BBVA | RESEARCH

Real Estate Outlook

2015
Colombia Unit

- Our analysis of the housing market's structural conditions shows that the market has great potential. Demand continues to be driven by the increase in household incomes and the shortage of housing. Compared to similar countries, supply is low
- We estimate that residential investment will grow by an annual average of 5.5% in 2015 and 2016, thanks to the long-term momentum of social housing. High-value housing will recover at the end of 2015, while non-residential buildings will make their biggest contribution to growth at the beginning of this year
- Prices in large cities will continue to moderate because of the ending of subsidies to the middle classes and lower demand, in an environment of more subdued GDP growth. This will lead to a renewed increase in the capacity of households to buy homes
- Mortgage lending remains dynamic thanks to low interest rates. We expect an increase in the transactions involving existing housing, which will partly offset lower borrowing for new, high-value housing

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1 Summary

An analysis of the housing market's structural conditions reveals the sector's high potential. The shortage of housing continues, although it is less severe than forecast ten years ago. Households increased their incomes and many made the jump to the middle classes. A large proportion of the high-income population does not own a home. Women have taken a greater share of the labour market, gradually closing the wage gap with men. Nevertheless, the standard of housing construction is still low when compared with similar countries. In addition, there is scope to increase the supply of non-residential buildings, such as offices, commercial premises and warehouses, because of their still-low penetration, the country's higher income and expectations of further opening to foreign trade.

In order to increase construction rates, we need, inter alia, good Territorial Planning Programmes (TPPs) around the country. The most recent TPPs have focused on urban renewal, high-rise building and providing public services.

The value of housing sales in Colombia is close to COP26trn (vs. COP24.5trn in 2013), of which COP8.8trn is in Bogotá (COP5.9trn) and its surrounding municipalities (COP2.9trn). Medellín occupies second place, despite its lower building activity and the moderation in sales prices there, and Cali has won back the third position, although it is only just higher than Bucaramanga.

According to La Galería Inmobiliaria (*a Colombian real estate analysis company),* **total sales grew last year by 4.5% annually (YoY)**, but if we exclude housing in the VIPA social housing programme, then we would see a 9.2% fall over the same period. **According to Camacol** (the construction guild) **total sales grew by 7.0% in 2014.** The differences are explained by the cities tracked by each institution. On both measures, social housing is clearly in the lead.

The building sector grew by 11.4% in 2013 and slowed to a rate of 7.8% a year in the first nine months of 2014. The slowdown was accounted for by the bigger stake taken by social housing (VIS in the Spanish acronym). **At the end of 2014 behaviour started to change,** heralding a shift in the trend, and one towards high-value housing supply. **The new momentum has a tailwind from the relative equilibrium between residential supply and demand**, partly as a result of the moderation in social housing projects, but also because of the smaller high-value projects (in Medellín, in particular). **The fact that unsold housing stock remains low is a good sign.**

It took longer to sell new housing in 2014. Taking 2013's average sales, existing inventory at the end of the year could have sold in 6.9 months. In 2014 the average time was 7.6 months.

After the robust increase in non-residential building permits at the end of 2013 and the beginning of 2014, a healthy adjustment is taking place. However, the lag between permits and building suggests that the slowdown in the sector will not be visible until the end of 2015. The rise in office supply resulted in projects being sold more slowly. By contrast, turnaround times were down for commercial premises thanks to stronger sales, and for warehouses because of lower supply.

Existing housing stock has been selling faster. Even so, this year a high volume of existing housing will continue to come onto the market. This is due to the delivery of homes that were bought off-plan, which is very widespread in the Caribbean region and, to a lesser extent, in Bogotá.

In general, social housing will provide the momentum, with a temporary boost from non-residential construction (in the first part of 2015) **and in high-value housing** (from the end of 2015). The government plans an investment of COP8trn over four years, between 2015 and 2018, and will drive the building of around 400,000 social homes in all through its programmes. Altogether, **we estimate that residential investment will grow by an average of 5.5% YoY in 2015 and 2016,** thanks to the permanent support of social housing. High-value housing will make a comeback at the end of 2015, while non-residential buildings will make their biggest contribution at the beginning of the year.

The moderation in housing prices in urban centres is opportune. In the third quarter of 2014, real housing prices (discounting inflation) grew by a national average of 6.2% YoY, down from the 2013 average of 8.5%.

Measurements of accessibility to housing showed that household purchasing power increased in 2014. For the first time since 2010, the time it takes for an average-income family to buy an averagely priced home in Colombia did not rise. Furthermore, **the price of the first mortgage down-payment, as a percentage of household income, remained the same, at 26%.**

Our outlook for 2015 is for greater moderation in the growth of housing prices. This is connected to a lower demand for new subsidised housing at middling prices. It is also related to the lower demand for higher value housing in a context of slower economic growth and a marginal increase in unemployment.

Mortgage credit remains dynamic. The low interest rates have supported the financial system's ability to originate mortgage loans. Mortgage credit continues to win share in the economy and now stands at 6.3% of GDP (including securitisations and housing leasing). **The financial system has increased its credit for existing housing considerably since 2010.**

Over the course of 2015, we expect the number of property transactions involving existing housing to rise, and with them their total credit volumes. On the contrary, there may be a slowdown in borrowing for new, high-value homes, which will not be fully offset by the greater borrowing demand for the social housing projects developed by the government. Altogether, we expect the mortgage credit balance to continue its double-digit growth, but at rates closer to 10% than to 20%.

