

A Note on the demand side of the construction and real estate industry

Mario Borg
CEO

Gozo Regional Development Authority

The last few years witnessed a marked increase in the level of awareness around Gozo urgent need for an integrated system where land use, planning and sectorial policies are in synergy with Gozo characteristics. Activities associated with construction and real estate top many policy discussions as they have a high impact on the way Gozo looks – both now and in the future.

This short note looks at recent growth in the real estate industry, with a focus on Gozo, from the demand side. This is done without trying to underestimate the regulatory dimension which is at least equally important.

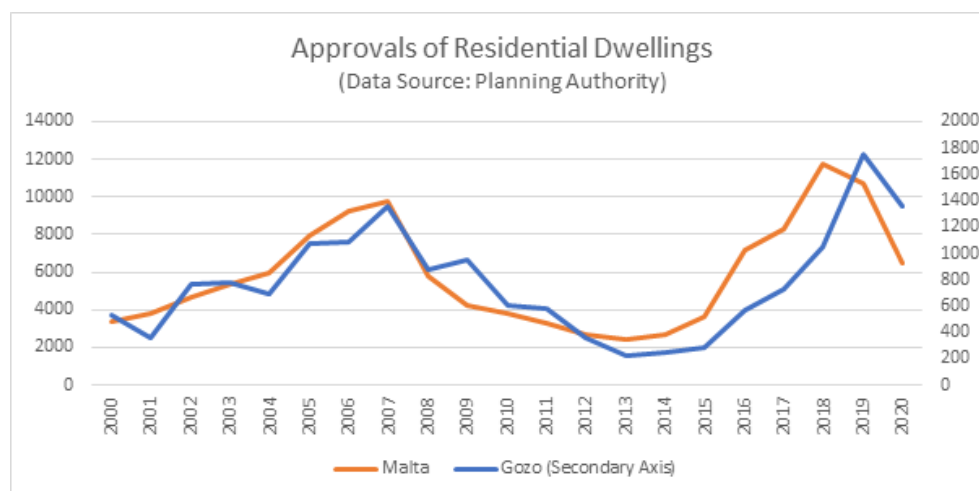
A Few Observations from Recent Trends

Data from the Planning Authority on approval of residential dwellings confirms the somehow cyclical nature of the industry reflecting several macroeconomic and social developments including perceived risk and rewards factors and demand spurred by demographic shifts. Regulatory changes, namely the increase in ODZ in 2006 and the increase in height limitations in 2006 definitively played a major role from the supply side, however as highlighted above these are out-of-scope with regards this rate.

A visual inspection of the number of approved residential dwellings shows 2007 and 2019 as the respective peak years in the two cycles. The increase in applications during the 2016-2020 period was much more accentuated than during the previous cycle that is the 2004-2009 period. In 2007, the magnitude of residential dwelling applications was 1.76 times higher than the underlying average trend. This strong momentum was surpassed in 2019, when 1,750 dwelling applications were submitted in Gozo, equivalent to 2.26 the average number of applications. A deceleration in the magnitude of applications appears to be currently underway both in Malta and in Gozo.

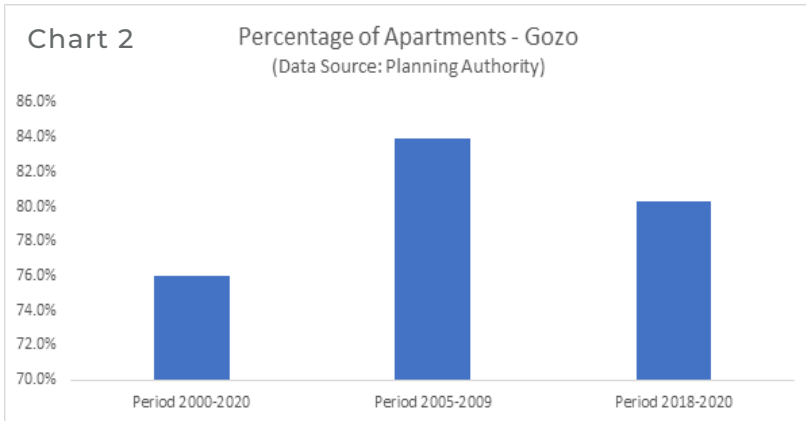
Data also confirm that although trends in residential dwelling applications in Malta and Gozo are correlated, the two islands tend to exhibit a degree of differentiation with the trend in Gozo tending to follow that in Malta with a lag of 2 years.

Chart 1



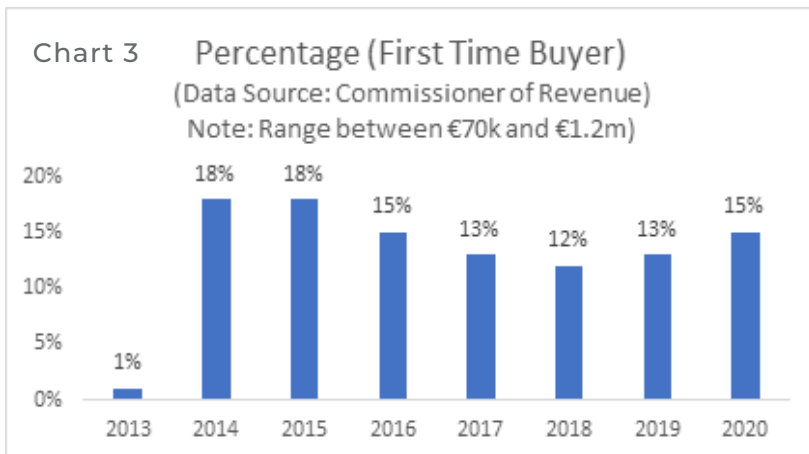
A Look at Some Underpinning Factors

The 2007 census outlines that Gozo has a population of 31,000 individuals, equivalent to 7.7 percent of the aggregate population. However, for most of the period under review the degree of residential dwelling applications in Gozo was considerably higher than what the proportion of the island's population would lead one to expect.



