

Box 5

RECENT DEVELOPMENTS IN CONSTRUCTION

On 18 January 2007 Eurostat issued its first monthly publication of estimates of euro area construction production, thus considerably improving the timeliness of an important indicator for the euro area economy. Construction accounts for just 6% of economy-wide value added and for around 20% of overall industrial production in the euro area, but it is much more volatile than other parts of the economy such as services. It also forms close to half of overall investment, typically a key driver of the business cycle. Construction output may therefore play a significant role in explaining the cyclical movements of the euro area economy.¹ This box presents the newly available construction data and briefly reviews recent developments in construction.

¹ For a more detailed analysis of the construction sector, see Box 6 entitled “Construction developments in the euro area”, in the September 2005 issue of the Monthly Bulletin.

Improvements in euro area short-term statistics for construction

Although previously calculated on a monthly basis, construction production data were released only on a quarterly basis and with some lag. The new monthly releases will be available roughly 50 days after the end of the month and reflect an improvement in the extent and timeliness of the underlying national data received by Eurostat. This is a further step towards meeting the requirements of the amended Council Regulation concerning short-term statistics and the Principal European Economic Indicators targets.²

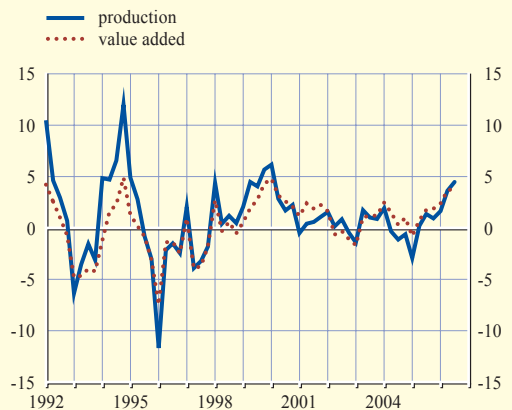
Calculated on a monthly basis, construction output can be volatile, the standard deviation of monthly growth being 3.5%. This makes it difficult to interpret monthly movements and suggests looking at a smoother presentation of the monthly series (e.g. annual percentage changes). Chart A shows that the annual percentage changes of the monthly production series follow reasonably closely the annual percentage changes of the quarterly construction value added series available from national accounts, and can thus act as a useful leading indicator of the latter (which is only released around 60 days after the end of a quarter). Both indicators aim to measure the output net of inputs in construction. The small discrepancies that can be observed between the two series may be due to small conceptual differences in the underlying definitions as well as to differences in the practical implementation of output measures in short-term statistics (e.g. incomplete coverage of construction) at the national level. In addition, the seasonal adjustment of the two indicators at the euro area level is not the same.³

Recent developments in construction

Following a prolonged period of sluggish growth, construction value added has picked up over the past year, expanding at an annual rate of 3.8% in the third quarter of 2006 – the highest rate of growth since early 2000. During the fourth quarter of last year the broad picture of an ongoing expansion prevailed; the three-month average annual growth rate rose to 5.0% in November (see Chart B). This is consistent with survey data that also point to strong activity in the construction sector. For example, the Purchasing Managers' Indices for construction output and new orders were in December at their highest levels since the survey began in 2000. Furthermore, although confidence in the construction sector, as measured by the opinion survey

Chart A Construction production and value added

(annual percentage changes; seasonally and working-day-adjusted quarterly data)



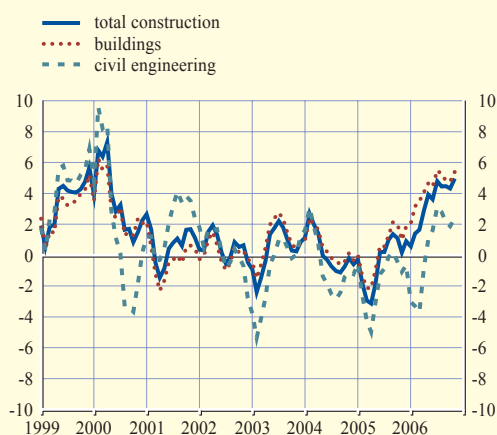
Source: Eurostat.

² Regulation (EC) No 1158/2005 of the European Parliament and of the Council of 6 July 2005 amending Council Regulation (EC) No 1165/98. See also Box 6 entitled "Further progress on the Principal European Economic Indicators" in the December 2005 issue of the Monthly Bulletin.

³ Eurostat compiles the monthly euro area index of construction production by aggregating working-day-adjusted country data and subsequently adjusting this aggregate for seasonal factors. Euro area value added data, on the other hand, are estimated by aggregating seasonally and working-day-adjusted country data. For more details, see Box 5 entitled "Differences between industrial production and value added data in industry in the first quarter of 2004" in the August 2004 issue of the Monthly Bulletin.

Chart B Construction production

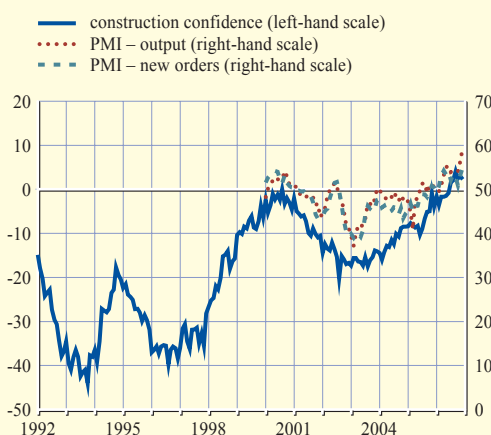
(annual percentage changes, three-month averages; seasonally and working-day-adjusted)



Source: Eurostat.

Chart C Construction survey indicators

(percentage balance and diffusion indicators)



Sources: European Commission Business and Consumer Surveys and NTC Economics.

conducted by the European Commission, fell slightly in the past two months, it remained high by historical standards (see Chart C).

That said, developments have differed within the construction sector. Buildings production, which constitutes around two-thirds of construction, accelerated during 2006 to a pace of growth close to its peak in the late 1990s (see Chart B). By contrast, civil engineering construction, which includes the construction of motorways, bridges and railways and accounts for the remaining third, has been weaker. Although it picked up during the first half of 2006, growth in civil engineering construction has since stabilised at a much lower level.

Differences between countries were also apparent. In several countries, value added growth was consistently strong in 2006, but in other countries growth gained momentum only during the year. The most significant driver of the euro area recovery in construction output during 2006 was the performance of Germany, where the three-month average of annual production growth rose to 9.6% in November. It is possible that this reflected the impact of the VAT increase which took effect in early January 2007, as firms and households brought construction forward to before the start of the year. However, the sustained pick-up in growth throughout the year may also signal the end of a prolonged spell of weak construction in Germany.

To sum up, construction output in the euro area has picked up markedly during the past year, reaching rates of annual growth not seen since the turn of the century. Although the strong growth was partly linked to developments in Germany, the continued strength of the available construction surveys suggests a favourable outlook for the construction sector in the near term.