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Housing Market Slump `Unthinkable' in Spain, Government Says

By Ben Sills

Sept. 18 (Bloomberg) -- A residential real estate slump in Spain, where prices have almost tripled since 1997, is ``unthinkable,'' the top economic adviser of Prime Minister Jose Luis Rodriguez Zapatero said.

The solvency of the banking system and of real estate developers, as well as the unmet demand for new homes, will prevent any meaningful price erosion, David Taguas, head of the prime minister's economic research unit, said in an interview yesterday at his office at the presidential palace in Madrid.

``To talk about severe adjustments or a meltdown in prices is ridiculous,'' Taguas said in response to reports pointing to an end of the Spanish real estate boom. ``That sort of crisis is unthinkable.''

The gains in housing prices are already slowing and excess supply may lead to a decline in prices, predicted Gonzalo Bernardos, an economics professor at the University of Barcelona, who expects a 20 percent drop by 2009. Home prices rose 5.8 percent in the second quarter from the year earlier period, the smallest increase in at least three years.

The Spanish banking system is also solid enough to withstand rising financing costs triggered by the fallout from the surge in defaults in the U.S. subprime mortgage market. A run on mortgage-lenders such as Newcastle, U.K.-based Northern Rock Plc or funding difficulties like those at Countrywide Financial Corp. in the U.S. are ``unthinkable'' in Spain, Taguas said.

Insurance Against Turbulence

Such a situation ``is completely out of the question'' in Spain, Taguas said. ``We have the good fortune to have one of the most efficient financial systems in the world. That's insurance in times of turbulence.''

For now the biggest threat to the housing market comes from excess supply. About 700,000 new housing units will go on sale this year, 300,000 more than projected demand, says Fernando Rodriguez de Acuna, president of R. R. de Acuna & Asociados, a real estate research firm in Madrid.

Taguas, who estimates demand for new homes at around 500,000 a year, argues that supply will likely contract, averting a decline in prices. Home starts already dropped 21 percent in May.

Rising interest rates have pushed home prices beyond the reach of many Spaniards.

The European Central Bank has doubled its benchmark rate to 4 percent since December 2005 as the European economy posted its biggest expansion since 2000. The fall-out from the U.S. subprime mortgage market rout is exacerbating the increase in borrowing costs pushing up wholesale financing rates, to which many Spanish mortgages are benchmarked. More than 90 percent of Spanish mortgages are variable-rate loans linked to money market rates.

Still housing demand has been sustained by an economic expansion that has outpaced that of the euro region for more than a decade. The European Commission predicted on Sept. 11 that the Spanish economy will grow 3.7 percent this year compared with the 2.5 percent rate in the euro region.

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