This fact is further put into perspective by the fact that circa 80 percent of all residential dwelling applications are for apartments. Of interest is the fact that the high share of apartments has remained quite constant over the years and does not appear to exhibit any meaningful change during boom years.

Figures on registered contracts from the Commissioner for Revenue shows that the number of First-Time-Buyers (FTBs) in Gozo is relatively low and stable at around the 14 percent level reflecting the fact a segment of the property demand in Gozo is attributable to individuals seeking a second property on the island as a summer residence / vacation home or as an investment property to tap into the rental market.

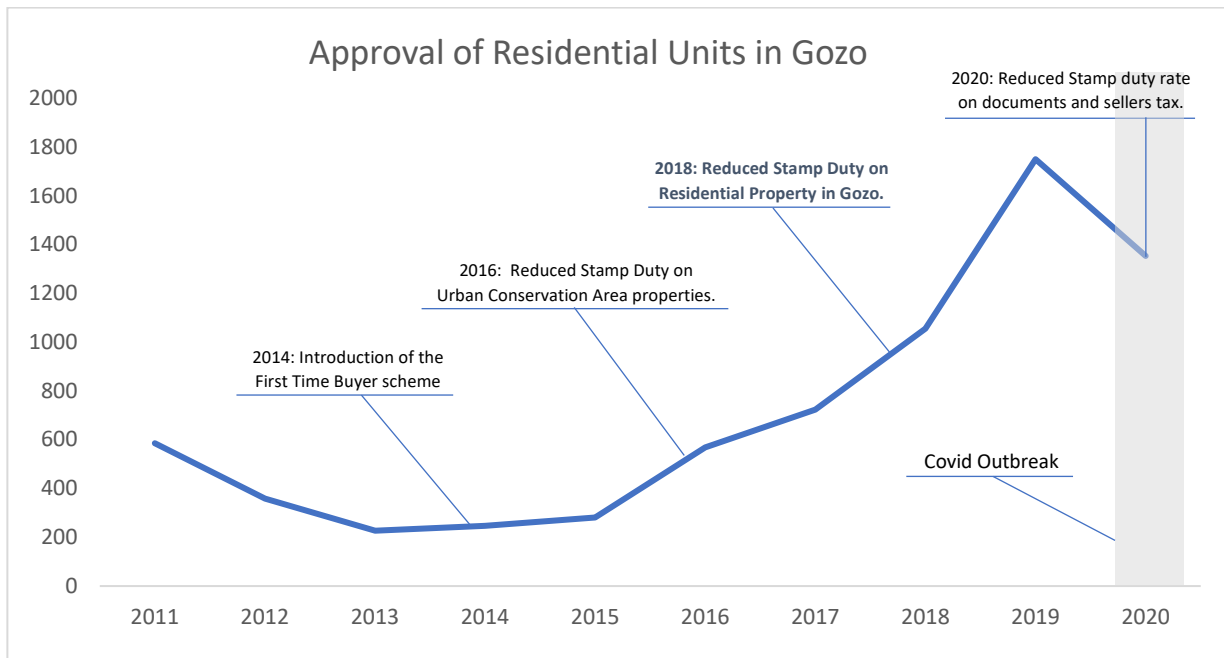


In terms of price dynamics, the same data sources reveal an interesting fact. That while over the 2013-2020 period, property prices published by NSO show an increase of over 40 percent, a simple average of figures based on contracts indicates an increase of just 12 percent over the same period. This points towards smaller units entering the market over time.

Timeline of Measures taken over the Years: A Case of encouraging demand

The construction and real estate have a very high multiplier. Many other activities depend on it and during the last few decades has always been regarded as a main driver of the real economy. The Government intervened several times to simulate the industry which include incentives related to restoration and conservation works of scheduled buildings in grades 1 and 2, as well as properties in Urban Conservation Areas, the introduction of the First Time Buyer scheme in 31st December 2014, a scheme whereby stamp duty on residential property in Gozo was reduced from 5 per

cent to 2 per cent, and finally in June 2020 as part of the Recovery Plan a further reduction of duty on documents from 5 percent to 1.5 percent with sellers having their tax cut from 8 percent to 5 percent. The measures mostly in the form of fiscal incentives, both fueled and sustained the momentum in the industry over the years. Of interest is the timing of the 2018 scheme which reduced stamp duty to 2 percent.



Summary Observations and Suggestions

Based on the above factors, the following observations can be summarized:

1. Although trends in residential dwelling applications in Malta and Gozo tend to be correlated, the two islands tend to exhibit a degree of differentiation. A key feature which emerges from the data is that the momentum of new applications in Gozo tends to follow trends in Malta with a lag of 2 years.
2. A very high percentage of all residential dwelling applications are for apartment.
3. First-Time-Buyers (FTBs) in Gozo is relatively low and stable at around the 14% level.
4. Real Estate market in Gozo becoming increasing characterized by small unit.

Suggestions:

1. The incentive for the purchase of property in Gozo in effect as from 2018 whereby, individuals benefit from a reduction in stamp duty, from 5 per cent to 2 per cent should be stopped.
2. Discriminate between type of properties with small units being subjected to either to higher stamp duty and/or higher subjected to additional fees.
3. Increase the minimum floor area to disincentivize the construction of small units.