

GCR rates outlook for construction industry negative

Factors such as regulatory uncertainty, low levels of public infrastructure spending and declining global commodity prices have converged to create turmoil within the construction industry.



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This is according to Patricia Zvarayi, senior corporate analyst at Global Credit Ratings (GCR).

"The uncertainty created by the convergence of these factors led GCR to downgrade or place on negative outlook all construction company ratings that it accorded during 2015," Zvarayi says. "When so many exogenous influences are combining at once, it is very difficult to see through this downward cycle, and no uptick is expected in 2016."

Two of the most crucial areas for new workflow, namely public infrastructure projects and the mining sector, remain very weak.

"The slump in commodity prices has significantly curtailed private sector demand, while falling fiscal inflows will force the South African government to scale back on its much promised infrastructure spend. Although the larger contractors have been successful at augmenting their order books internationally, muted global growth prospects have seen several large projects in sectors such as oil and gas pushed out significantly," she says.

External projects

"In addition, certain South African contractors have encountered challenges with external projects, which have been a massive drain on cash resources and have contributed to the significant loss in value suffered by such listed players. Larger contractors should possess adequate financial resources to ride out the cycle, although earnings are likely to be modest. On the other hand, we have already started to see smaller contractors struggle or go into liquidation."

Zvarayi says regulatory uncertainties also pose a threat to the outlook of the construction industry, one of which is the proposed amendments to BEE codes.

"The construction sector is one of nine local industries with specific BEE codes which could weaken several contractors' scores if regulations change. Any recalcitrance could further strain the industry's relationship with the government, given the negative scrutiny arising from alleged collusion while building or upgrading stadiums for the 2010 FIFA World Cup, as well as poor delivery and onsite incidents related to certain contracts."

Positive developments

Despite these challenges, however, Zvarayi says these obstacles have also contributed to positive developments within the construction industry. "Some of the major positive outcomes of the difficult market conditions include enhanced management oversight and streamlined operations and improvements to risk protocols.

"Despite the tough economic conditions and the negative outlook on the industry, companies with robust contingency plans in place are likely to maintain sound credit risk profiles in this difficult cycle," she concludes.

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