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THE GLOBAL ECONOMY AND ITS INFLUENCE ON THE SLOVAK CONSTRUCTION SECTOR

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ABSTRACT

For the construction industry, globalization is a trend that means two things: many opportunities and many threats. In the conditions of globalization many management approaches, such as organization structure, strategy forming, planning, motivation and control procedures, communication channels, risk management, etc., must transform.

The aim of the paper is to analyze the influence of globalization on the construction industry in Slovakia and identify the impact of globalization on construction companies in this area.

KEY WORDS

- Construction enterprise management,
- globalization conditions,
- productivity of the sector,
- gross domestic product (GDP),
- global economic crisis

INTRODUCTION

The construction sector is important to the European economy; it accounts for 4 - 9% of gross domestic product (GDP) in the EU Member States and 4 - 10% of total employment. The sector consists of a strong home-oriented market structure, a large number of micro and small companies, including the self-employed, a number of very large international companies (but a decreasing number in a global comparison), and a very low level of R&D investment, especially when compared to Japan.

The construction sector is characterized by many small enterprises and high labor intensity; it is also highly dependent on public regulations and public investments. Thus, policymakers frequently use the sector as a trend indicator – a cyclical stabilizer of macro – economic trends, which are restricted in periods with economic expansion and stimulated in periods of recession.

SWOT ANALYSIS OF THE CONSTRUCTION SECTOR

For Slovakia, it is important to recognize the conditions of the European construction market. We will analyze its Strengths, Weaknesses, Opportunities and Threats (SWOT).

Strengths

- Increased focus on R&D among the large construction companies,
- growing specialization in many firms has created highly knowledgeable and competent companies within specific construction fields.

Weaknesses

- Low productivity,
- weak industry image among customers and potential new workers,
- problems with health and safety in terms of accidents and physical strain on employees,

(percentage change from preceding year)	2007	2008		2009		2010	
		Spring	Jan-09	Spring	Jan-09	Spr.	Jan-09
World GDP growth	5.1	3.1	3.3	-1.4	0.5	1.9	2.75
<i>GDP growth in:</i>							
- the US	2.0	1.1	1.2	-2.9	-1.6	0.9	1.7
- Japan	2.4	-0.7	-0.1	-5.3	-2.4	0.1	-0.2
- China	13.0	9.0	9.7	6.1	6.75	7.8	8.0
- EU	2.9	0.9	1.0	-4.0	-1.8	-0.1	0.5
- Slovakia	10.2	6.4		-6.2*		1.1*	

Source: Summary Report, 67th Euroconstruct Conference, Warsaw, June 2009, p. 33

*Forecast, Ministry of Finance and Statistical Office (June 2009)

The EU forecast – an overview

Real annual % change unless otherwise stated	Euro area			EU 27		
	2008	2009	2010	2008	2009	2010
GDP	0.8	-4.0	-0.1	0.9	-4.0	-0.1
Consumption	0.5	-0.9	-0.3	0.9	-1.5	-0.4
Total investment	0.0	-10.4	-2.7	0.1	-10.5	-2.9
Equipment	0.5	-16.7	-3.7	1.1	15.4	-3.8
Construction	-1.2	-7.2	-2.6	-1.2	-7.9	-2.7
Employment	0.7	-2.6	-1.5	0.7	-2.6	-1.4
Unemployment rate*	7.5	9.9	11.5	7.0	9.4	10.9
Inflation	3.3	0.4	1.2	3.7	0.9	1.3
Gov't balance (% GDP)	-1.9	-5.3	-6.5	-2.3	-6.0	-7.3

* of the labour force

Source: Summary Report, 67th Euroconstruct Conference, Warsaw, June 2009, p. 37

- problems with undeclared work,
- little interest in further education and training among small construction companies,
- low level of R&D investment among small – to – medium (SME) construction companies,
- SMEs lack marketing, ICT and management skills.