2 Current structure of the real estate market in Colombia

The housing shortage is less acute, but high unmet demand remains

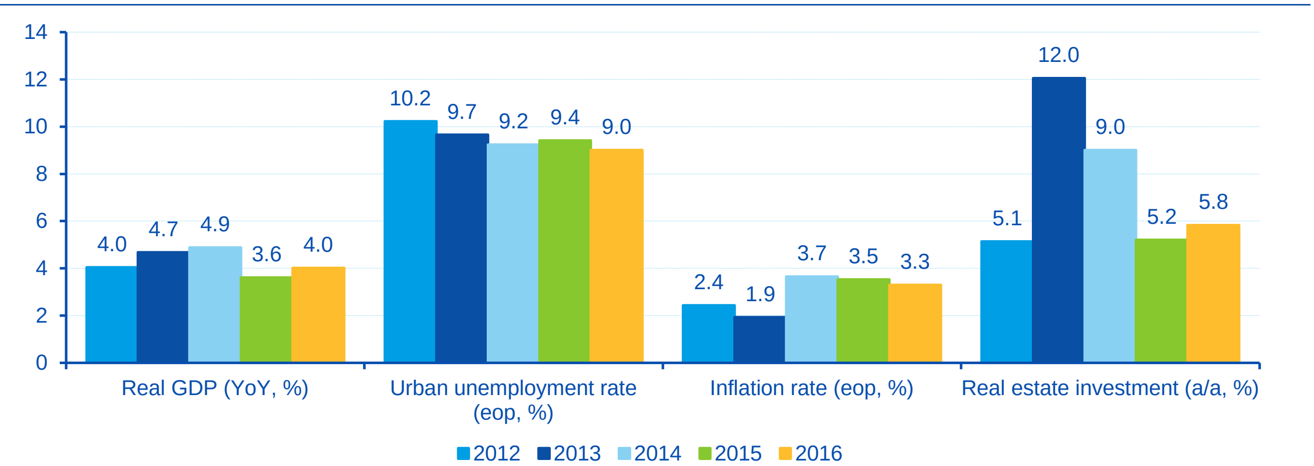
Using 2012 figures, the government has estimated the quantitative housing shortage as being 554,087 units. This meant the shortfall has been considerably reduced in relative terms since the census of 2005, when 12.6% of households did not have a home, figure which was down to 5.5% by 2012. There has been significant progress if one bears in mind that the population grew by 8.6% over this period, and households by 21.8%, with a greater increase in the second group because of the fall in the number of family members per household. Thus, while in 2005 each household contained 3.9 people on average, by 2012 this had fallen to 3.5. In absolute terms, there was a reduction of 477,000 units in the housing shortfall over these seven years. Similarly, **in 2012 the qualitative shortfall was 1,093,006 units, a reduction of 7.8% and 92,000 units since 2005**. Thus, the percentage of households living in sub-standard housing is 10.9%, compared to 14.4% in 2005. **The total deficit (quantitative and qualitative) was 27% of households, equivalent to 1,647,093 units**.

An increase in household incomes also means high demand

In 2014, the country's GDP per capita was USD13,460, adjusted for purchasing power parity, over double the figure in 2000 (USD6,620), representing a notable increase in the average per capita income in a household. Each person in the household has a monthly income equivalent to COP538,000 (in 2013 pesos), which is 50% higher in real terms than in 2003 (after discounting inflation). That is, a typical Colombian family, with 3.5 people in the home, has an average monthly income of COP1.9mn (2013 pesos).

According to our calculations, the percentage of people in the middle, upper-middle and upper classes (people with incomes of over USD15,000 p.a.) climbed from 13% to 20% between 2006 and 2014. This meant an increase of 3.1 million people in these income brackets over eight years. Today, there are 15.6 million people on low incomes, 24.4 million in the medium-low bracket, 4.4 million in the middle-middle class, 3.9 million in the middle-upper class and 4.9 million in the upper class ("middle class" is defined on page 3 of our Explosión de la clase media emergente Watch, in Spanish only). This is, without doubt, the result of the country's economic stability, with high growth rates, low inflation and reductions in unemployment (Figure 2.1).

Figure 2.1
Colombia's macroeconomic conditions: 2014 and expected for 2015



Source: DANE and BBVA Research

A large proportion of the high-income population does not own a home. As of 2013, 43% of households owned their own home, 4.1% were paying for it and 16.3% lived in usufruct with the owner's permission. Furthermore, **34.8% of households were renting their home.** By income level, among the 20% of households with the highest income in the country (5th quintile, technically), earning **incomes of over COP15mn a month per household, 35.3% were renting**. In the next 20% (quintile 4), in the COP9.4mn to COP15mn income bracket, 42.5% were paying rent. And for the 20% with intermediate incomes (quintile 3), of between COP6.3 and COP9.4mn, 44.6% were in rented accommodation.

What is more, demand was concentrated on flats, particularly in the case of households joining the high-income group for the first time. The proportion of households living in a house, although still the largest, fell from 64.4% in 2011 to 57.2% in 2013. At the same time, the percentage of households living in flats climbed from 30.6% in 2011 to 38.4% in 2013.

