

GRDA NOTE



The demand side of the
Construction and
Real Estate Industry

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A Note on the demand side of the Construction and Real Estate Industry

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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 underplay the regulatory dimension which is at least equally important.

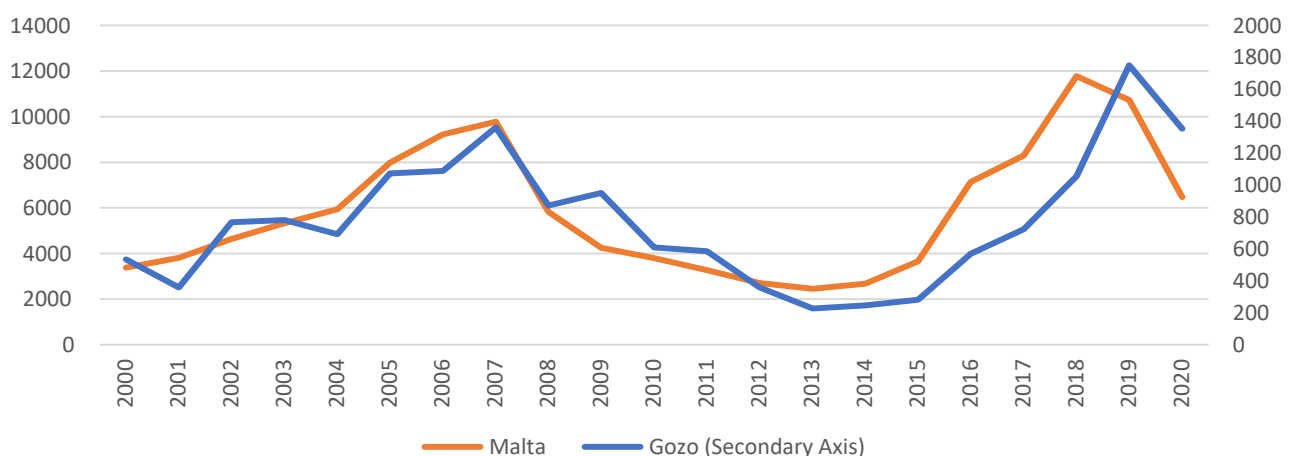
A Few Observations from Recent Trends

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 underpinned by demographic shifts. Regulatory changes, namely the increase in ODZ in 2006 and the increase in height limitations in 2016 definitively played a major role from the supply side, however as highlighted above these are out of scope with regards this note.

Chart 1

Approvals of Residential Dwellings

(Data Source: Planning Authority)



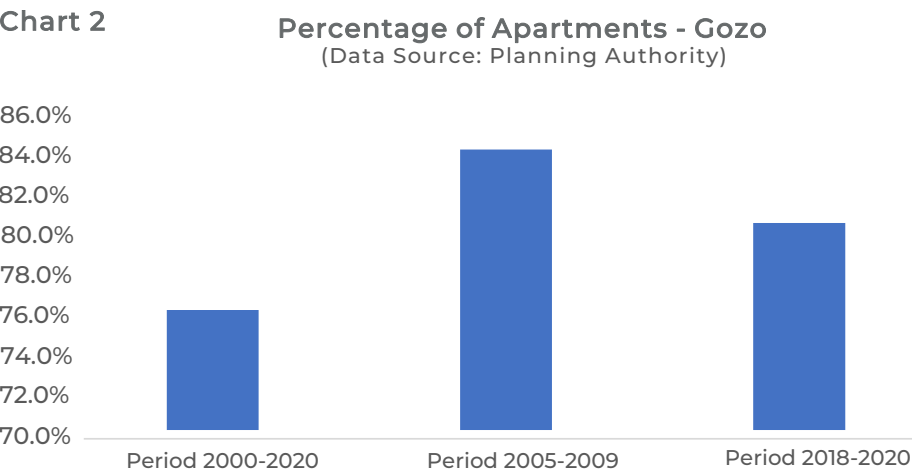
A visual inspection of the number of approved residential dwellings shows 2007 and 2019 as the respective peak years in the two cycles. The increase in applications during the 2016-2020 period was much more accentuated than during the previous cycle. In 2007, the magnitude of residential dwelling applications 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 underway, however the numbers remain high.

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.

