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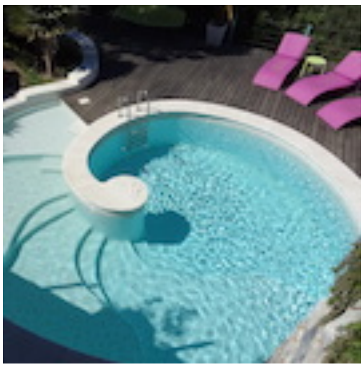
Spanish Market Report

2019

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Introduction

There's no doubt the Spanish property market is in better health in 2019 than for more than a decade. The domestic market is up, both in terms of transaction numbers and prices. Lower prices, rising employment and continuing low interest rates are helping. Meanwhile, the overseas market is at record levels. In fact, there are already 25% more foreign buyers in Spain in 2019 than at the peak of the market before the 2008 crash. All the signs show a sector continuing to expand. However, the property market remains patchy, very buoyant in some regions but flat in others.

I will take a look at who is buying what and where, from the perspective of the overseas market. However, I will also cover factors that may impact the Spanish domestic market in 2019. I will cite statistics and opinions from a variety of sources published throughout the year. These include official INE (Spain's Institute of Statistics) figures and opinions from analysts and valuers.

Where the numbers come from

The Notaries produce the most reliable property market statistics. Consequently, I use those and ignore the Property Registries. Unfortunately, the INE uses both and it can be confusing if you don't know which you are looking at. There are discrepancies between the two for the simple reason they are not counting the same thing. The Notaries' returns count when a transaction actually happens, the date on which a purchase completes. On the other hand, the figures from the Property Registries reflect when that same purchase is inscribed in the registry. And that may be weeks, or even months, later. A purchase completed in a November or December may not make it into the registry until the following year.

And we are not talking a few percentage points out of sync. As we don't yet have 2018 full year returns I'll make the comparison with the first half-year. The Notaries counted 285,822 purchases in 2018 January - June period. However, according to the Registries reckoned 236,524 was the right figure. That's a discrepancy of 19%. And all because Notaries count a deal done and Registries count inscriptions, weeks or even months later. So, unless otherwise stated, the property statistics quoted in this report are those from the Notaries.

Full year stats for 2018 are published during the first two quarters of 2019 and I'll update this report as they become available. I also post news on social media as it becomes available so follow The Property Finders on Twitter and Facebook.

The Good News in Spain

Overall, unemployment continues to fall. It finished 2018 just below 15%, that's the lowest in a decade. Youth unemployment is down to just over 30%. Mortgage approvals rose 10% in 2018 and interest rates remain low. Euribor, which sets the interest rate for the majority of Spanish mortgages ended 2018 at -0.147%. The number of domestic property transactions was up 11%. All autonomous regions registered price increases at some point during 2018, although there were fluctuations.

But there are always buts

Yes, unemployment is down but it is still the 2nd highest in the Eurozone, only in Greece is it worse. And 14.8% has to be viewed against the Eurozone's average of 8.1% and the OECD average of 5.2%. Moreover, in some Spanish regions, Andalucía, Extremadura and the Canary Islands for example, unemployment is still above 20%. Spain has five of the ten worst unemployment black spots in the EU. (Source: Eurostat)

Yes, youth unemployment is down but it is still an average 30% nationally, as high as 50% in some regions. In Germany, it is 6% for the same age group. In fact, one third of the under 30s age group in Spain has never had a job.

Yes, job creation is up but seasonal, temporary and part-time contracts still outnumber permanent ones by a big margin. For example, there were 1.6 million job contracts (new and renewals) signed in August 2018. Sounds good and, in fact, it's a 4.3% rise compared with 2017. But only 153,921 were for permanent jobs, 90.39% were temporary. And permanent doesn't necessarily mean full-time; 60,958 of the 153,921 were for part-time positions. So, it's no surprise that tourism took over from construction as the biggest source of employment in Spain in 2018, with 13.7% of the total workforce. Unfortunately, jobs in tourism tend to be low-skilled, low paid, temporary and seasonal.