Finally, **a structural change in the demand for housing is occurring as a result of more women going into the job market and taking a share of the country's income.** Over 54% of women are currently active in the labour market, double the figure of thirty years ago. This is related to educational progress. Women born in 1954 received the same education as the men in their generation, but those born later received more. Now, for every four men between 25 and 40 with a university degree, there are five female graduates. What is more, although the sexes start university in similar proportions, men are 10% more likely to drop out, so more women are graduating. As a result, nowadays the proportion of labour income earned by women in Colombia is 45% (according to household surveys).

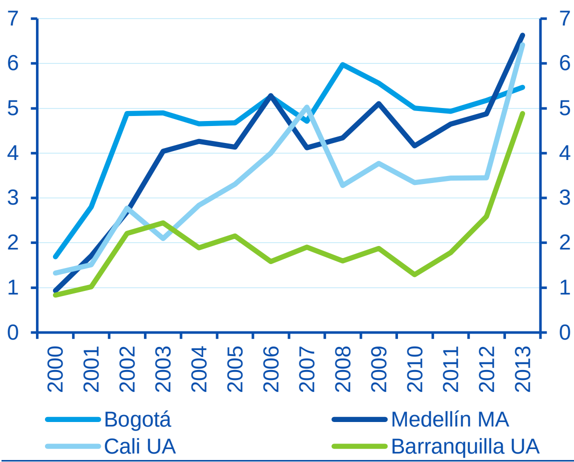
Year-on-year (YoY) housing construction is low, although it has accelerated significantly in the last few years

Housing construction is currently at its historical peak, at 230,000 formal homes (i.e. with a building permit) a year. Bogotá accounts for 29% of licences (34% if Cundinamarca is included), followed by Antioquia (12.7%), Atlántico (6.6%), Santander (6.5%) and Valle (6.5%). Participation differs depending on the value of sales; on this reckoning Bogotá and environs take 50% of the national total (35% in Bogotá alone), followed by Antioquia (18.3%), Santander (8%) and Valle (7%).

But is building really high? The number of residential units built in a year, per one thousand inhabitants, is a standard measurement of new housing supply every year. Figures 2.2 to 2.5 show the results of the measurement since 2000 and since 2007, depending on the availability of data from the Building Census for the country's main cities. The national average has risen considerably since 2000, when 1.6 units were built for every 1,000 inhabitants, to 2013, when it was 6.0 units. This progress was accounted for, at the beginning of this decade at least, by progress made in Bogotá, Medellín, Cali and the coffee axis, whereas Bucaramanga and Barranquilla were less dynamic. More recently, growth has been accounted for by intermediate size cities (very significantly in Popayán and Neiva) and the impressive surge in Barranquilla since 2010, although the latter is still below the national average.

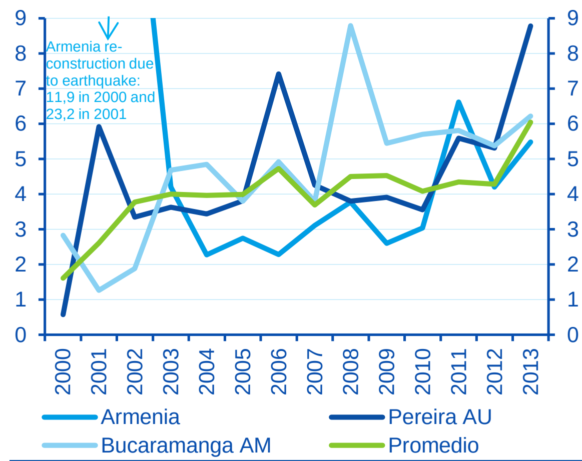
When these figures are compared internationally they are still low, if we bear in mind that Colombia still has a housing shortage. For example, in Chile over the course of 2013, 118,800 houses were built, a ratio of 6.7 units per one thousand inhabitants. This figure is higher than Colombia, even though the housing shortage in Chile is below 2%, according to the most recent estimates.

Figure 2.2
Housing construction per 1,000 inhabitants by city*



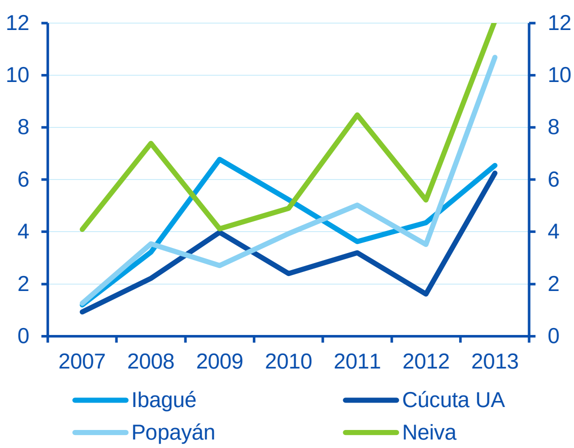
* Data available since 2000.
Source: DANE and BBVA Research

Figure 2.3
Housing construction per 1,000 inhabitants by city and national average*



