resident households in Q3 fell a further 1% quarter-on-quarter, following four consecutive quarters of sharp declines (-44% year-on-year). Total outstanding mortgages in Luxembourg are now down 1% year-on-year. This is the first time outstanding mortgages have fallen since data compilation began in 1999.

The ten-year fixed interest rate on new mortgages has fallen slightly since May 2023, averaging 3.8% in September (+2.2 percentage points over one year). Variable rates stabilised at around 4.8% (+3.3 percentage points over one year). Average rates on outstanding mortgages stabilised at 2.8% in Q3 (+1.2 percentage points over one year).

Financial sector

INTEREST RATE ON OUTSTANDING HOUSEHOLD TERM DEPOSITS



Source: European Central Bank

Savings in Luxembourg relatively better remunerated

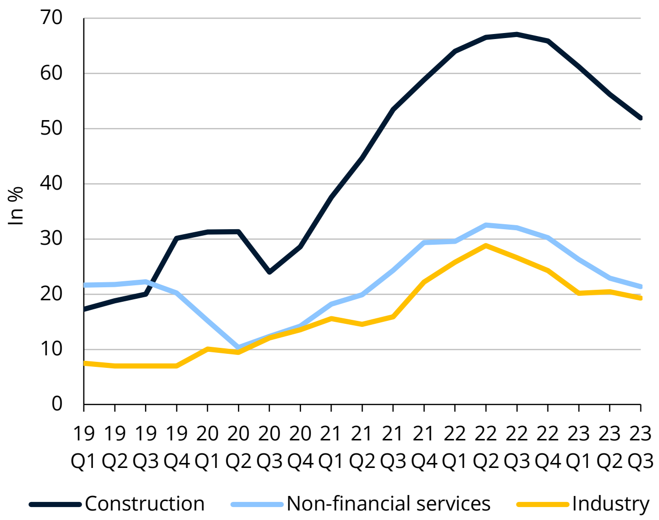
While the rise in key interest rates has pushed up lending rates, it has also enabled banks to raise rates on savings accounts. Since the first rate hike by the European Central Bank in July 2022, rates on household deposits with agreed maturity (up to 2 years) have risen 3.2 percentage points in Luxembourg (compared with +2.1 percentage points in the euro area). Household deposit rates have increased most in Luxembourg.

In September 2023, the average interest rate on outstanding term deposits in Luxembourg was 3.3%, the same as in France and just behind Belgium (3.4%). The average rate in the euro area is 2.3%.

This rise in interest rates has encouraged households to put more money into term accounts. Since July 2022, outstanding term deposits by resident households have increased fivefold in Luxembourg and by a factor of 2.5 in the euro area.

Labour market

PERCENTAGE OF COMPANIES REPORTING RECRUITMENT DIFFICULTIES



Source: STATEC (business surveys)

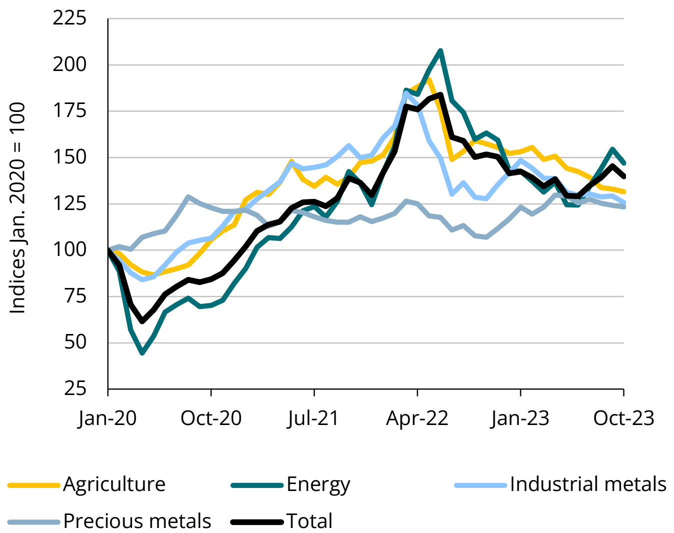
Recruitment difficulties persist

Slowing employment and rising unemployment have helped ease recruitment difficulties, which peaked in 2022. But this does not mean that the labour shortage problem has been resolved, including (or even especially) in those sectors where worker numbers have fallen the most in recent quarters. As a result, half of all construction companies were still reporting recruitment difficulties in autumn 2023, despite the fact that this sector lost 1 000 workers between Q4 2022 and Q3 2023 (-2% seasonally adjusted). In manufacturing, where employee numbers fell more than 1% between Q1 and Q3 2023 (500 fewer jobs) but where hiring prospects have been improving since the summer, 20% of companies are still struggling to recruit. In both cases, although tensions have eased in recent quarters, the numbers remain well above pre-crisis Covid levels.

Within non-financial services, two areas in particular are experiencing fewer recruitment difficulties: a third of firms engaged in legal and accounting activities or in IT programming and consultancy are still struggling to find staff, down from two thirds in late 2022.