The intractable problem

In 2017 The Organisation for Economic Cooperation and Development (OECD) published one of its periodic in-depth reports on Spain. While noting improvements in the economy since the previous report in 2014 it highlighted persistent structural problems hindering sustained recovery. It seems not much has changed. They were the same issues mentioned in the 2014 report, above all the dire unemployment figures.

The reality is that Spain has never been close to full employment even for adults. For example, when it was the fastest growing economy in the Eurozone in 2007 average unemployment was 8%. That's a figure most developed countries would consider high in a recession. But it's so much worse for young people. In the thirty years between 1986 and 2017 the average youth unemployment rate was 34.96%, more or less where it is today. So, in spite of several boom periods in that timeline, Spain has made little progress in improving job prospects for young people. This suggests that the domestic housing market will remain relatively weak for years to come. Ten years after the 2008 property crash Spain's property market is 50% smaller than it was.

There may already be a new blip on the employment horizon. Spain's minority Socialist government, with one eye on Cataluña and the other one on the fact that it only controls 84 of 350 parliamentary seats, plans a 22% hike in the minimum wage, effective January 2019. This is the biggest increase in over 40 years. The governor of the Bank of Spain slammed the move, predicting job losses and lower job creation. And he predicted this will disproportionally affect the young, the low paid and low skilled. That's the very demographic the government says it will help.

The Overseas Property Market - Why Spain?

For lifestyle Spain is hard to beat, it's relaxed and easy-going, safe and child-friendly. Life expectancy rose by ten years between 1970 and 2015. At 80yrs for men and 85yrs for women Spaniards have the highest life expectancy in Europe and are second worldwide. Japan does better but only by a few months. The climate suits all tastes. It ranges from four seasons with a proper winter and lots of snow in the north to the sub-tropical south. The micro-climate zones on the Mediterranean coasts of Andalucía have the best winter temperatures on the European mainland. And not for nothing are The Canary Islands often referred to as Europe's Caribbean. Once again, Spain's beaches and marinas have more Blue Flags than any other country in the world. a total of 691. In fact, Spain has occupied the top spot ever since the scheme began in 1987.

For the cultural tourist Spain has some of the oldest cities in the world and 47 UNESCO World Heritage sites. This puts it in third place globally, behind Italy (54) and China (53). Within Spain, Andalucía is the region with the highest number (8) of recognised sites. The latest one to be be awarded UNESCO status was the Medina Azahara near Córdoba in 2018.

Living well is affordable with food and drink prices below the E.U. average according to Eurostat. Spanish cuisine is world-class. For the third year running Spain has three restaurants listed in the top ten restaurants in the world, more than any other country. And there's a total of seven in the top fifty. Sports and outdoor enthusiasts are spoilt for choice. Golf, tennis, equestrianism, skiing, wind & kitesurfing, mountain biking, rock-climbing, hiking, fishing - the list goes on and on. The result is that Spain has a quality of life that's hard to beat.

The Overseas - Domestic Split

One of the most striking features of the overseas property sector during Spain's long recession is how little it was affected by what was going on during the domestic economic meltdown. It's true that the overseas market fell by about 75% after 2007. It would have been even worse but for the fact that many buyers were already locked in to off-plan purchases made before the crash. But the decline hit bottom in the second half of 2010 and the number of foreign buyers has increased every year since. Meanwhile, the domestic property market was still falling in 2013. When the first upturn was registered in 2014, it was fully four years behind the overseas sector. That's why any analysis of Spain's property market has to look at the domestic and overseas markets separately.

Buoyant and growing

The most detailed breakdown of the overseas market is published half-yearly, first half in November, second half in May of the following year. So, I'm writing this report based on the first half results for 2018. However, first and second halves are normally broadly similar so they are a good indication that the overseas market is on target for another all-time record. The Notaries' returns show a total of 53,359 foreign buyers in the year to June. That's an increase of 5.6% compared with the same period in 2017. In addition, foreign buyers represent a 18.7% share of the total market. This means that the all time record of 100,116 foreign buyers in 2017 is likely to be bettered.

Just how important international buyers are for the property market in Spain is underlined by that fact that this sector is already more than 25% larger than it was at the pre-crash peak in 2006. In contrast, the Spanish domestic sector is approximately 50% smaller.

Where is the Action?