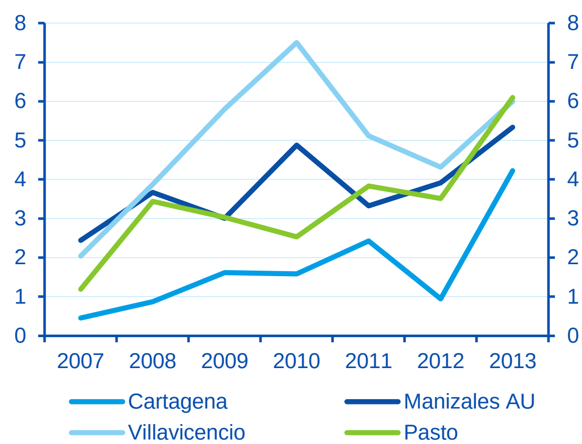
* Available since 2000. Average: Bogotá, Medellín, Armenia, Pereira, Bucaramanga, Cali and Barranquilla since 2000. Since 2007. Also includes Cartagena, Manizales AU, Popayán, Neiva, Villavicencio, Pasto, Cúcuta AU and Ibagué.
Source: DANE and BBVA Research

Figure 2.4
Housing construction per 1,000 inhabitants by city*



* Data available since 2007.
Source: DANE and BBVA Research

Figure 2.5
Housing construction per 1,000 inhabitants by city*



* Data available since 2007.
Source: DANE and BBVA Research

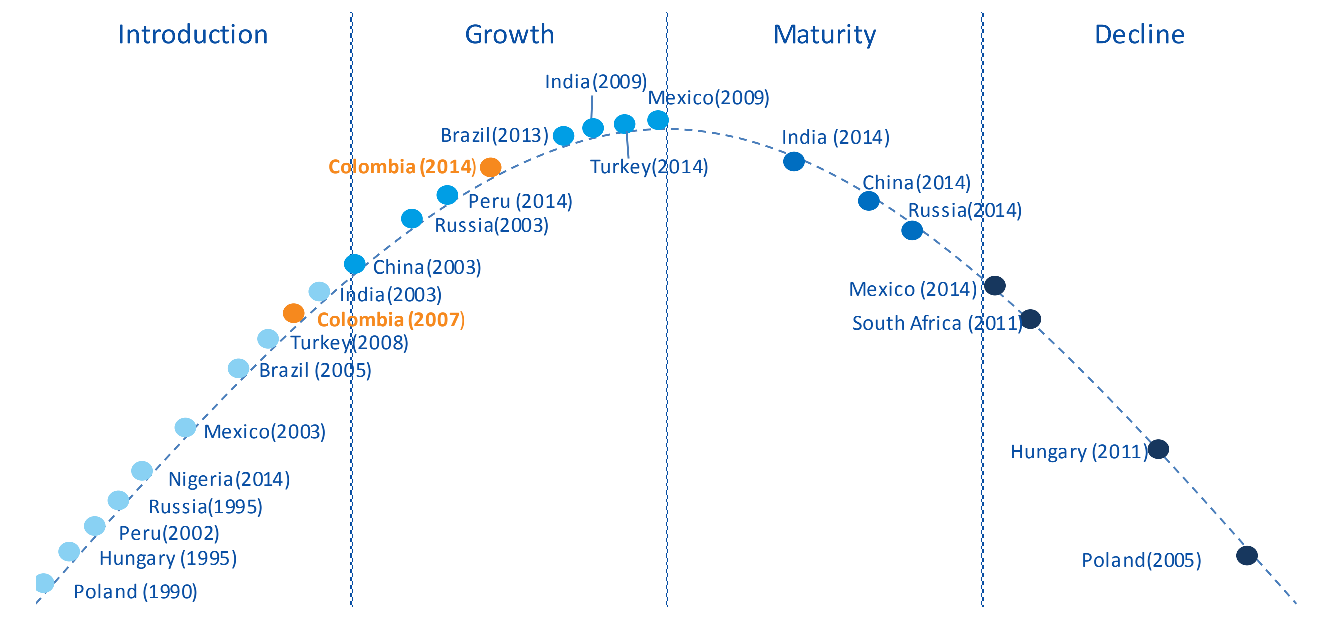
In order to increase the rate of construction, the country needs solid Territorial Planning Programmes (TPP). Many cities are currently in the process of creating the ground rules which will govern their urban planning in the future, or else have recently passed the framework regulation. Cities have made a commitment to urban renewal, high-rise building and the provision of sufficient public goods to encourage concentration in city centres, rather than around the periphery (See Box 1).

Colombia has enough space to increase non-residential supply

The number of square metres of shopping centres per inhabitant in Colombia is still low when compared with other countries in Latin America, and even more so compared with developed countries. Chile has the largest figure in the region, with 0.177 square metres in gross leasable area (GLA) per inhabitant, with Venezuela in second place at 0.122 square metres. Colombia is in the middle, with 0.074m^2 per inhabitant, more than Brazil (0.057m^2) and Peru (0.055m^2), while Argentina and Mexico have lower rates (0.033m^2). These numbers are very different in the United States (2.215m^2), Canada (1.362m^2) and Australia (0.916m^2), (*Colombian Shopping Centre Association* and the *International Council of Shopping Centers*). In terms of the number of shopping centres, without controlling for each country's size, Mexico is in the lead (630 centres), followed by Brazil (429), Colombia (183), Venezuela (168), Argentina (86), Chile (85) and Peru (38).