Inflation

COMMODITY PRICES



Sources: Macrobond, STATEC calculations

Pressure on commodity prices eases

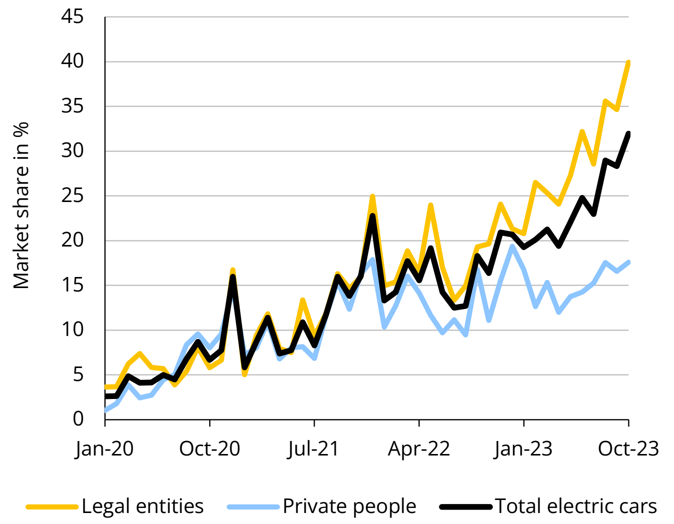
Commodity prices rose sharply in 2021 due to supply difficulties related to the post-Covid recovery. They peaked in spring 2022 following the Russian invasion of Ukraine. Since then, prices for most types of commodity have tended to fall.

Prices for energy products began to rise again between June and September 2023, in line with the rise in oil prices over this period. However, they fell back again in October (a trend that is expected to continue in November). Only gas prices, which are not directly linked to oil prices, have been rising steadily since May 2023.

Staple food prices have been falling back, particularly for oils, which had soared over the past three years (+225% between May 2020 and March 2022), partly due to droughts in Spain, but also cereal prices, which rose sharply after Russia blocked Ukrainian cereal exports. Sugar was the only commodity for which prices did not fall back in late 2023 (up to October at least), but stabilised at a rather high level.

Energy

NEW REGISTRATIONS OF ELECTRIC CARS IN LUXEMBOURG



Source: SNCA

Electromobility boosted by companies and leasing

Registrations of fully electric cars in October passed a symbolic milestone in Luxembourg, accounting for more than 30% of new registrations for the first time. While market share was just 6% in 2020, it rose to 24% in the first ten months of 2023. This is mainly attributable to registrations by legal entities (companies and leasing companies), which account for around 60% of the market.

In 2020, the market share of electric mobility was relatively similar for companies and private individuals. However, in 2023, it will be around twice as high for companies (29%) as for individuals (15%). Growth in plug-in hybrids is less dynamic, rising from 5% in 2020 to 7% in the first ten months of 2023 (9% for corporate customers, 5% for private customers).

At present, fully electric vehicles account for 5% of the Luxembourg car fleet, while plug-in hybrids make up 3%.

Dashboard

	Feb-23	Mar-23	Apr-23	May-23	Jun-23	Jul-23	Aug-23	Sep-23	Oct-23	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	-3.1	-1.4	-7.4	-7.1	-6.3	-6.6	-5.0	-10.3	...	-7.5	-0.3
Construction output per working day, in volume	0.3	-2.1	0.8	-2.6	-0.5	-1.1	7.1	-2.4	...	0.1	0.2
Turnover by volume of total retail trade	-2.2	-5.1	-4.4	-3.0	3.4	-0.7	-2.3	-3.7	...	-2.2	1.6
Prices, wages											
Consumer price index (NCPI)	4.3	3.6	3.7	3.6	3.2	3.7	4.2	4.0	3.2	3.8	6.8
Underlying inflation	4.8	4.7	4.9	4.8	4.7	4.9	4.5	4.3	4.2	4.3	5.1
Oil product index	-3.5	-11.4	-13.5	-13.9	-17.4	-12.8	-1.3	-0.6	-10.8	-4.5	36.1
Industrial producer price index	13.0	9.7	2.5	-1.4	-3.8	-7.2	-7.3	2.2	...	-4.1	26.0
Construction price index[1]	14.1	14.1	12.3	12.3	12.3	...	...	...	...	12.3	13.9
Average wage bill, per person (National accounts)	6.4	6.4	6.3	6.3	6.3	...	...	...	...	7.0	6.0
Foreign trade											
Exports of goods (volume)	-1.9	-0.7	0.2	-4.0	0.9	6.2	-1.7	0.2	...	1.5	-4.8
Imports of goods (volume)	2.8	2.4	-8.2	-3.2	-1.8	-5.8	2.3	-3.2	...	-2.4	4.3
Employment, unemployment											
Domestic number of employees	2.9	2.7	2.7	2.4	2.2	1.9	1.9	1.7	1.4	1.7	3.3
National employment	2.3	2.2	2.3	2.1	1.9	1.7	1.5	1.5	1.3	1.4	2.4
Unemployment rate (% of working population, seas. adj.)	4.9	4.9	5.0	5.0	5.2	5.2	5.3	5.5	5.6	5.5	4.8

Source: STATEC
[1] Estimates based on half-yearly data

Indicators

	Quarterly variation in %					
	2022 Q2	**2022 Q3**	**2022 Q4**	**2023 Q1**	**2023 Q2**	**2023 Q2**
Eurozone - real GDP growth (European Commission)	0.8	0.3	0.0	0.0	0.2	-0.1
Luxembourg - real GDP growth (STATEC)	-0.2	0.0	-2.1	0.6	-0.1	...
	Annual variation in %					
	2019	**2020**	**2021**	**2022**	**Forecast 2023***	**Forecast 2024***
Luxembourg - real GDP growth (STATEC)	2.9	-0.9	7.2	1.4	1.5	2.5

*Forecast from the Note de Conjoncture 1-23 (June 2023)

GDP at current prices (2022)	Minimum monthly salary (01/09/2023)	Consumer price index (10/2023)	Current account balance (Q2 2023)	Resident population (01/01/2023)
EUR **77 529** million	EUR **2 570.93**	**1 002.09**	EUR **1 347** million	**660 809**
	Next scheduled salary indexation: **Q3 2024**	Index half-yearly average: **995.34**		

STATEC

For further information
Press office | +352 247-88455 | press@statec.etat.lu
statistics.lu

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