I said in the introduction to this report that, in spite of lots more good news, the market is still patchy. This really stands out when you look at the variation between the autonomous regions. Way out in front is the Comunidad Valencia with 15,613 foreign buyers, up 16.7%. Andalucía is in 2nd place up 8.2% with 9,737. In contrast, regions not located in the Mediterranean hotspots don't fare so well. Cantabria welcomed just 145 buyers from overseas in this period while Extremadura was the lowest with 144.

The reality is that around 60% of all Spain's property sales in the first half of 2018 occurred in the Mediterranean coastal regions on the mainland and in the Balearics and the Canary Islands. That's because these are the places the majority of international buyers head for. And when you add the Madrid region to the mix, the market share rise to 70%, making it easy to see how uneven the recovery is.

And the same patchy recovery pattern occurs within regions as well. Andalucía, Spain's largest autonomous region, is a good example of this. About 20% of all property transactions in Spain take place in Andalucía. However, Andalucía has eight provinces and more than 33% of transactions occur in just one province, Málaga. Moreover, the city itself, plus Marbella, Estepona and Mijas account for 45% of all purchases in the province. So, one third of Andalucían purchases occur in one province while half of purchases in that province occur in relatively small area. It's obvious there's not much going on elsewhere.

However, there was a standout statistic in these figures. Two leading Mediterranean destinations registered fewer foreign buyers compared with the same period in 2017. Cataluña's total of 7,570 foreign buyers was down 5.3%. Without doubt, the region's political turmoil following the Independence referendum in October 2017 is part of the explanation. In recent years overseas investors have been an important part of the region's property market. I'm also wondering if the much tighter control of Barcelona's tourist rental market is acting as a deterrent. And I don't just mean the serious buy-to-let investor, I also include second home buyers who want some rental income to cover running costs. I discuss these restrictions in a blog here.

However, I find the decline in the Balearics is a bit more puzzling. The 3,173 overseas purchasers represented an 11.2% decrease. One reason might be high prices fuelled by lack of supply. In the first half of 2018 overseas buyers in the Balearics paid an average €2,790 per square metre. That's more than double the price paid in the Comunidad Valenciana (€1,304 pm2) and 65% more than in Andalucía (€1,655). Also, Mallorca, the main market of the Balearics, introduced much more restrictive tourist rental laws in 2918. Perhaps these are partly responsible for the fall in overseas buyers.

Who is Buying
Surprise, surprise, it's still the Brits in the lead.In spite of so much negativity on the part of many commentators and market analysts, almost willing the British market to collapse to back-up their argument, it is proving remarkably resilient. I wasn't one of the doom and gloom brigade, I looked at the figures rather than speculate. In the full year after the Brexit referendum there were just 816 fewer UK buyers compared with 2016. The impact on the wider overseas market was zero, given that foreign buyers increased by 12,478 over the same period.

The Ups and Downs
So, I'm not surprised that the 2018 notarial returns show the Brits, as ever, heading the nationality league table. And that's in spite of an exchange rate between some 20% weaker against the Euro since the referendum. And while the overall international sector increased by 5.6% British growth was even higher at 8.8%. In fact, British buyers purchased 7,613 properties in the first half of the year, well ahead of the French who were in 2nd place with 4,211 and 3rd place Germans on 4,138. And the British represented 14.8% of all foreign buyers. In addition, in some regions the British market share was even higher. In Andalucía 28% of foreign buyers were British, 23% in the Comunidad Valenciana and an astonishing 57% in Murcia.

In contrast with the rise in British buyers, both the French and German markets were down, -4.55% and -2.05% respectively. And in growth terms, non-EU numbers outperformed everyone, up 12.27% on the previous year.

Typically, second half-year purchases by international buyers are broadly in line with the first half. As a consequence, doubling up on the first half totals is a good guide to the full year results. Based on these latest notarial returns I predict international buyers for the full year 2018 will be another record. And I'm confident the British will still head the nationality league table by some margin. They have for the last fifty years and if Brexit uncertainty and a lousy exchange rate hasn't put them off I guess nothing will. Once the Brexit dust has settled British buyers will still be the most important group for the overseas property market in Spain.

