Housing slump hits Spain

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The clearest indication of the impact of the global credit crunch is the sharp slowdown in the housing sector. The housing slump in Spain is particularly sharp.

There are now very few areas in the country where you cannot see new building developments filled with banners displaying the phone numbers of people desperate to sell them. In the capital Madrid, buildings are littered with “For Sale” signs. Hardly a day goes by without stories appearing in the media of developers abandoning half-finished apartment buildings and leaving buyers with the terrible prospect of never seeing their homes finished. Growing numbers of borrowers are missing mortgage payments for the first time and figures have doubled from last year.

Many of the workers to first feel the consequences of the housing slump have been poorly paid immigrants who flocked to Spain from North Africa, Eastern Europe, and Latin America to find work during the construction boom. Pavel Santa, a Romanian construction foreman who came to Spain with his wife and works for a management committee of a property company, recently had his mortgage interest rate reset, causing the monthly payment to take up almost all of his 1,800 euros monthly salary. “I’m at the limit,” Santa told bloomberg.com. “I live worse than I did in Romania.”

The output from Spain’s construction sector decreased by 8 percent in 2007, the largest fall recorded in the European Union. The number of companies filing for bankruptcy rose by a huge 87 percent in the last quarter of 2007, compared with the same period in 2006, and several high-profile construction companies have gone bust in recent months laying off tens of thousands of workers. The trade group, G14, which speaks for Spain’s largest developers, predicts that over one million residential and commercial construction jobs could be lost. Unemployment already stands at nearly ten percent of the working population and has increased for five consecutive months.

The most recent International Monetary Fund forecast suggests economic growth will fall from 3.8 percent last year to 1.8 percent this year—one of the biggest drops among developed nations, and that inflation will rise to 4 percent. The country’s current account deficit is the second highest in the industrialised world, after the United States, at 9.5 percent of GDP. Last year’s sale of 80 tonnes of gold by the Bank of Spain was widely seen as an attempt to finance the deficit, but it now means the bank’s reserves are just €13 billion, equal to 12 days of imports.

With interest rates at historic lows over the past few years, and returns on investments in the stock market declining with the bursting of the dot-com bubble, large and small investors poured money into the real estate market to the point where an unprecedented 18.5 percent of the Spanish economy became housing related. This market was fuelled by cheap credit, low wages for migrant workers in construction, and in many cases, outright fraud, and corruption.

House prices in Spain are overpriced and are set to drop for the next three years. In January the number of house sales dropped by 27 percent compared with last year and the number of mortgage deals fell by 25 percent.

In 2007, 32,000 real estate agencies—just over 40 percent of Spain’s total—shut down for good. Fernando Encinar, a director of Spain’s leading online estate agent, idealista.com told the *International Herald Tribune*, “We have to accept this is not a gentle correction, but a full-blown crisis. We can only hope it will be sharp and short.” Mikel Echavarren, CEO of Madrid-based real estate consulting firm Irea added, “This talk of a ‘slowdown’ makes me laugh. First, they talked about a ‘soft landing.’ Then it was a ‘slowdown.’ Those are deceptive terms. We are in a serious crisis."

Many real estate groups are coming under pressure to write down the value of assets on their books. The Bank of Spain has asked banks to set aside more money against loans made to builders and real estate developers. Increasing numbers of bankers are making public their fears that in the current financial climate many mortgages taken out in the last 10 years will not be paid back. "This puts fear among a number of banks who rely on the construction sector", said the president of Caja Madrid, Miguel Blesa, one of the largest savings banks in Spain.

Consumer confidence is at record lows, with the official Credit Institute index for March standing at 74—well below the 100 mark which "separates pessimism from optimism". Spain is a real disaster," said Marco Valli at investment bank UniCredit MIB. "The housing downturn is spilling over very quickly to all other sectors, helped by the surge in inflation that dampens purchasing power at a time in which consumer confidence drops due to the weakening labour market and economic outlook."

Spain has one of the highest budget surpluses in the industrialised world and government ministers and officials have played up this fact to say the country is better positioned to weather the financial storm. Prime Minister Jos(Luis Zapatero of the ruling Spanish Socialist Workers Party (PSOE) promised during the recent election campaign, "We've saved, we've managed our finances well and we've got a bigger surplus than expected, so we can stimulate the economy and help families."

The €20 billion surplus will be cut by almost half this year, according to official forecasts and fall even further next year, if the government carries out its election promises. These include an annual income tax rebate of €400, mortgage relief, an increase in the lowest state pensions by 26 percent and a public works programme aimed at building 150,000 affordable homes a year. The government has also promised to invest in major road and rail building programmes, such as the high-speed rail link between Madrid and the regions.

Even so, according to Antonio Argandoña, professor of economics at the Navarra University IESE Business School as reported in the *Christian Science Monitor*, these measures will only have a limited effect. "The tax rebate is a temporary aid; it will only help for one trimester. And extending mortgage terms may help families who already have loans, but it's going to impede access to new credit, since the banks aren't going to be as interested."

"The problem lies not so much with the measures themselves, but with the nature of the crisis. They can create more public works, but that takes time. Governments just don't have the tools to stop this kind of decline. Indeed, it is likely that the worst is still to come. 2009 is the year the bad news spreads to other industries. We're not going to touch bottom until 2012," Argandoña concluded.

These sorts of pronouncements have been followed by demands for the Socialist Party government to start attacking "outmoded labour practices" and "lack of flexibility" in Spain's labour market, which many economists blame for Spain's low productivity. Under current Spanish law, for example, workers on permanent contracts are protected by high severance payments compared to elsewhere in Europe.

Attacks levelled against Spain's working class are a minefield, in a country that is already deeply polarised and plagued by growing social inequality. The report *Spain: Going Places* reveals that among the 30 OECD countries, Spain was the only one where growth in real average wages has declined since 1995. They rose 1.9 percent a year between 1990 and 1995 and then declined 0.5 percent a year in 1995-2000 and 0.3 percent in 2000-2005. This was mainly due to the creation of a huge number of jobs that were part time or temporary contracts.

Over the same period, the ruling elite have massively increased their wealth at the expense of the working class. Another recent report, *Spain Enters the Millionaire's Club*, reveals that Spain has joined the "select club" of 10 countries with the most millionaires in terms of liquid financial assets. Their number grew by 5.7 percent in 2005, the second-fastest pace in the European Union, to 148,600 people.