By cities, Medellín has the highest penetration of shopping centres in Colombia, although it is in the municipalities with under a million inhabitants where they are springing up fastest (Montería, Yopal, Florencia and Pitalito). Medellín has 0.172m^2 of shopping centres per inhabitant, followed by Cali (0.169m^2), Bogotá (0.152m^2), Bucaramanga (0.104m^2), Barranquilla (0.103m^2), Ibagué (0.056m^2), Armenia (0.042m^2) and Sincelejo (0.033m^2). These figures are below those of Mexico City (0.24m^2), Santiago de Chile (0.23m^2) and Sao Paulo (0.20m^2), although they compare favourably with Buenos Aires (0.09m^2). On the other hand, **60% of new projects (during 2014 there were 54 new centres) are being executed in intermediate regions, with shopping centres of between 5,000m^2 and 20,000m^2.** These new developments will lift Valledupar and Villavicencio above the national average of m^2/inhabitant and even above Medellín, inasmuch as they are expanding cities (in demographic and economic terms) which are preparing for future demand, which will depend on the transition in Colombian purchasing habits, which will be linked to the increase in incomes (Figure 2.6).

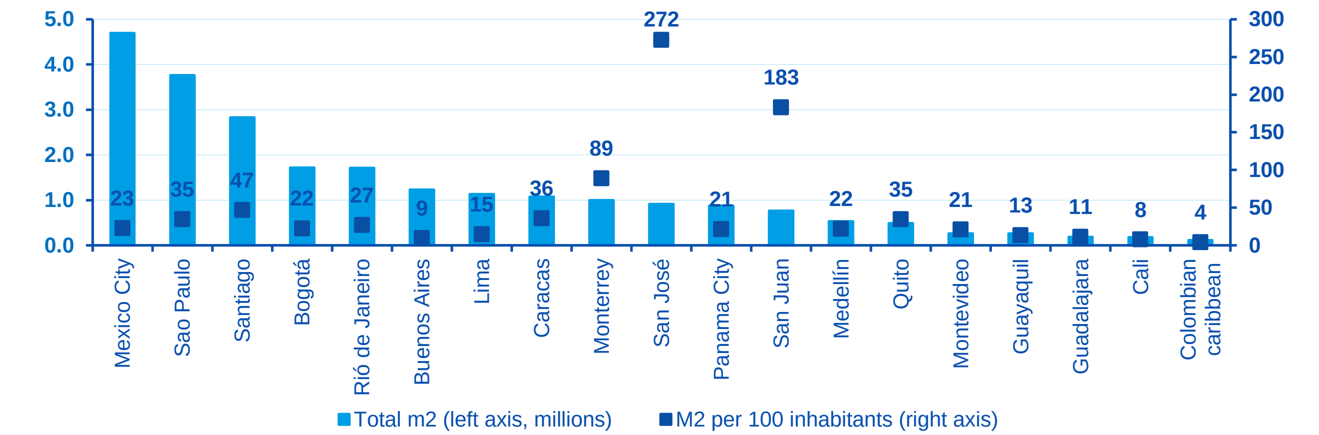
Figure 2.6
Modern retailing cycle (penetration of department stores and specialised retail outlets)
International comparison - emerging countries



Source: BBVA Research and AT Kearney (2014)

When it comes to **the Colombian office market**, meanwhile, **Bogotá leads the way, registering a total of 1.72 million square metres of supply in May 2014, followed by Medellín with 0.53 million m^2 and trailed by Cali (0.16 million m^2) and Barranquilla (0.08 million m^2).** Nevertheless, penetration per 1,000 inhabitants is still far lower when compared with cities in the region (Figure 2.7), principally in small cities with intense commercial activity such as San José (Costa Rica) and San Juan (Puerto Rico).

Figure 2.7
Office space (m^2) by city and m^2 per 100 inhabitants



Source: BBVA Research and AT Kearney (2014).

Finally, in the warehouse and storage market, **between 50% and 60% of the companies using storage services do not own their premises.** The average size of warehouse is between 1,550m^2 and 1,800m^2, depending on the type of property. When free trading zones were created in Colombia, this encouraged the construction of logistics hubs in the country because of the tax breaks and other incentives for external trade.

Table 2.1
Relevant indicators for the Colombian real estate market

Relevant indicators	
Population (million inhabitants, 2014)	48.0
GDP per capita (USD at PPP, 2014)	13,459
Geographical area (‘000s of km^2)	1,141.7
Housing stock (‘000s of units, 2013)	12,965.1
Housing stock per 1,000 inhabitants (2013)	270.02
Average house price (COP ‘000, 2014*)	158.1
Bank lending for new housing (% of total, 2014*)	47.5
Financed existing housing (‘000s, 2014*)	55.5
Average duration of mortgage (years, 2014)	Between 8 and 10
Average percentage financed of the home value (LTV, %, 2014)	54.8
Average interest rate on housing loan (E.A.,%, 2014)	10.9
Mortgage portfolio** (% of GDP, 2014)	6.3

*Average between September 2013 and September 2014. **Includes leasing.
Source: DANE, FMI, Asobancaria, Superfinanciera and BBVA Research

Box 1. Territorial Planning Programmes (TPP) around the country

Urban planning in Colombia faces at least three medium-term challenges. First, to establish the size of cities and the type of expansion they want to embark upon. Second, to increase the amount of public space in cities, which is currently less than $4m^2$ per person. According to the World Health Organisation, this figure should be closer to $15m^2$. Third, to improve urban mobility, with faster and more accessible transits.

