INTRODUCTION

The housing market is once again a leading player in the real estate sector. Following a period of stagnation between 2009 and 2013, activity resumed in 2014 primarily through cooperatives and development management. Market fundamentals improved in 2016, showing an increase in the number of deals and price stability. 2017 is proving to be a confirmation of the robust health enjoyed by the market, shown by a high degree of developer activity and interest on the part of new players in investing and professionalising the sector.

DEMAND-SIDE BEHAVIOUR

The strong performance of the housing market is mirrored in the rise in the number of deals during the first 8 months of the year (January-August 2017), reaching a total of 315,795 transactions. This represents an increase of 14% over the same period in 2016, according to data published by the National Statistics Institute. Although the recovery of the market is now a fact, we nevertheless remain far from the figures recorded for the years prior to the crisis, when 555,221 deals were struck between January and July.

In the Research and Housing departments of BNP PARIBAS REAL ESTATE we consider that the total number of deals recorded for 2017 could reach 530,000.

The figure above shows the trend in the number of private sector housing transactions since 2007, differentiating between new build and second-hand properties, as well as sales and acquisitions made by overseas buyers and sellers, according to the Registrars Association.

DEMAND REMAINS STABLE
The trend goes into reverse as of 2014, with deals on second-hand property predominating due to the standstill of development activity. The increase in these sales continued throughout 2015 and 2016. Nonetheless, within the near future the sales of new homes will steadily gain market share.

The increase in residential sales is not due to changes in foreign demand. This has remained at around 13% since 2014 with both sales at from domestic and overseas buyers rising in parallel.

There is no change in the composition of overseas buyers. Particularly noteworthy is that demand originating from the UK remains significant despite Brexit, cornering 14.9% of the total deals struck by overseas residents in Spain. Besides the British, the main overseas buyers of housing in Spain are French, German, Belgian, Italian and Scandinavian.

There is a significant change in trend over the last 18 months in how sales of new build operate.

During the economic slowdown, the average time to market of a development hovered between 40 and 60 months.

New build projects are now launched in areas where the levels of supply are controlled and, above all, are adjusted to fit the potential demand: the entire housing is already sold prior to the handover of keys. Factors favouring this sales approach include bank requirements for the funding of new projects (between 50% and 60% of pre-sales) and the presence of pent-up demand in the location.

Despite the BREXIT, 14.9% of total foreign transactions come from the United Kingdom.
STOCK TREND

2016 closed with unsold new housing stock amounting to 491,693 units, some 4.31% less than the figure for 2015. The provinces holding the greatest percentage are Alicante, Madrid and Barcelona, together representing 25% of the total stock of unsold private housing. This available stock represents 1.9% of the total housing stock, compared with 2.1% in 2015.

The number of new build permits confirms the return of developer activity. Up to July 2017 these had increased by 19.0% in comparison the same period in 2016. Estimates for the close of year point towards growth of 35%. The number of finished residential units is showing a year-on-year increase of 43% up to June 2017.

The market is being driven by new players, notable among which are Metrovacesa, Neinor Homes, Aedas Homes, Vía Célere and Aelca. All have important major shareholders, Santander and BBVA in the case of Metrovacesa and large American funds, such as Lone Star with Neinor, Värde Partners with Vía Célere and Aelca with Centerbridge. This represents a new business structure for developers with deeper financial backing and cross border involvement.

PRICE TRENDS

Analysis shows prices have trended upwards since the first quarter of 2014 in line with the recovery of housing demand.

The average price per square metre for private housing stood at €1,530/sqm in the second quarter of 2017.

In towns and cities of more than 50,000 inhabitants, the highest private house prices were recorded in San Sebastián: €3,286/sqm, Sant Cugat del Vallès: €2,876/sqm, Barcelona: €2,852/sqm, Getxo: €2,763/sqm, Pozuelo de Alarcón: €2,659/sqm and Madrid, at €2,652/sqm. The price per square metre has yet to re-attain the peak achieved in the first quarter of 2008, when a figure of €2,101/sqm was reached.

The luxury residential sector was one of the least affected by the property crisis and is currently experiencing fastest growth.
Prime projects in Madrid and Barcelona are selling at average levels of €8,000/sqm, reaching between €15,000/sqm and €20,000/sqm in some exceptional developments. Again projects have yet to regain market peaks of 2007 when prices in Madrid were €9,700/sqm and in Barcelona €10,800/sqm.