What's in Demand - Resales v New Build
The appetite for new-build properties seems unstoppable, with contemporary and minimalist architecture at the top of everyone's list. However, the supply side of new apartments and houses has lagged way behind demand since the recovery began. Inevitably, this imbalance has skewed new-build prices, to an extent I believe is unsustainable. New may be nice but is it worth paying double, or even more, per square metre than a resale? I don't believe it is but overseas buyers are doing it. Consequently, I see problems ahead as some of these new-builds start to appear on agents' listings as resales. Sellers will find out they can't ramp up their asking price over and above what the resale market can stand just because they paid an inflated price when they bought. The alternative will be that their property will languish on the market for years.

Lack of Supply
In Q1 - Q3 of 2018, building licence approvals across Spain totalled 75,299 compared with 2017 full year's figure of 80,786. With Q4 results still to come its clear the number of new

builds is growing but only slowly. Therefore, the supply side is unlikely to improve significantly in the short term. And even if building licence numbers suddenly increases in 2019 the inevitable time lag between approval and a project being ready for sale means no immediate improvement. In my view, only a big and sustained increase in the supply of new-build properties will reduce the pressure on prices. However, I can't see that happening in the near future. In my opinion, it's more likely that demand for over-priced new-builds will start to fall. Many aren't that well-located or of particularly high quality and it's hard to justify the asking prices. Already, there are rumours circulating of developers delaying the launch of new phases as sales slow.

Lack of well-priced, top quality properties in prime locations is also a feature of the current resale market. However, available stock is more in balance with demand. And there's no sign that buyers in the resale sector are prepared to pay excessive asking prices. In my experience they are much more likely to walk away than overpay. According to the latest statistics, prices at the end of 2018 were about 7% more than at the end of 2017. I estimate prices have recovered about 25% of what was lost in the crash. However, that still puts prices about 15% - 20% below the previous peak in 2007. Look hard and there are still good deals available. Interestingly, a 2018 report from Tecnocasa, one of the big valuing companies in Spain, suggests asking prices are, on average, about 20% above the eventual price achieved. When over-optimistic sellers reduce asking prices to more in line with what the market can stand, they sell. And in price per square metre terms that will be way below new-builds prices.

The Price Conundrum
Marbella, the sixth most expensive town in Spain, is a good example of the new-build versus resale price conundrum. With thorough research it is still possible to identify well-located properties for between €2,000 and €4,000 per square metre. At the end of 2018 I located a 3 bedroom detached villa front line to one of the coast's best golf courses priced at €2,450 per square metre. It had been on the market for a while at the equivalent of €2,810 per square metre and sold quickly after its reduction for €2,264 psm. That's about 20% below the original asking price so perhaps Tecnocasa is right. I found a larger villa in the same prime area with an asking price equivalent to €3,000. It has also been reduced from a higher asking price.

The fact is that just before prices crashed, buyers in this area were paying between €6,000 and €7,000 per square metre for the very best locations and quality. In the resale sector prices should still be well below those levels to secure a sale. However, buyers are already paying more per square metre than the pre-crash peak just to get their hands on a new property. In some cases the new-build premium is as much as 50% above the equivalent resale price. I've worked in the Spanish property market for many years and been through a few high/low cycles and I can't remember a time with such a discrepancy between new and resale prices.

Building licence approvals will be around 80,000 for the full year. I can't see this improving the supply side in a meaningful way as it will be 2020/1 before these properties are in the sales pipeline. In the meantime, I worry that some buyers are paying such inflated prices for new build properties that they may never see a return on their investment. While I can accept some purchasers don't mind too much about not making a profit I've yet to meet one happy to make a loss.

Rental Yields
There is a close link between rental yields in Spain and the health of the Spanish tourism sector. Currently, Spain is the second most visited country in the world. According to Ministry of Tourism statistics about 35% of Spain's 80m+ tourists do not stay in hotels. Obviously, some will have their own homes, or stay with family and friends, but that leaves a serious number of overseas visitors renting privately. As a result, rental yields make letting a property in Spain an interesting option. And not just for the buy-to-let investor but also as a way to cover a property's running costs. Across the board, top quality, prime located properties were 100% occupied in high season in 2018.