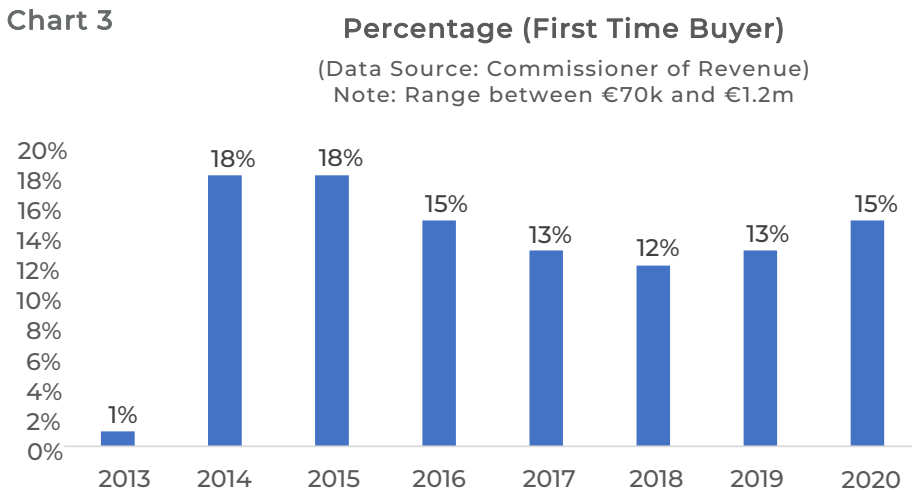
A Look at Some Underpinning Factors

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 all of residential dwelling applications are for apartments. Of interest is the fact that the high share of has quite the apartments remained constant over 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 TimeBuyers (FTBs) in Gozo is relatively low and stable at around the 14 percent level reflecting the fact a high level 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 and possible price appreciation.

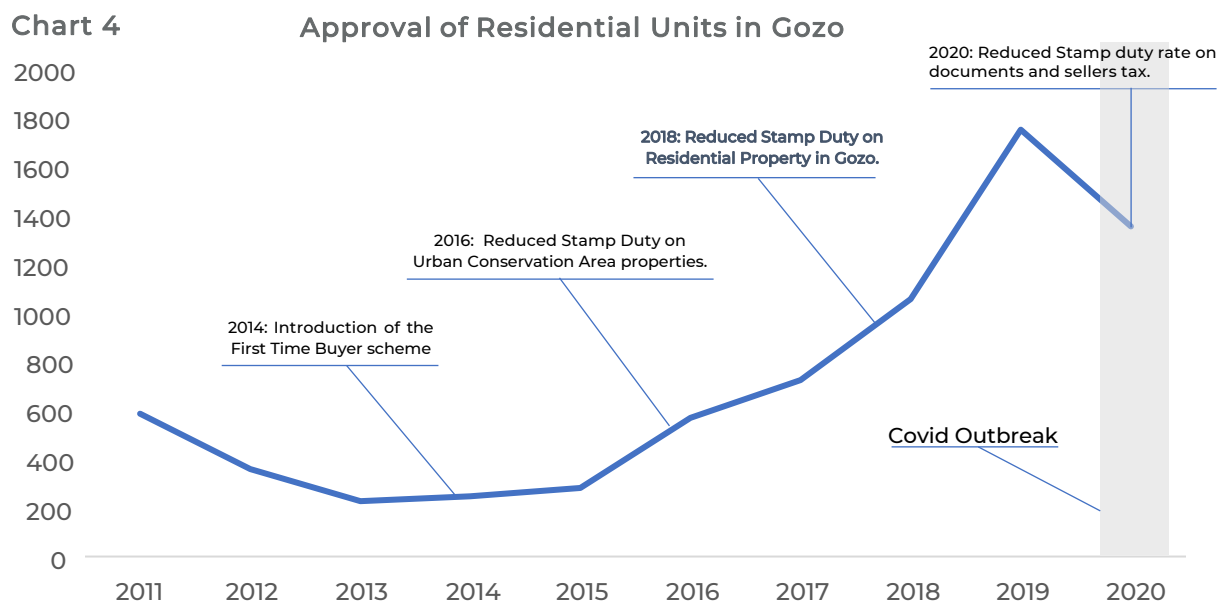


In terms of price dynamics, the same data sources reveal an interesting fact. That while over the 2013-2020 period, property prices published by NSO show an increase of over 40 percent, a simple average of figures based on contracts indicates an

increase of just 12 percent over the same period. This points towards smaller units and possibly of lower quality, 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 as a result has always been regarded as a main driver of the real economy. Government intervened several times to simulate demand in the industry which include incentives related to restoration and conservation works of scheduled buildings in grades 1 and 2, and in Urban Conservation Areas; the introduction of the First Time Buyer scheme on 31st December 2014, and a scheme whereby stamp duty on residential property in Gozo was reduced from 5 per cent to 2 per cent. 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 was also announced. The fiscal measures both fueled and sustained the momentum in the industry over the years.



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.
2. A very high percentage of all residential dwelling applications in Gozo are for apartments.
3. First-Time-Buyers (FTBs) in Gozo is relatively low and stable at around the 14% level.
4. Real Estate market in Gozo becoming increasingly characterized by small unit and potentially of lower quality.

In view of the fact that there is wide acceptance that investment in Gozo in real estate should be encouraged to be sustainable and hence incentives must address quality, the following suggestions are proposed:

1. The incentive for the purchase of property in Gozo in effect as from 2018 whereby, individuals benefit from an overall 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 higher stamp duty and/or additional fees.
3. The minimum floor area should be increased to disincentivize the construction of small units.
4. An assessment to explore ways how to internalise costs should be undertaken so prices of properties reflect 'fully' the cost to society.

The GRDA is currently working on a study to seek to understand the main supply and demand dynamics that have occurred in the real estate in Gozo over the last decade. This note is based on preliminary results.



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