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Malta's real estate growth vis-à-vis housing affordability

by **Denis H. Camilleri**

MALTA'S real estate growth may be gauged from the value of an average property contract in 1982 which stood at Lm3,766, to that of a property contract in 2004 at Lm38,668. This implies an annual average growth of 10.25% p.a., double the annual growth of the GDP current market price/capita, which over the same period stands at 5.125% p.a.

If one takes a look at the value of properties purchased by foreigners, this stood at Lm12,600 per unit in 1982, while in 2005 the price per unit stood at Lm126,000, a tenfold increase. These property contracts now make up 22.25% of the GDP at current market prices as opposed to 9.75% in 1982.

These findings reinforce the conclusions of the BICC *State of the Construction Industry Report* for 2005 which shows the present healthy state of the construction industry, although possibly not such a safe work environment.

Although the share of this industry to the national GDP is not so apparent, it is in the multiplier effect that this industry is a major pillar to Malta's economy, which over the immediate past economically depressed years, has acted as an anchor to keep our economy aboard, with this feel-good factor around.

This, as also noted on a global level, when the collapse of the world stock markets at the turn of this century did not have a devastating effect, such as what had happened in the Thirties, due to the healthy state of residential home ownership.

Over the past 24 years, from 1982 to 2006, as per Table 1 and Figure 1, affordable house prices have increased by 737%, doubling in price over the initial 10-year period, doubling again in price over the subsequent 10 years and then nearly doubling again in price over the past four years. The affordable house price growth over the past 24 years stands at 8.18% p.a., increasing to 18.4% over the past four years.

Although this double figure growth rate is considered unsustainable, for 2007 a growth rate of 12.5% is being quoted, due to the arrival of low-cost airlines to Malta, together with Malta's probable entry into the Eurozone as from January 1, 2008.

This growth rate is to be compared to the average global house price standing at 8.5% for 2006, with a forecast for a slowdown of the average global housing price growth into 2007.

Figure 1 reflects the affordable Maltese property growth rate over the past 24 years, with an average growth rate over this period of 8.18% p.a. Over the initial five-year period, between 1982 and 1987, this growth rate stood at a low of 5.4% pa. Over the next five years, from 1987 to 1992, this growth rate increased to 10.5%, while for the following five years, from 1992 to 1997, it stood at 8% p.a., easing off to its lowest in the next five years, between 1992 and 1997, to 4.2%. The double figure growth for the immediate past four-year period at 18.4% pa has been noted in Table 1.

The trend line plotted for this period (as per Figure 1) shows that the property market coincided in the initial years 1982-1997, but underperformed for the period 1997-2002 (as outlined in Table 1). Between 2002 and 2006 the property market has overshot the trend line with the actual value for 2006 standing at Lm516/m^2 compared to the expected growth over the past 24 years, which works out at Lm427/m^2. This signifies that currently, first-time buyers are paying 20% more for their residence than their previous counterparts in the initial 20-year period under consideration.

The period 1997-2002 for the lowest growth rate at 4.2% coincided with a conference organised by the Chamber of Architects and Civil engineers in 1999 on "Housing Affordability in Malta", followed by another conference organised by the Housing Authority in 2000 on "Social Housing Now and in the Future", which helped to create an awareness on housing affordability.

Unfortunately this awareness was not carried forward. It was known that EU membership in 2004 would cause a hike in property prices, however, inadequate action was taken, evidenced by the double digit growths referred to over the past four years.

Figure 2 shows that although Fgura, Marsascala, Mosta and San Gwann in the initial years may have been slow

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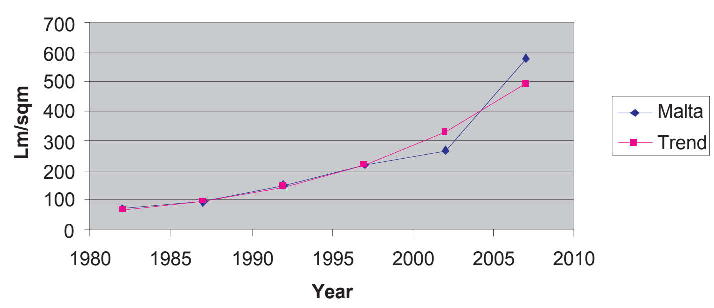
Table 1: Affordable property rates for the Maltese Islands over a 24-year period

