Grant Thornton

Focus on: construction and real estate

International Business Report 2009 – Sector focus series

The Grant Thornton International Business Report (IBR) 2009 reveals that privately held businesses (PHBs) in the construction and real estate sector are markedly less confident regarding economic prospects for the year ahead than they were in 2008, dramatically affecting the 'big decisions' these businesses have to make. In 2008 a net balance[1] of +47 per cent were optimistic compared to -20 per cent this year. Across all sectors businesses are also less optimistic (-16 per cent) than they were in 2008 (+40 per cent).

IBR 2009 examined the optimism of privately held businesses across eight sectors which we are pleased to share through our sector focus series.

Of the eight sectors, hospitality is the most buoyant with an optimism/pessimism balance of just +2 per cent; ahead of technology (-7 per cent), financial services (-9 per cent), health and education (-19 per cent), manufacturing (-19 per cent), construction and real estate (-20 per cent), retail (-20 per cent), and transport (-39 per cent).

This series will provide key findings, insights into specific national market sectors and our perspective on the outlook for each sector. It will also suggest what tactics businesses should consider in the current economic climate.

If you have 'big decisions' you need help with, please visit www.gti.org. For more information on IBR visit www.internationalbusinessreport.com

The construction and real estate sector

The global construction and real estate sector has encountered tough conditions over the past year.

Contractors have worked through any backlog following the sustained period of robust expansion of the past few years and are now experiencing falling orders. The sector in many countries is experiencing a marked contraction and is having to shed jobs for the first time in many years.

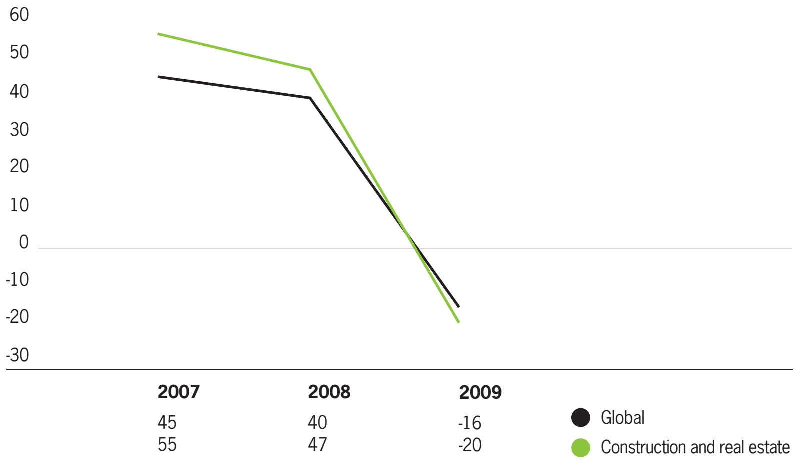
Public sector investment programmes in health, education and infrastructure projects have inevitably been hit by the global recession, although the impact has been mitigated as governments have attempted to shore up demand by proceeding with, or bringing forward, investment programmes. But the boom in private sector investment is well and truly over, replaced by severe contraction as the economic recession takes its toll. The credit crunch and a weakening housing market have hit residential building hard in most economies, while the bleak economic outlook and financial constraints are depressing new building projects in the industrial and commercial sectors.

[1] the balance is the proportion of companies reporting they are optimistic less those reporting they are pessimistic.

Optimism/pessimism

- PHBs in the construction and real estate sector are considerably less optimistic about their country's economic outlook (-20 per cent) than they were in 2008 (+47 per cent)
- levels of optimism regarding economic outlook globally are down 56 per cent compared to 2008.

Figure 1: Outlook for the economy over the next 12 months: 2007-2009
Average percentage balance of businesses indicating optimism against those indicating pessimism