Opportunities

- Growth markets in new Member States, China, India and others,
- demographic changes leading to the development of new markets,
- environmentally sustainable development, including waste management,

- off-site construction,
- embedding ICT in construction products and processes to improve efficiency and effectiveness,
- virtual prototyping for design, manufacture and operations,
- new market segments in BOOT activities (Build – Own – Operate – Transfer).

Threats

- Many European markets with stagnating growth, if any growth at all,
- increasingly globalized engineering sector, where Japanese and US construction companies will enter certain European construction sectors,

- recruitment and retention of ageing workforce in some low-skilled professions,
- inter-European price-based competition represents a threat to employment in some EU 15 countries [1].

GLOBAL ECONOMY IN RECESSION

Slovakia is starting to experience the first impacts of the global economic crisis. The country's GDP growth has started to decline to 6.4% (2008) after a record 10.2% growth (2007); for 2009, analysts forecasted an overall GDP decline to 6.2% (07/2009). This development also has an influence on Slovak construction, and the first signs that the long-term sector growth has ended are clearly visible. The sector is experiencing decreasing demand, which causes a lower utilization of capacities, which translates to a decrease in the planned sales volume of the industry.

For the coming period 2010-2011, companies have shown a significant level of uncertainty and force-limited possibilities for their business development. Therefore, the direction in which the economic crisis is moving, which exerts a high impact on the development of demand, will be one of the key drivers for the construction industry's overall development.

Lean times ahead for European construction

Construction output across the 19 countries in the EURO-CONSTRUCT network is projected to fall by 7.5%, following an estimated decline of 3.1% this year. Output is expected to fall further in 2010 (-1%), which means a three-year recession for construction. A gradual recovery is expected in 2011 (+1.6%).

The market across Western Europe is in a very weak position. The volume of construction output in the 15 Western European countries is expected to contract by 8% this year and a further 1.5% next year, following an estimated decline of 3.6% in 2008. Thus, the overall construction market in Western Europe will have reduced in size by 13% by the end of 2010 compared with the peak in 2007.

The worst performers over the next two years (2009-2010) are expected to be Ireland, where the industry is projected to reduce in size by 51%, Spain (-25%), Finland (-21%) and Portugal (-18%). Only Switzerland (+2.3%), Germany (+1.1%) and Sweden (+0.5%) are expected to record growth over this period. Overall, the market is forecast to recover by only 1% in 2011. James Hastings, head of construction futures at Experian, the UK representative of Euroconstruct, has stated: "While countries such as Germany were not nearly so exposed to 'toxic' debt as the UK, their export-led growth has been badly hit by the decline in world trade, with a consequent knock-on effect on construction activity."

Slovakia forecast – the main economic indicators

Index (%)	2008	2009	2010	2011	2012
GDP	6.4	-6.2	1.1	3.4	4.8
Consumption	6.1	-1.7	0.9	2.1	3.3
Total investment	6.8	-5.1	1.9	2.5	3.3
Equipment and service exports	3.2	-19.2	-1.0	6.2	8.5
Employment	3.2	-3.2	-0.9	0.7	1.3
Unemployment rate	9.6	12.5	13.4	13.2	12.6
Real wage growth	3.3	0.3	0.2	1.4	2.2
Inflation	3.9	1.4	2.5	3.3	2.9
Gov't balance (% GDP)	-6.5	-7.1	-7.3	-6.7	-5.3

Source: Ministry of Finance and Statistical Office (June 2009)

Source: 67th EUROCONSTRUCT Warsaw, June 2009

Fig. 1 Gross Domestic Production, Construction Output and Gross Domestic Fixed Capital Formation

The forecasts for the market as a whole have been revised downwards compared with the forecasts made last December due to the worsening global economic environment and the uncertainty regarding the approaches being taken by banks and governments to deal with improperly functioning credit markets.

Members suggest that the Euroconstruct housing market continues to be characterized by a significant contraction in mortgage lending and housing transactions as well as by rising unsold stock levels, weak supply and falling house prices in many countries. Furthermore, the prospect of further job losses - with unemployment levels projected to rise in every Western European country (except Austria and Italy) and in Poland between 2009 and 2011 - may extend the length of time before the housing market moves into a recovery phase.

