

Chapter 4

The Spanish housing market: recent changes, risks and affordability problems

Robust housing demand, along with relative supply rigidity, has caused sustained growth in purchase and rent prices since 2014

- Housing purchases are remarkably robust, despite the slowdown observed since 2022 Q4, against a favourable macroeconomic backdrop and tighter financial conditions since early 2022.
- Demographic growth is a key factor in explaining the strong demand for both owner-occupied and rental residential housing.
- This population growth is largely explained by significant net external migration, which has intensified since 2022.
- Net household formation is concentrated in certain regions and in the main urban areas, where the highest house price and rent increases have been observed.
- The increase in the demand for a main residence has been accompanied by the strength of demand from non-residents, whether for owner-occupied or rental (but mainly holiday) housing.
- Recourse to mortgage financing for purchases has declined since the start of monetary tightening, although the number of new residential mortgages was higher in 2023 than in 2019.
- Banks seem to have maintained prudent credit standards when extending mortgage loans, thus avoiding the build-up of imbalances such as those that led to the 2008-2013 real estate and banking crisis.
- Prudent credit allocation in recent years, along with house price and labour market dynamics, have contributed to a notable shift in housing demand among the lower-income groups towards a rental market that is relatively small in the context of the EU-27.
- Despite the significant increase in the privately owned rental supply, it seems to have been insufficient to absorb the strength of demand, with a low proportion of professional agents and social rentals.
- The contribution of new housing to aggregate supply has been limited, owing to, among other factors, construction workforce shortages, rising production costs and a lack of investment to acquire and develop new urban land available for construction.
- Residential housing supply rigidity is also explained by the low house renovation capacity, empty houses not matching current household preferences, regulatory uncertainty and the rise of alternative housing uses, such as holiday or seasonal rentals.
- The lacklustre housing supply in the recent period, compared with the robustness of demand, has significantly underpinned house purchase and rental price growth.
- However, cumulative growth is uneven and stronger in new housing, large urban areas and tourist areas.

Despite the notable dynamism of residential housing market activity, the vulnerabilities and risks to financial stability associated with this market are contained

- There are no indications of the real estate market becoming oversized. The share of the construction sector in total employment and the ratio of residential investment to GDP are low by historical standards.
- Nor have any warning signs been observed in relation to the credit market. In general, credit standards related to collateral and maturity are at prudent levels.

- Indicators of loan repayment capacity based on borrower income also stand at prudent levels, although some deterioration has been observed in the most recent period.
- The latest data (for 2023 Q4), suggest that the average house price valuation indicator stands close to the equilibrium level.

Housing affordability difficulties have become more pronounced over the last few years, particularly for certain types of households and in certain geographical areas

- By cohorts, housing affordability poses greater challenges for lower-income households and those with scant saving capacity, groups that include a high proportion of young people and foreign residents.
- The housing affordability difficulties owe to property prices rising faster than these cohorts' income, which tends to be subject to more uncertainty due to their labour market situation.
- By geographical area, the difficulties are most acute in areas that are more economically buoyant and those with higher levels of tourism.
- The proportion of mortgaged households overburdened by their housing costs is low.
- The lesser burden on mortgaged households appears to reflect, at least in part, sound selective lending by banks, which only extend credit to households that have sufficient savings and income relative to the price of the property.
- By contrast, the percentage of renter households that are overburdened by their housing costs is very high, above the EU-27 average.
- Lower-income households, which cannot afford home ownership, face high rental costs relative to property prices. This partly owes to problems in the functioning of this market.

The adverse social and economic consequences of these difficulties warrant the adoption of economic policy measures geared to correct them

- Housing cost overburdening limits households' ability to save and may influence not only their consumption and investment decisions but also their decisions on where to live, whether to have children and whether to continue their education.
- In consequence, housing affordability problems may have both short and long-term negative implications and may give rise to lower aggregate productivity and lower economic growth.
- Considering the scale of the problem diagnosed here, it seems unlikely that isolated short-term actions may be sufficient to significantly reduce today's housing affordability difficulties.
- At the same time, public policies should be designed to ensure that actions that may have relatively limited effectiveness in the short term do not ultimately have significant unwanted effects that hinder the functioning of this market in the medium and long term.
- Insofar as today's housing affordability problems are the result of imbalances that have built up over many years, they must be addressed via a combination of multiple structural policies in different areas.
- In particular, the measures adopted should:
 - envisage a broad time horizon for design, implementation and evaluation of the public policies;
 - involve all the various tiers of government with responsibility for housing, in a coordinated manner and in collaboration with private initiatives;

- focus, in particular, on stimulating housing supply, especially in the rental market and social rentals, prioritising allocation of the available resources to the most vulnerable groups; and
- consider other aspects that affect the housing market, such as those relating to the functioning of the labour market, the strength of economic productivity and tax and transport policies.