There is high demand for both long and short term rentals. However, it is absolutely essential that the location is the best and the property must be in 5* condition. What used to be considered luxury items, such as free wifi, flat screen t.v. & satellite, high quality interiors and equipment, are now standard requirements. It doesn't have to be a grand detached villa. There is just as much demand for smart two bedroom apartments in the right location.

I thought property price rises would squeeze yields. However, demand is so outstripping supply that doesn't seem to be happening. In general, an apartment or townhouse can achieve 8% gross yield if available for short term lets throughout the year. A similar property let long term can achieve 5%-6%. At the top of the market a detached beachside property can gross 10%+ in the short term market. In all cases, location and interior finishes are key.

Tourism numbers
It seems likely that demand for short-term holiday rentals is only going to increase. Spain's international tourism sector has experienced remarkable growth in the last decade. In 2007 59m overseas visitors was an all-time record but that figure had increased to 81m by the end of 2017. With 73.8m foreign tourists counted between January and October 2018 it seems probable that full-year figures will, once again, top 80m. There are also signs that improved marketing to pitch Spain as a year-round destination is paying off. In 2018 the three winter months, January through March, plus October, showed the biggest monthly increases. This indicates there is improving rental potential throughout the year and not just in the traditional high season summer months

Analysis of the tourism statistics show that the number of foreign tourists declined in both July and August 2018. It seems the loss was the result of the recovery in cheaper package-holiday destinations such as Tunisia, Morocco and Egypt rather than fewer high-end tourists. And the very high demand for the most expensive rental properties seems to bear this out. In fact, I think that Spain has probably come to the end of year-on-year higher tourist numbers for the present and 80m± is the maximum it can accommodate with current infrastructure. The most important thing, in my view, is that there are no losses at the top of the market and that the quality sector grows.

Important for Yields
When I am working for a client whose brief requires reliable rental income I target certain areas and ignore others. In addition, I look for a type of property and reject others. Get the location wrong, even by just a few kilometres and income may be halved. As well as pinpointing the right location in a particular area you need to be in the right region because some have legislated against short term holiday lettings, pressured by the powerful hotel lobby and disgruntled locals. This is particularly true in city centres, such as Barcelona and Madrid, Valencia, Palma and Málaga where tourist lettings have overrun some districts. So, if rental income is a requirement of your buying plan then check the legislation in that autonomous region because there are differences.

Nevertheless, many property owners in Spain like the idea of covering running costs and don't want the property empty for long periods of time. But the days of leaving a set of keys at the local bar and crossing fingers that no emergencies will arise are over. You need to be 'rental ready' and you can read my bog with more information here.

Spanish Fixed Rate Mortgages
It's a fact that the majority of all overseas buyers in Spain since the property crash have been cash-rich. Obviously, the principle reason for this is that Spanish banks were drowning in bad debts and new mortgages were scarce. Only a massive bail-out from the European Central Bank prevented widespread collapse. And even when a foreigner passed the status checks the amount a bank offered dropped from 100% to 60% of the value. As a result the buyer needed a much bigger deposit than previously and overseas buyers who actually needed a mortgage to purchase struggled to get approval.

In contrast, the banks are very keen indeed to lend to international buyers who don't require a mortgage. One of the first questions I ask potential clients is whether they they are cash buyers or if they need finance. I do this because I believe it is better to get an indication of borrowing potential before I start a property search. When the answer comes back that they are cash buyers I always ask if they are aware of the fixed rate mortgages currently available in Spain. Most are not. However, once they knew all my recent clients who had intended to buy with cash have opted to take the maximum they could borrow. The typical response has been 'where do I sign'?

Euribor is the interest rate which fixes the majority of Spanish mortgages and it's been in negative territory since February 2016. It closed 2018 at -0.147%, rising slightly in each of the last 3 months of the year. In the recession fixed rate mortgages disappeared from the market. Now about 40% of all new Spanish mortgages are fixed rate loans. Indeed, the majority of international buyers are opting for fixed rate over variable rate loans. My advice to cash buyers, irrespective of the currency, is to protect their capital and take a Spanish mortgage.

Spoilt for Choice

There are many products to chose from with fixed terms from 5 - 25 years, interest rates from 2.5% and up to 70% LTV. There are a lot of variables, such as country of residency, amount required, location of purchase. However, there are no restrictions on nationality or purchase price. A good broker is essential. Status is scrutinised very carefully but in general the process is straightforward and quick. In the case of some of my clients we have even had banks competing for the business.