The weaker economic forecast for the Euroconstruct area as a whole is expected to lead to a decline in the total number of units constructed in the Euroconstruct Area to 1.73 million this year, 5.4% below the corresponding estimate for 2009 last December and 34.1% below the peak year total of 2.62 million in 2007 [2].

EXPECTATIONS FOR THE DEVELOPMENT OF THE SLOVAK CONSTRUCTION SECTOR

The Slovak construction sector has entered a new era. After a long period of growth, the latest forecasts show that this year there will be a decline in the volume of construction. The main reason for such a change is the world economic crisis, which is also affecting Slovakia, and we can already observe its first impacts on Slovak construction. The long-term impact on Slovak construction is difficult to estimate as the crisis is just in its first phase.

As the latest results show (performed in April 2009), the expectation of industry decline has heavily increased. For 2009, 63% of respondents expect the industry to decline this year. On average these enterprises (total sample) forecast the sector decline at 4%, but if we take a more detailed look, the reality could be much worse: over 20% of respondents expect a decline of more than 10%.

With regard to sales developments for 2009, companies expect their sales to follow the overall construction sector's direction and for average sales to drop from the 9% forecasted for 2009 (forecast done in 2008 for the coming year) to 2% growth in 2009 (the current forecast). Improvements are connected with changes in the overall sector (and economy), which are expected for the period 2010 – 2011, when average sales growth should improve to 5%.

The main driver for the sales slowdown is a decrease in demand.

What are the obstacles to growth for Slovak construction companies?

Most of the construction companies interviewed (89%, 90% in 2008) confirmed that they are experiencing obstacles in their business growth. If we take a closer look at the portfolio of constraints indicated, we can see that the key factor limiting companies' business growth is insufficient demand, which has swiftly grown from 26% of the respondents in 2008 to 43% of the companies in 2009. The next factor was stiff competition, at 40% (49% in 2008, 33% in 2007). The most significant change is in the area of labour resources, which is viewed as a limiting factor by far fewer companies (7%) than last year (72%). This is explained by the increased number of workers in the labor market as a result of the reduction in demand and number of projects.

Other obstacles include:

- Insufficient demand
- Weather conditions
- Insufficient labor resources (skilled)
- Insufficient financial resources
- Bureaucracy (dealing with public authorities)
- Competition
- Escalating cost of materials
- Escalating labour costs
- Other

Sources used in getting new business contracts

During the last 12 months most construction companies have not changed the methods/sources they use for new order acquisitions. The most frequently used source of new deals is long-term contacts/networking (personal contacts), which is used by 84% of construction companies; the rating of the usefulness of this source was also very high (8.4 points out of a maximum of 10). This source was followed by direct requests from customers at 78%, which was the most frequently used source for both 2007 and 2008. On average companies use 2.4 sources (2.2 in 2008).

Supplier selection process

The research results show that the most frequently used methods for selecting suppliers are preferred partnering agreements (58% in 2009, 56% in 2008) and long-term contacts/networking (56%, a decrease from 75% in 2008, but an increase in its impact rating from 7.7 points to 8.8 points). Other methods are used less often (e.g. tenders 16%, a drop from 29% a year earlier). On average, the firms use two methods for selecting suppliers (the same as in 2008).

What are the most frequent criteria used by construction companies for selecting their suppliers? The two key criteria used by the construction companies for the selection of their suppliers are the experience of the supplier (76%, growing since 2007) and price (74%, an increase from 60% a year ago). These two are distantly followed by the references of the suppliers (64%). The company size criterion has almost disappeared (a decrease from 21% in 2008 to 5% in 2009). On average, these firms use between two to three criteria for the selection of suppliers (the same was valid for 2008).