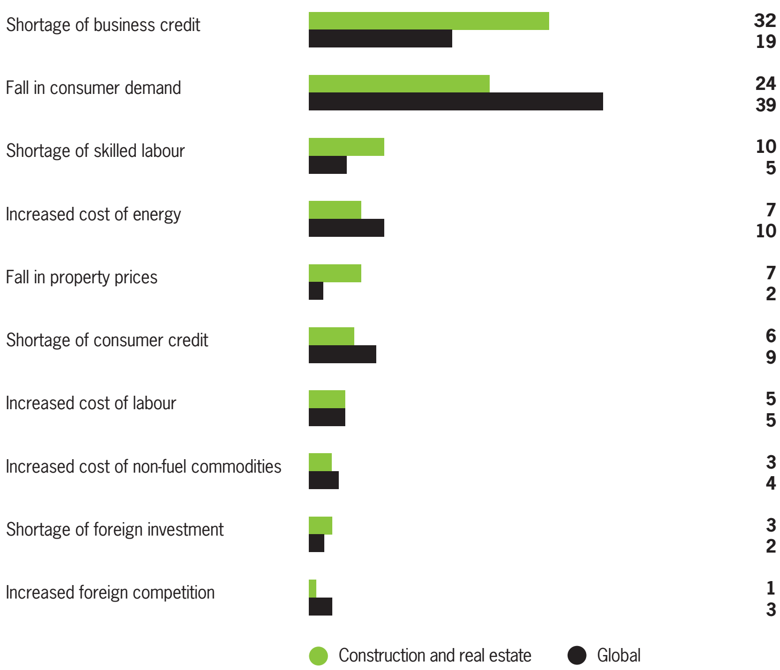


Source: Grant Thornton IBR 2009

Greatest concern

- shortage of business credit is viewed as the greatest concern restricting expansion for PHBs in the construction and real estate sector at 32 per cent (the global average is 19 per cent)
- fall in consumer demand is of greatest concern on average globally (39 per cent); in the construction and real estate sector it is the second greatest concern (24 per cent).

Figure 2: Greatest concern in the next 12 months
Average percentage of businesses



Source: Grant Thornton IBR 2009

Eiten Inamura
Grant Thornton, Japan

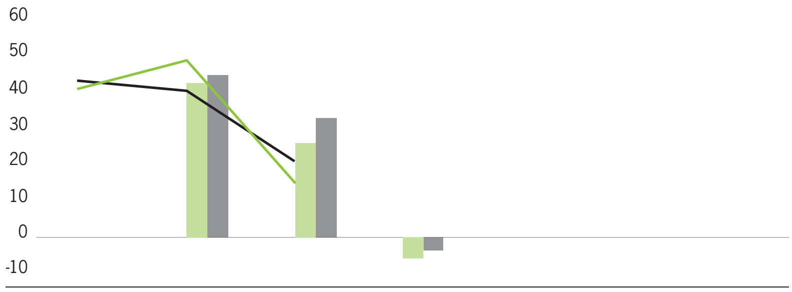
"Resources for investment in Japan have diminished as North American firms repatriate funds exacerbating the credit crunch affecting the sector. Banks are holding off refinancing matured loans for property developers and real estate investment trusts and funds. As a result, a number of listed Japanese companies in property development went out of business in the last six months even though many reported huge income. There are many opportunities for investment in the Japanese property market with prices about 50 per cent down from their peaks in Tokyo – especially in the residential sector."

Employment

- similarly to businesses globally, expected employment growth in the sector has fallen sharply; from +26 per cent in 2008 to -6 per cent in 2009
- businesses globally expect employment to contract from +33 per cent in 2008 to -4 per cent in 2009
- actual employment growth in the sector in 2008 (+15 per cent) was notably lower than expected (+26 per cent).

Figure 3: Employment history: 2007-2009

Percentage balance of businesses



	2006*	2007	2008	2009**
Expected construction and real estate	–	43	26	-6
Expected global	–	45	33	-4
Actual reported global	44	41	21	–
Actual reported construction and real estate	41	49	15	–

*expected data for 2006 not available
**actual data for 2009 will be available in IBR 2010

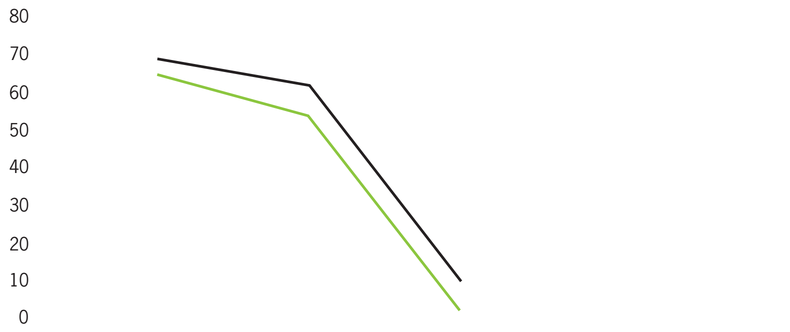
Source: Grant Thornton IBR 2009

Revenue expectations

- PHBs in the construction and real estate sector are much less optimistic about their revenue prospects (+4 per cent) compared to 2008 (+55 per cent)
- expectations for selling prices have also fallen, from a balance of +24 per cent in 2008 to just +1 per cent this year.