It was only last year that the medium-term design for cities in Colombia was discussed within the remit of approving their Territorial Planning Programmes, or TPPs — POTs in the Spanish acronym. TPPs were passed in many cities which would be in place for at least 13 years, while some are being debated with a view to approval in the 2015 parliament. If we review some of the texts that have been passed, and some of the projects, we can verify certain coincident factors between the three challenges listed above.

Growth in city centres and more public spaces

The first shared point in the TPPs is that of controlling the disorderly expansion of cities and giving priority to locating their inhabitants in the centre. The advantage of this policy lies in savings on infrastructure such as roads, water supply, electricity, etc. for the municipalities. Furthermore, it reduces commuting times for the inhabitants and limits car congestion on the routes out to the suburbs. However, it is demanding in terms of denser infrastructure requirements in central zones, with greater demand for public services and roads.

Cities have different methods for dealing with this proposal. In Bogotá, the TPP proposed by Mayor Petro (not implemented) was based on high-rise construction, which would replace land that is not available on the outskirts of the city as a result of the environmental restrictions that have been imposed on it. These plots of land will increase the natural spaces available to the city, preserving many wetlands, among other natural ecosystems.

In Medellín, a green belt has been proposed (the Ring Garden) for the city, which will mark out the natural limits to the urban settlements by a kind of environmental city wall. This will: i) prevent peripheral urban construction; ii) give priority to flat areas over the hillsides, and iii) provide more natural public spaces. The city will also create a natural park lengthwise along the banks of the River Medellín.

Cali is using a combination of expansion and densification. The urban expansion area will continue to be the Cali/Jamundí corridor, and the Navarro Eco-city will be built with at least 6,000 housing units. Construction on the hillsides has also been approved, with building plans of at least 20 hectares (ha) in areas which are not high risk. Areas have been designated for densification and divided into four hubs: calle 25, some neighbourhoods to the east (La Floresta, Saavedra Galindo, Rafael Uribe Uribe, Santa Mónica Popular, among others), calle 13 and neighbourhoods in the industrial zone (calle 8). Finally, the city's public spaces will be enlarged, giving priority to projects located in areas with the largest shortage of public zones.

In Barranquilla, expansion has not been entirely ruled out, but will depend on the existing infrastructure. With the green district around the city and other projects too, the aim is to rise from $0.87m^2$ of public space per person to $6.2m^2$ over 20 years.

In Bucaramanga, construction was restricted in environmental zones that are next to neighbouring municipalities and other rural zones, and the amount of land allocated for urban expansion was reduced. Furthermore, high-rise buildings in the metropolitan area were limited. In the category of public spaces, a fund was set up to be financed by construction firms to offset the impact of further buildings. The goal is to increase the current $4.5m^2$ of park per person to $10m^2$.

Priority for public and non-motorised forms of transport

Cities have changed their goals for infrastructure construction, shifting away from wide avenues for private cars, which provided incentives for the use of individual cars, to lanes which are exclusively for public transport, bike lanes and pavements for pedestrian mobility. The ultimate aim behind these programmes is to discourage use of motorised transport by providing a fast and more convenient public transport service.

In Bogotá, the TPP which was not implemented proposed population densification along the metro line corridors (not yet built) and the TransMilenio line, while non-motorised, pedestrian and cycle transport systems are given priority in central areas.

In Medellín, the aim is to discourage use of the private car and give priority to the pedestrian. Thus, each administration will allocate at least 50% of its budget to transit infrastructure, with 25% going on pedestrian routes and non-motorised mobility, and the other 25% on mass collective public transport.

In Cali, priority was given to building the infrastructure for the *MÍO* (large-scale public buses) and on extending pedestrian networks such as footpaths, bike paths and bike lanes.

In Barranquilla, the integrated mass transport system will be improved, as will bicycle facilities since, of the 1.8 million inhabitants in Barranquilla and Soledad, only 0.1 million use motorised private transport. Similarly, building permits in areas close to the public transport system will be given priority approval.

In Bucaramanga, a sustainable mobility system will be developed, as will an increase in non-motorised transport, with pedestrian and bike path networks to connect production areas, urban facilities and residential zones. An external ring road is also being proposed to prevent regional traffic (from nearby cities) from crossing urban areas. This latter project is essential because a high proportion of the population working in Bucaramanga lives in the municipalities close to the metropolitan area.

Conclusion

A new vision for cities, from recommended size and mobility, to the provision of public spaces, was the basis of the TPPs that have been designed recently. The points they share are: avoiding peripheral growth around municipalities, giving priority to densification and high-rise building (except in Bucaramanga), along with safe and legal construction; encouraging construction close to public transport networks; increasing the provisioning for public and natural spaces; and promoting public and non-motorised transport over private vehicles.

As well as the regulations contained in the TPPs, which are at a municipal level, there is also another possible law in the offing (although currently shelved) which would enforce the economic, environmental and social sustainability of buildings and would coordinate national rulings with municipal decisions within the institutional framework for construction. This bill was given prominence mainly because of the awareness created by the structural problems of a building in Medellín, which ended up by collapsing.