Locality (Lm/sqm)	1982 (Lm/sqm)	1987	1992	1997	2002	2003	2004	2005	2006	% growth rate pa 1982 - 2006	% growth rate pa 2002 - 2006
Fgura / Paola / Zabbar	45	55	110	175	200	247	291	327	398.2	9.25%	18%
M'Scala	50	75	160	160	217	258	347	371	443	8.63%	19.60%
Mosta / Naxxar	80	85	125	205	225	279	399	415	493.3	7.89%	21.70%
San Gwann	65	75	110	185	239	286	323	416	537	8.80%	22%
Sliema inner prime	90	145	190	305	379	352	399	565	593	7.40%	14.68%
St. Julians	80	100	175	235	295	311	360	544	535	7.90%	19%
Swieqi	85	105	180	275	337	346	407	454	614	7.90%	15.80%
Malta	**70**	**91**	**150**	**220**	**270**	**297**	**361**	**442**	**516**	**8.18%**	**18.40%**

Source: D.H. Camilleri in-house valuations

Figure 1: Malta affordable property in Lm/sqm over the past 24 years



YEAR	MORTGAGE MONTHLY PAYMENT		MEDIAN FAMILY INCOME**	QUALIFYING MONTHLY INCOME		RATIO OF QUALIFYING FAMILY INCOME		HAI	
	3-bed	2-bed/r		3-bed	2-bed/r	3-bed	2-bed/r	3bed	2bed
1982	Lm60	Lm42	Lm184	Lm240	Lm168	1.3	0.91	77	110
1987	Lm69	Lm49	Lm242	Lm276	Lm196	1.14	0.81	88	123
1992	Lm108	Lm72	Lm320	Lm432	Lm288	1.35	0.90	74	111
1997	Lm165	Lm106	Lm427	Lm660	Lm424	1.55	0.99	65	101
2002	Lm169	Lm113	Lm522	Lm676	Lm454	1.29	0.86	77	116
2004	Lm169	Lm121	Lm605	Lm712	Lm484	1.18	0.80	85	125
2005	Lm215	Lm177	Lm642	Lm752	Lm620	1.17	0.97	85	103
2006	Lm260	Lm184	Lm715	Lm910	Lm644	1.27	0.90	79	111

****The median family income is factored at 1 for 1982, 1.35 for 2002, increasing to 1.5 for 2006 accounting for the second wage earner.**

Source: Updated table in "Housing & Poverty in Malta", D.H. Camilleri BoV Review, Autumn 2000.
A 100 HAI signifies that a family earning the median household income just qualifies for a median residence, while with a HAI of less than 100 signifies that the median family has to do away with other necessities.

Measures to improve affordability

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starters, with all localities picking up over the past four years. Marsascala, Mosta and San Ġwann had a higher annual growth than average (*See Table 1).*

The above average affordable Malta house rate of Lm516/m² is to be compared with upmarket residential developments which presently average out at Lm1,500/m², with the top end in the Lm2,000/m² bracket. Furthermore, the growth rate of these upmarket developments have been subjected to growth rates varying from 15% pa down to 9.5% p.a., compared to the comparable growth rate for affordable properties over the same 24-year period at 8.18% p.a.

These upmarket developments may be compared to similar developments in London at Lm7,500/m², and Dublin and Paris at Lm4,000/m². Madrid, Sydney and Croatia attract the same Malta price tag, Phuket and Cape Town attract half the price, and Bulgaria a quarter of the price.

The Housing Affordability Index (HAI) in Table 2 has been calculated for the period 1982-2004. For a three-bedroomed median apartment the HAI has for 2006 at 79 slid down from the previous two years at 85.

However, 1997 fared the worst with a HAI of 65. For a two-bedroomed median apartment the HAI had increased from 110 (1982) to 125 (2002), however dipping to 103 (2005) and up again to 111 (2006). The HAI index is considered the same in France. Here HAI is taken at 100 in 1992, increasing steadily to 160 in 1999, dipping to 140 by 2003.

The HAI refers to repayments. However the down payment necessary to purchase affordable premises is also to be catered for. For a three-bedroomed apartment this works out at Lm10,000, while for a two-bedroomed apartment this amounts to Lm7,200. These expenses are due to the normal 10% deposit anticipated together with purchase expenses, which include stamp duty and notarial and survey fees.

However, the price earning ratio, prior to double figure annual property growths in 2002 for a median-priced three bedroomed apartment stood at 6, as in 1997, rising to 7.12 in 2006. These ratios are considered high, as a long-term (35 years) average level of house prices to incomes ratio is about 3.5.