Figure 4: Revenue expectations: 2007-2009

Average percentage balance of businesses indicating optimism against those indicating pessimism



	2007	2008	2009
Global	70	63	11
Construction and real estate	66	55	4

Source: Grant Thornton IBR 2009

Roberto Lacerda
Grant Thornton, Brazil

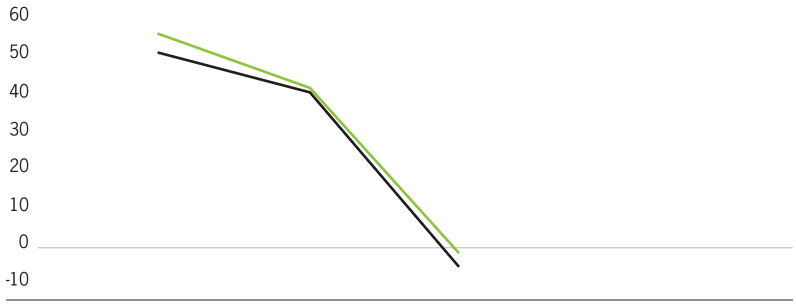
"Merger and acquisition activity in the Brazilian real estate sector is widespread at the moment. As finance becomes less available and more costly, international companies are also finding excellent opportunities for investment in Brazil. The Brazilian market, however, is likely to recover quicker than most, given the absence of the debt burden that afflicts many other countries, plus the substantial boost from the government's infrastructure programme."

Profitability expectations

- PHBs in the construction and real estate sector are less optimistic about their profitability prospects (-1 per cent) compared to 2008 (+42 per cent)
- levels of optimism globally have fallen 46 percentage points from last year.

Figure 5: Profitabilty expectations: 2007-2009

Average percentage balance of businesses indicating optimism against those indicating pessimism



	2007	2008	2009
Construction and real estate	55	42	-1
Global	52	41	-5

Source: Grant Thornton IBR 2009

Constraints

- as with businesses globally, the shortage of orders/reduced demand is viewed as the major constraint restricting expansion for PHBs in the construction and real estate sector (52 per cent) and represents a significant increase from 2008 (34 per cent)
- the lack of availability of skilled workforce is cited by 35 per cent of PHBs in the construction and real estate sector, compared to 27 per cent of businesses globally.

Figure 6: Constraints on expansion

Average percentage of businesses rating constraint 4 or 5 on a scale of 1 to 5 where 1 is not a constraint and 5 is a major constraint

Source: Grant Thornton IBR 2009

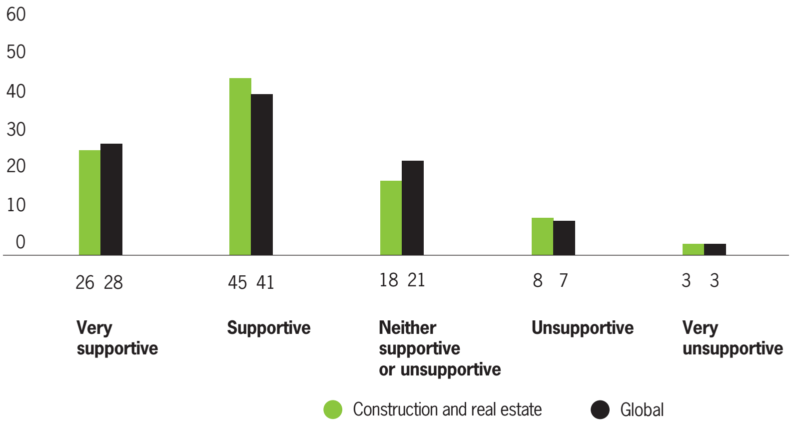
Clare Hartnell
Grant Thornton, United Kingdom

"Uncertainty is undermining confidence with the lack of credit and stringent lending criteria inhibiting activity. For some retailers, payment of rents on a monthly rather than quarterly basis has eased cash flow issues. With more regular payments, landlords are also able to see which tenants are having difficulties sooner. Overall, tougher conditions in the property market means that people who dabbled in property during the boom times, when the going was easy, will exit the market leaving it to the seasoned professionals once again."

Support of lender

- 71 per cent of PHBs in the construction and real estate sector classed lenders as very supportive or supportive, towards their business, slightly above the global average (69 per cent)
- similarly to businesses globally, 11 per cent of PHBs in the construction and real estate sector classed lenders as unsupportive or very unsupportive towards their business.