Spanish Property Market - Conclusions

In December 2018 the International Monetary Fund issued a warning about early signs of a 'slight overvaluation' in property prices. It noted that Spanish banks are highly exposed to real estate sector developments and may underestimate the speed at which house prices and relaxed lending criteria can gain traction. The IMF was particularly critical of the lack of progress in setting up a monitoring agency. It has been urging Spain to do this for years, ever since the 2008 banking meltdown. The last PP government put this on hold but current PSOE administration is working on legislation to give the Bank of Spain the necessary powers. This same report puts average price rises between 2014 and 2017 in the region of 15% nationally. However, in the prime spots important to the overseas market I would put the increase at closer to 25% in that period.

Also in December 2018, I noted warnings from valuers about the spectre of overvaluations creeping back into the market. Given that most banks currently offer maximum loans of 80% LTV, those without a large deposit are effectively excluded from the market.In reality, it's been more than a tendency, most banks have been ordering valuers to be conservative. The loan is then offered on whichever is lower, the valuation or the property price. Unsurprisingly, it's always the valuation.

So, the IMF comments about 'slight overvaluation' in prices or the possibility of deliberate mortgage overvaluations are a bit worrying. They may be only a warning flag but they may also be the first signs of something more serious. Even more reason then for buyers to be very cautious, particularly in the new-build market. It is essential to do the research and compare asking prices for new property with comparables in the resale sector. Look peak prices prior to the crash and ask yourself if you should be paying even more than that now. Remember that resale prices are still approximately 20% - 25% below that level. Buyers in the new-build sector should be cautious and ignore what an agent friend of mine calls 'candles and cushions' marketing. Lots of soft focus life-style images, very seductive, but better to check the price.

Getting it Right

However, what attracted record numbers of overseas buyers to Spain in 2018 will continue to impact during 2019. If you buy at the right price, Spanish property is still relatively affordable. There's potential for substantial capital growth in the medium term and excellent rental yield potential. But, buying at the right price for the current market is key. In addition, Spain is perceived as a relatively safe and stable country. There's no doubt that Spain's property and tourism markets have benefitted enormously from instability and insecurity elsewhere. Hopefully, that won't change. If it doesn't I predict international buyers will head for Spain in even higher numbers in 2019. The sun continues to shine and the quality of life is rated one of the best in the world. What's not to like?

The lack of high-quality inventory at the right price in prime locations will be an issue throughout 2019. As I've shown in this report the recovery has been restricted to the very prime locations in a handful of regions. As far as the overseas market is concerned that means the Mediterranean coasts, the Balearics and the Canaries. It certainly hasn't been across the board but price rises are now putting pressure on budgets. As a result buyers may struggle to find what they want in their preferred location. Some compromises may be necessary.

My advice to buyers in 2019 is do not obsess about new-builds, especially if not located in prime positions. Many are not. Consider equivalent resales, calculate the price per sq.m. to include any renovation if it's needed. Then you can take an informed view on what makes the best financial sense. The result will almost certainly be a lower price, a bigger property and, most important of all, a superior location. A thorough search can still uncover some real deals although they will be harder to find in 2019. Nevertheless, there will always be some sellers more motivated and realistic than others.

Don't buy anything that is blighted. Roads tend to get busier over time so if it's noisy now it will only get worse. If there is a mobile mast in view assume there will be more as the tendency is for them multiply. Electricity pylons are also a big no-no. We can assume new housing will increase in the medium term. So it's essential to be aware of local planning issues and what might be in the pipeline. Already, in some areas I can count twenty cranes while standing still. If there is vacant land nearby find out with absolute certainty what, if anything, can be constructed. The selling agent saying it is green zone is just not good enough. Why risk losing a fabulous view?

And finally, when I am assessing properties for my clients I always ask the following questions. If circumstances change and they need to sell quickly is the price right to enable them to do that? Secondly, is this a property for which there will always be demand irrespective of market conditions? Without doubt, the shambles of recent years taught us a valuable lesson. And that is that there will always be demand for top quality in prime locations. It always has been, still is and always will be about location.