A significant pricing spread exists among the 52 provinces across the country. As can be seen from the map, the provinces with the highest prices, exceeding €2,000/sqm, are Madrid, Barcelona, Vizcaya, Guipúzcoa and the Balearic Islands. The average house price has increased by some 1.6% over the last 12 months. The provinces recording the greatest price rises are Barcelona, Madrid, Guadalajara, Málaga and Las Palmas.

Two indicators measure the affordability of house buying for families:

- No more than 33% of the available household income to mortgage repayments. The situation here has improved considerably since 2008 as a consequence of the fall in prices and the slide in the Euribor. This indicator currently stands at around 34% in June 2017, the most recent figure published by the Bank of Spain. It must be borne in mind that it is highly dependent on interest rate movements and may vary significantly during the lifespan of the mortgage.

- No more than 4.5 – 5 years before refinancing the mortgage. The most recent figure published by the Bank of Spain is 7 years, whereas the average in Europe stands between 4 and 5 years.

Financing conditions, an enabler of housing demand, is much improved. The Euribor, which is important for refinancing, is at a low and consumers are able to get good access to credit. Following a number of years of restrictions and reluctance on the part of banks to grant mortgages, the situation has changed significantly, the number of mortgages granted and funds loaned are increasing substantially. Nevertheless, although the number of mortgages is increasing, banks are more cautious with regard to their lending criteria and levels of indebtedness of borrowers. Many of the deals have, however, been performed using equity, without the need for financing or with a level of borrowing lower than 30%.
The upper figure sets out the trend in the granting of mortgages for housing from 2010 up to August 2017. The year to date has seen an aggregate year-on-year increase reaching 12% with fixed-rate mortgages gaining market share in the face of fears of interest rate rises over the medium term.

From January to August 2017, 210,439 mortgages were signed, in comparison with the 185,920 recorded for the same period the previous year. The outlook is consequence very positive, as all of the sales contracts which are currently being agreed will show up in the data when the keys are handed over.

**RENTAL MARKET**

The rental market in Spain is less mature than that of other European countries. This, however, is changing and we are witnessing the unprecedented development of the sector.

The difficulties in obtaining finance experienced by certain segments of the population, for example young people, together with employment mobility, are favouring the rental market. This is changing society’s attitudes. Until recently renting was considered «money down the drain», however a high percentage of the population now regard it as a stable life option. New generations are displaying a much more favourable attitude towards the rental market encouraged by different lifestyle patterns - single-parent families; “millennials”; single households.

Rental will become progressively more important over the coming years. The increase in the demand for rental property, centred particularly upon Madrid and Barcelona, has already led to a rise in prices. At the close of the third quarter, the price of rented housing in Spain stood at €9.40/sqm/month, representing a year-on-year increase of 24%. Prices in some cities are at an all-time high, as in the case of Barcelona, where the figure of €18.30/sqm/month has been reached. Madrid is also seeing a rental market boom, with increases of around 11% to an average of €15.30/sqm/month.

The development of the market in the city of Valencia it is also noteworthy, with rental prices rising some 6.1% over the last 12 months and reaching an average of €8.20/sqm/months. There is a low degree of institutionalism in the Spanish market as many rental properties are in the hands of private individuals.
In countries such as Germany there are a number of firms specialising in the sector who often possess 100,000 residential units under management. The entry of new landlords from the fund and Socimis (real estate investment trusts) sectors – attracted by the yields offered by the sector and the strong short to medium-term outlook, is leading to the professionalisation and the development of an institutional framework. Blackstone, Tauro Real Estate, Catella, Activerum SG, Vitruvio Socimi and Renta Corporación already possess significant portfolios of Spanish housing under management and at the forefront of market developments.

There are a number of factors why investors consider this is the perfect time to invest in acquiring residential portfolios:

1) Low purchase prices, in many cases with reductions of between 30% and 50%.
2) Attractive yields, of around 5%.
3) A rising market, the outlook pointing to short to medium-term price increases.
4) Increase in the demand for office space, attracting demand for housing in the surrounding area.

In addition to traditional, long-term rental, the last two years have seen significant growth in new rental models, specifically short and medium-term. A clear example of this phenomenon is that of “Airbnb”, a model with very strong business growth, the demand for which is principally based on tourism. This business is mainly affecting the strongest markets - city centre zones and tourist destinations. The supply is becoming scarce in this market and the phenomenon could lead to an increase in prices over the short term. Some landlords are opting for this business model therefore reducing the stock available for traditional rental.

Nevertheless, it must be borne in mind that these are new models which lack regulation, and which, over the short to medium-term, could be affected by future legal requirements.