The impact of EU enlargement on Slovak construction

Ninety-three per cent of the Slovak construction companies participating in our survey confirmed that EU enlargement and the inclusion of Slovakia into the EU economic area had an impact on the construction sector (88% in 2008). The areas impacted most

Source: The Slovak Construction Annual 2008

Fig. 2 Development of the construction industry – share of GDP (%)

Source: The Slovak Construction Annual 2008

Fig. 3 Development of the construction industry – share of total employment (%)

Source: The Building Contractors Union of Slovakia (July 2009)

Fig. 4 Construction production 2008 – 2009 (mil.€)

(according to the companies' perceptions) have in some instances changed since last year (as did the situation in EU construction overall). The impact on labour is no longer considered so high (i.e., the return of Slovak construction workers from abroad), which also impacts the area of costs. A major increase has been recorded in the area of possibilities for new market expansion, which grew

Development of construction production in Slovakia

Fig. 5 Development of construction production (%)

Residential construction – Slovak Republic

Fig. 6 Development of residential construction (%)

from 55% in 2008 to 71% in 2009. Companies would like to offset local decreasing demand by potential business abroad (which might not be easy due to the overall difficult situation in the construction sector in other EU countries as well)[3].

Construction production in June 2009

Construction production amounted to EUR 556 million in June 2009. Its year-on-year decrease, which had continued since the beginning of the year, moderated to 0.3%. The average daily production decreased by 4.9% compared with June 2008. The development of construction production was mostly affected by enterprises employing 20 people or more. Their volume of production increased by 5.4% year-on-year, as a result of a significant increase in realized civil engineering works (by 30%). A decrease in the construction of buildings (by 11.9%) continued.

In view of production specifications, the construction of buildings decreased by 7.9%, but civil engineering increased by 22.6%. Non-

Non-Residential construction – Slovak Republic

Fig. 7 Development of non-residential construction (%)

Civil engineering – Slovak Republic

Source: The Building Contractors Union of Slovakia (July 2009) – Figures 5, 6, 7, 8

Fig. 8 Development of civil engineering (%)

domestic construction production represented 4.3% of the total volume, and it decreased by 2.9%, year-on-year.

Over the first half of 2009, construction production amounted to EUR 2,579.4 million, i.e., by 9.2% less in comparison with the corresponding period last year. Domestic production amounted to EUR 2,465.1 million, and the downward rate was unchanged. New construction work, including modernization and reconstruction in the amount of EUR 2,032.8 million, decreased by 8.5%. They represented 82.5% (by 0.7 p.p. more than a year ago) of the structure of domestic production. Repair and maintenance work in the amount of EUR 415.4 million was down by 14.4%; their percentages decreased by 1 p.p. to 16.9%. Non-domestic production was down by 9.9%. Labour productivity (EUR 13,905.6), which is measured by construction production per employed person, decreased by 13.2% [4].

Conclusion

The European construction sector faces important challenges today and in the near future. Most of the factors which influence and drive change in the sector will affect it in the years to come. Most of the driving forces mentioned in this report are external factors, which are changing the framework conditions, against which the actors, for example, companies, employees, and sector organizations, will have to act.

The market situation for the construction sector as a whole is also changing. Growing awareness of sustainability leads to environmentally related demands from private and public customers and to demands for relevant public regulations at both the national and EU levels. A greater awareness of health and safety issues in the construction sector also puts pressure on the sector to change and improve the construction process. Construction through public-private partnerships (PPP) is a developing market. These partnerships open up new types of market activities for the financing and operation of construction outcomes. Other market developments relate to demands from the market and public authorities focusing on the construction process and products. Market expectations evolve with activities to improve sustainability in the construction process, materials and constructions, as well as with rising awareness of health and safety aspects in the sector.

Forces driving change from within the sector are mostly the use of new technologies and organizational changes to adapt to the external drivers of change. Several factors will play a significant role in improving the sector's competitiveness in the future, such as the use of ICT in materials and buildings (intelligent buildings), for presentations internally and externally (visualization), for communication with customers and among the partners within a construction project, and for process control (monitoring and tagging activities, materials and equipment). In procurement as well as during the construction process the use of e-business improves information sharing and virtual collaboration.

A central theme in construction management is 'lean' construction, planning the process at various levels to safeguard an optimal flow by identifying potential obstacles and the timely availability of materials, machinery and labour.

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