In the Congress, this event raised doubts about the sector’s regulatory capacity, ranging from ombudsmen and notaries, to each city’s environmental institutions. Furthermore, it provided incentives for the inclusion of new parameters required in the approval of construction licences. However, to date it is unlikely that this law will be passed because of new legislative priorities.

3 Situation and outlook for the real estate sector

Challenging macroeconomic environment for 2015 and 2016

Oil has been an important source of growth in recent years, particularly between 2008 and 2011 when the economy faced and overcame the international crisis. Since June 2014, oil prices have fallen by 55%, mainly due to the increase in supply and an anemic demand. **The impact on growth will be limited because of the low incidence of oil in GDP and the compensating effect of other activities which have been driven by the real devaluation in the exchange rate (industry and agriculture).**

Consumption will be the key mainstay, growing by 4.3% YoY in 2015. In addition, there will be high public consumption because of the flexibility provided by the fiscal rule for expenditure when revenues fall, the central government's support for social housing and, finally, because regional governmental mandates draw to a close in 2015. **We expect 3.6% growth in 2015, a figure that compares favourably worldwide and to lower terms of trade. For 2016 we project expansion of 4.0%, a value that is relatively close to the economy's potential** (Figure 2.1 in section 2). In response to economic deceleration, the central bank will reduce its interest rates in 2015 if inflation expectations remain anchored. Similarly, there may be a lower inflow of direct foreign investment in 2015 and 2016.

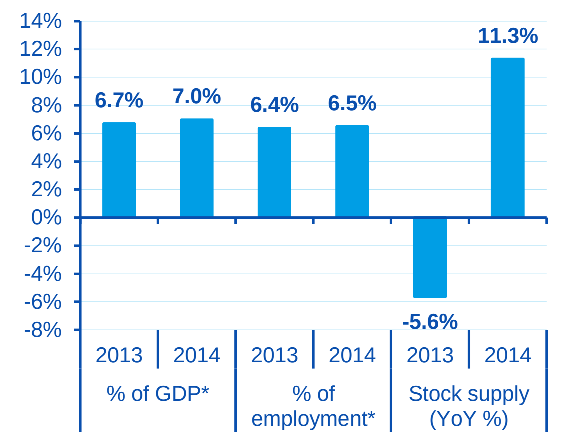
Recent performance: dynamic activity but less added value

The building sector grew by 11.4% in 2013, before moderating to a YoY rate of 7.8% in the first nine months of 2014. This slowdown was accounted for by a greater participation in social housing (VIS), which has less added value because top coats and finishes, as well as masonry, are sometimes absent, but not because of a drop in activity in the sector as a whole. In fact, employment in construction (which also includes civil projects) grew by 38,600 employees between September 2013 and September 2014, and the inventory of homes already built or under construction rose from 80,900 units in December 2013 to 90,000 in December 2014 (+11.3% YoY), breaking with the trend to the downside that we saw through most of 2013 (Figure 3.1, with data from La Galería Inmobiliaria, the growth in supply continued in January).

The supply of buildings is divided between social housing, with 30%, and housing of higher value, with 69%, in the country's eight largest cities (Bogotá and metropolitan area, Medellín, Cali, Bucaramanga, Barranquilla, Cartagena, Santa Marta and Villavicencio). The proportion of social housing is significantly higher in Barranquilla (52%) and Cali (51%) but lower in Bucaramanga (8%), Cartagena (12%), Villavicencio (16%), Medellín (22%) and Santa Marta (26%). In Bogotá it is close to the national average (32%). Taking the eight cities together, the supply of social housing increased its total share (from 28% in 2013), mainly because of the greater contribution from Barranquilla, Santa Marta and Cali. On the other hand, according to the building permit registry, permits for social housing grew by 53.3% in 2013, whereas permits for higher-value housing grew at a rate of only 0.15%. In total, they grew by 14.3% (Figure 3.2).

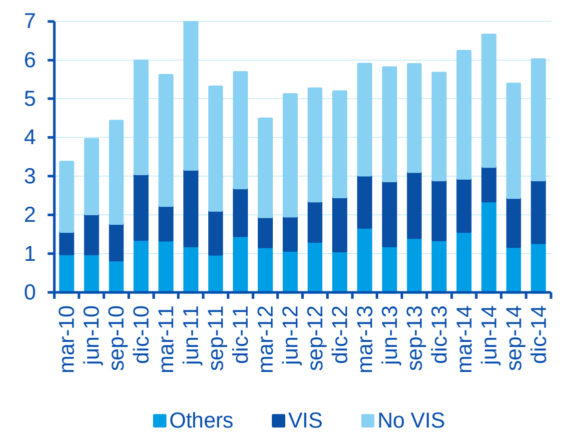
In 2014, behaviour started shifting slowly, which will be visible in 2015, given that the lag between permit and construction is at least eight months. **As of December, social housing permits fell by 17.9% YoY, and those for non-social housing grew by 12.3% YoY, with permits overall falling by 0.7% annually**. This reflects how the uptick in higher value housing was not enough to offset the drop in social housing, although it also heralds a forthcoming change in the trend in the supply of high-value housing (Figure 3.2). **This was accounted for by the launch and roll-out of new housing projects, with the former growing by an annual 7.2% in 2014 and the latter by an annual 1.7%.** The rise in project launches was fairly steep in Cúcuta (191% over the year), Boyacá (106%), the Caribbean zone (104%), Valle (75%), Tolima (49%) and Caldas (44%). By contrast, there were falls in Nariño (-64%), Santander (-25%), Antioquia (-17%) and Huila (-14%).