The figure above details the trend in the number of land deals at a national level from 2009 up to the second quarter of 2017, the most recent data published by the the Ministry of Development. At the close of the second quarter, the number of land deals amounted to 10,339, reflecting an increase of 28% in comparison with the first half of 2016. In historical terms, more land transactions are recorded during the second half of the year. Therefore, if we apply the average increase for the last 4 years, 2017 would close with approximately 22,700 deals.

Demand interest is focused on the most stable markets, such as Madrid and Barcelona. Nonetheless, faced with the scarcity of available ready to build land, the scope of searches is fanning out towards other markets where the demand for housing is increasing significantly, such as Seville, Málaga and Valencia.

Rising residential market.
Perspective of price growth in the medium-short term
Indeed in Valencia a number of acquisitions of ready to build land were made during the last 12 months within the main areas of the city, Aelca in Patraix, Aedas in Quatre Carreres and Neinor Homes in Malilla. Despite the fact that a large volume of land is available in Spain, the average lead time for the creation of ready to build land amounts to 8 years due to the planning procedures of local authorities. As nobody was interested in investing in the market within this context given the property crash, no new land has been generated over the last 10 years. Where ready to build land is truly lacking is within the most sought-after niches.

As may be seen in the foregoing figure, the average price in towns and cities with a population exceeding 50,000 inhabitants in the main provinces has been on the increase since 2016. In some areas of strong markets upward pressure on prices is being generated by the reduced availability of ready to build land: prices increased by up to 30%-40% over the last 2 years. Prices have increased notably in markets such as Valdebebas, Montecarmelo and even El Cañaver as a consequence of the very scarce offering of ready to build land.

Although the banks are willing to fund land deals, a significant number of the transactions are financed cash down, a fact which demonstrates the current level of confidence in the market and the strong outlook over the short/medium-term.

**DIRECT INVESTMENT IN HOUSING**

Along with the housing portfolios of investment funds and Socimis, the housing market moves a considerable amount of money through private hands. The figure below shows the trend in direct investment in housing since 2007, taking into account the number of transactions, the average price and a theoretical average floor area for the houses. Detail is additionally given on the influence of Madrid and Barcelona on the total.

In recent months the market has reached cruising speed with the entry of new players - investment funds interested in participating in the Spanish housing market through the injection of capital into leading Spanish developers.

The American fund Lone Star acquired the property subsidiary of Kutxabank for €930M in 2014 and Värde took over Via Célere for €90M and Aelca for €50M.

2017 is expected to close with approximately 22,700 transactions.

Average land price. Municipalities > 50,000 pax

We are facing a solid market with an excellent behavior on the part of the fundamentals.
Joint ventures between investors and local firms are also being seen; the fund supplying the capital and the firm its local knowledge. This is the case with Morgan Stanley and Gestilar; and Green Oak with Ibosa for the Torre Borealis project in Madrid.

The recovery of the housing market is driving real estate firms to make the jump into the stock market. Following the flotation of NEINOR HOMES in June and AEDAS HOMES on October 20, there are now two property developers quoted on the stock market. The capitalisation of the two together amounts to more than 2.8 billion Euros. Moreover, the American fund Värde is preparing the flotations of Vía Célere and Aelca. These are anticipated for 2018, taking advantage of the high degree of interest in investing in Spanish property.

**OUTLOOK WHERE ARE WE HEADING?**

- The strong outlook for the Spanish economy over the short to medium-term will favour the demand for housing, within a market context where the current supply is limited. Demand will be supported by better mortgage lending conditions.

- Robust demand, together with the current levels of supply, will contribute to price stabilisation or moderate increases in the strongest markets.

- The market is moving at three different speeds. Firstly there is Madrid, Barcelona and their metropolitan areas.

Further back we find markets such as Costa del Sol, Valencia and the Balearic Islands where demand is high and prices are showing buoyancy. The rest of the market is bringing up the rear where, depending on the specific location, movement is less positive.

- The rental market will continue to grow in importance and it is anticipated that prices will increase, particularly within the main markets. The greater involvement of new players, Socimis, Servicers, investment funds and family offices, attracted by the appealing yields offered by the rental market will contribute to the development of the sector. New firms are likely to appear as demonstrated by the creation of Tempore Properties by SAREB.

**Price stabilization**

[Graph: Spanish housing investment]

**Is a bubble in sight?**

Many people are asking whether the strong return of developer activity and the increase in prices may lead to a new property bubble. There are grounds to suggest that the market is heading towards stabilisation rather than a new negative scenario. The credit restraint policies of financial institutions favour sustainable development of housing, in areas where there is real demand and an excellent sales pace. The existence of these factors in the majority of projects militates against worries of a market implosion.
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A 360° vision

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