Figure 7: Level of support provided by lenders
Percentage of businesses

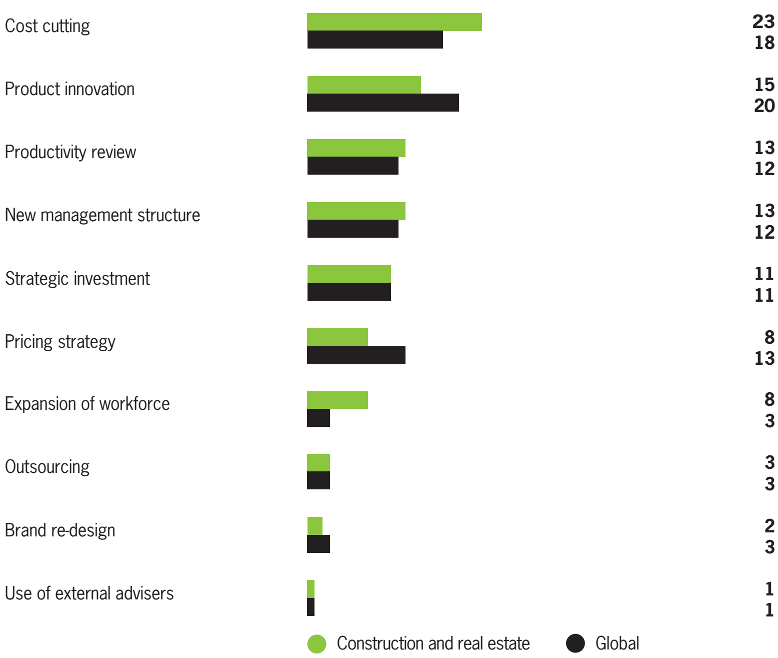


Source: Grant Thornton IBR 2009

Business planning

- cost cutting is the most successful initiative that PHBs in the construction and real estate sector have put in place to increase profitability, 23 per cent of businesses in the sector cited this initiative compared with 18 per cent of businesses globally
- product innovation is the most successful initiative globally, it is cited by one fifth of PHBs globally and by 15 per cent of those in the construction and real estate sector
- pricing strategy has been a more successful strategy for PHBs globally (13 per cent) than those in the construction and real estate sector (8 per cent).

Figure 8: Successful initiatives that have been put into place to increase profitability
Percentage of businesses



Source: Grant Thornton IBR 2009

Todd Taggart
Grant Thornton, United States

"Many projects that were ready to proceed are being put on hold as access to credit is denied. The housing crisis in the United States will continue to haunt the construction and real estate sector. Many weaker players will be forced to liquidate or merge, but the sector should emerge stronger with recovery picking up momentum late this year and into 2010."

Outlook

The outlook for 2009 is very subdued as the global economy endures a synchronised recession affecting most major economies. Real estate and construction demand in many countries is at a low ebb due to weak demand, exacerbated by concerns that banks cannot finance developments, even if the economic case for the project seems viable. The slump in the housing market in several large countries will sustain the decline in residential building for at least another year. Meanwhile, retail development projects are falling victim to much reduced consumer demand and new office building is suffering from contraction in the financial sector and generally reduced demand for office space.

In 2010, a mild economic upturn is expected which should translate into better prospects for the sector. In addition to a gradual resumption of mainstream activities such as private commercial construction, some niche markets could prosper. The energy industry's demands on construction, particularly in renewables such as wind, biomass and sea power, will continue to support activity among specialist firms in these areas. And investment in buildings, infrastructure projects, health and education will become stronger as emerging economies resume vigorous growth.

In most countries, recovery will be gradual and it is widely expected that a more difficult environment will prevail in the sector over the medium term than for most of the past decade.

Tips for survival

- reduce operational costs, but try to avoid cuts that will hurt later
- tight cash flow management
- investigate possibilities in new markets
- try to get extended terms from suppliers
- keep the work force together even if it means pay cuts and reduced hours
- consider asset management where recurring fee income can be obtained
- capitalise on the steep fall in prices by storing up cash to get a good deal at low cost when the time is right.

Reasons to be cheerful

- there are good deals to be done by people who have cash; properties and construction businesses can be obtained at bargain prices
- consolidation in the market is producing viable firms that can provide a range of consultancy services
- stronger economies will emerge from the ruins of the debt financed boom of recent years
- a great deal of money, perhaps $10 trillion, is sitting around in money market accounts waiting until the market hits rock bottom
- although the future environment will be very different, recovery will gradually emerge.

The Grant Thornton International Business Report (IBR) is an annual survey of the views of senior executives in privately held businesses (PHBs) all over the world. Launched in 1992 in nine European countries the report now surveys over 7,200 PHBs in 36 economies providing insights on the economic and commercial issues affecting a segment often described as the 'engine' of the world's economy.

To find out more about IBR and to obtain copies of reports and summaries visit: **www.internationalbusinessreport.com**

The site also allows users to complete the survey and benchmark their results against all other respondents by territory, industry type and size of business.

Participating economies

Argentina
Armenia
Australia
Belgium
Botswana
Brazil
Canada
Chile
China
Denmark
Finland
France
Germany
Greece
Hong Kong
India
Ireland
Italy
Japan
Malaysia
Mexico
Netherlands
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