However, the HAI did not worsen over the past years as the increase in property prices has been mitigated by lower mortgage rates and a longer repayment term. Truly, knowingly or unknowingly it has been the banks that over this 24-year period have kept the HAI hovering around 65-88 for a three-bedroomed apartment and 101-125 for a two-bedroomed apartment.

The Central Bank's discount rate stood at 6% in the early Eighties, dipping to 3% 18 months ago, to presently stand at 3.75%. On the other hand, private banks have extended the Eighties/early Nineties' 25-year repayment term to the present 40-year term.

Considering the present global Central Bank discount rates, the US Fed rate has increased from one to 5.25%, with 17 straight quarter-percentage point increases over the past 30 months, with the latest hit being June, 2006. The European Central Bank, although initially treading cautiously and keeping its rate at 2% for an extended period, has similarly increased its discount rate from 2 to 3.5% with six interest changes over this year.

What further increases are in store? Does Malta's entry into the ERM signify that a reduction in local mortgage rates could be a possibility? Prospective buyers are to consider that a 75 basis points increase in the discount rate signifies a 10% increase in mortgage repayments or approximately a 3.5% increase for every 25 basis points increase.

The quality and cost of the accommodation to be purchased is to be gauged, bearing these possible increases in the repayment costs over the years. All this also needs to be considered against the median wage increase, which over the past for years averaged out at 3.2% p.a., as opposed to 4% p.a. for the past 10-year period.

Although the real estate market has been bullish these past years and is expected to remain so for some time, a weakening of the affordability for first buyers is expected. This is because now the banks' measures in sustaining the decrease of affordability over the past years no longer appear to be viable in the coming years. This is due to expected increases in lending rates, while the repayment period cannot be extended much further, unless it is to be expected that our children will also be burdened with our repayments.

The various subsidy schemes presently in place need to be reinforced with other measures.

The Housing Authority should step up its annual sale of apartments, which has averaged out at 200 units per annum for the past 10 years. Also the 30% reduction in market price offered is to be revisited, as the affordable house (as seen), is presently selling at a 20% surplus over the past 24-year period selling rate. This signifies that the present cost to the authority is of a lower proportion of the total sale proceeds than previously.

The present stamp duty purchase charge for a first-time buyer has to be downsized to under 1%, with this rate being applicable for properties up to the Lm60,000 mark and revised periodically according to the affordability index. The present reduced rate of 3.5% instead of the 5% stamp duty on properties costing less than Lm30,000 still imposes a great strain on the down payment to be made before to the initiation of the bank's mortgage monthly payments.

The Estate Agents Association has to introduce a social scheme whereby sale services to first-time buyers are offered at a subsidised rate, closer to the 1-2% range. This could signify a saving of Lm2,500 for an affordable three-bedroomed apartment and Lm1,500 for a two-bedroomed one.

Initiatives should be handed out to present owners of vacant property for these to be released onto the market. Findings of the 2005 census are awaited as it is probable that the proportion of vacant properties has surpassed 23% of the market as listed in the 1995 census.

Finally the long-awaited rental amendments,[1,2] should help a couple to decide what is better in their particular circumstance, whether to purchase or rent their home.

The possibility of renting out by Maltese couples would create another market, being of financial benefit to both owners of presently vacant property, and also to tenants who are given the opportunity to live a better life. This is due to the fact that rentals hover around the 3.25-3.75%[3] of the market value, which is presently less than mortgage rates, with further no down-payment necessary for rentals. The downside of renting out is that couples do not participate in the capital growth of their homes.

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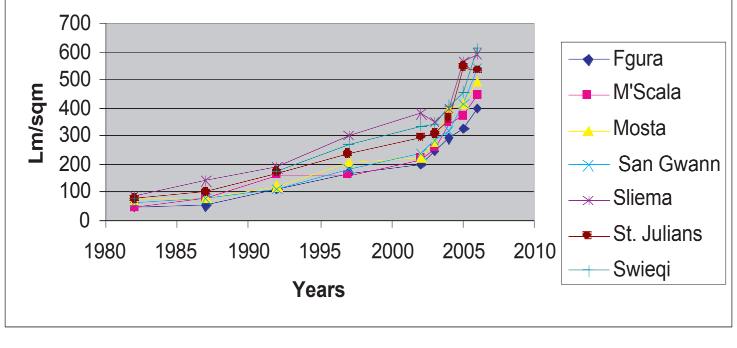
Figure 2: Property market rates in Lm/sqm for various localities over a 24-year period



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