Figure 3.1
Construction sector indicators (% of GDP and % variation)



* Includes civil works.
Source: DANE, Camacol and BBVA Research

Figure 3.2
Construction permits by end use (million m^2, quarterly accumulation)



Source: DANE and BBVA Research

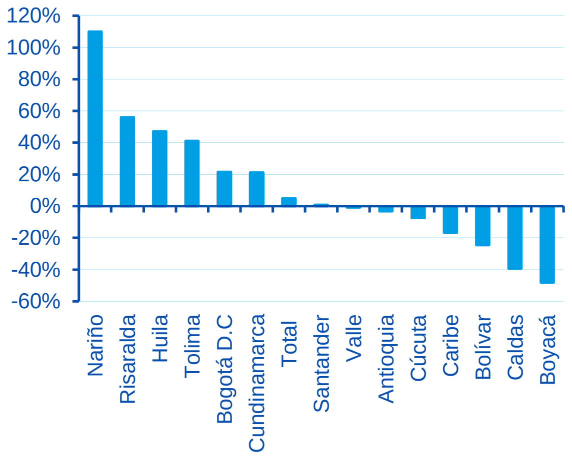
When we compare these results with the gap between launches and sales in 2013, only the momentum in the Caribbean zone is unexpected, since there was already a surplus of launches over sales in 2013 and during 2014 this widened. On the other hand, the results in Cúcuta and Tolima were anticipated, because their gaps in 2013 were very much in favour of sales, as was the case in Valle and Boyacá, although to a lesser extent. Likewise, the correction in Antioquia came as no surprise because of the surplus of launches over sales in 2013. Altogether, the behaviour of residential supply and demand is close to equilibrium, although with a tendency towards over-demand (Figure 3.3). This is partly due to the moderation in social housing projects, but also to the smaller number of high-value projects (in Medellín, in particular).

By category, most of the available supply is in middle class housing. 76% of the total is concentrated on cost brackets 2 (22.2%), 3 (26.2%) and 4 (27.8%). The rest is spread between bracket 1, with 3.3%, bracket 5 with 12.3%, and the final 8.1% being in bracket 6. Bracket 1's smaller share of the whole is accounted for by the lower availability of cheap land and because of its high stock turnover, since demand tends to be permanent and subsidised (Figure 3.4).

Unsold stock in the housing construction sector is still scarce. All the cities in the country changed to the "sell to build" model, which ensures that when the building stage has ended, there are guaranteed customers (who have already made their purchase) for the project. Not one of the country's most important cities has more than 6% of unsold built housing. Cali, Bucaramanga and Barranquilla have managed particularly well, with percentages of just 1%.

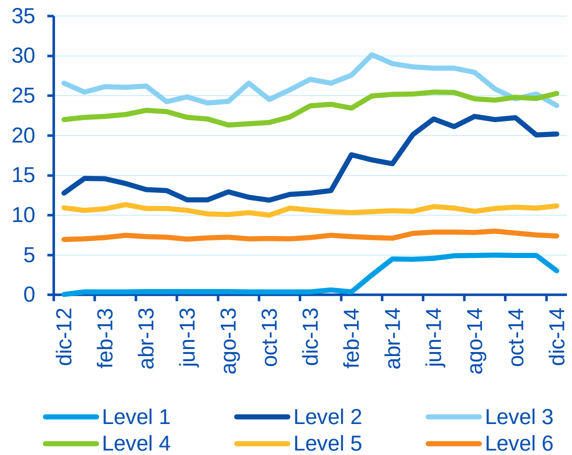
Finally, **there has been a modification in construction habits towards projects with more units, although smaller in terms of square metres**. Thus, whereas projects on offer grew by only 4.8% during 2014, the units available increased by 15.1%, while the square metres available expanded by 9.3%. This trend is more apparent in Bogotá and nearby municipalities, Bucaramanga, Santa Marta and Barranquilla. Villavicencio is the only exception, where the number of projects is growing more than the units.

Figure 3.3
Gap between sales and launches (%)



* A positive value means more sales than launches.
Source: Camacol and BBVA Research

Figure 3.4
Available supply by income level* ('000s of units)

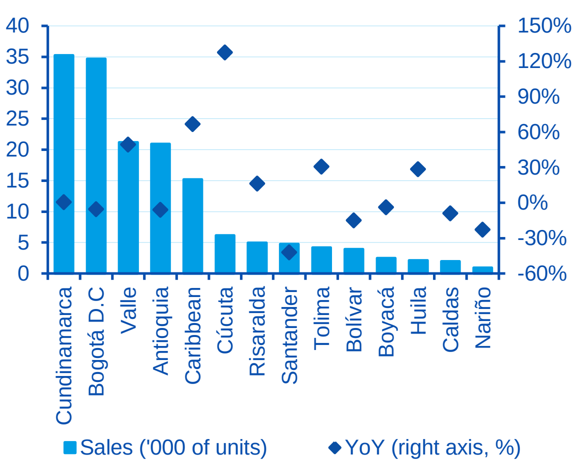


*Level 6 meaning the highest income
Source: Camacol and BBVA Research

Housing sales are moving at the rate of social housing projects

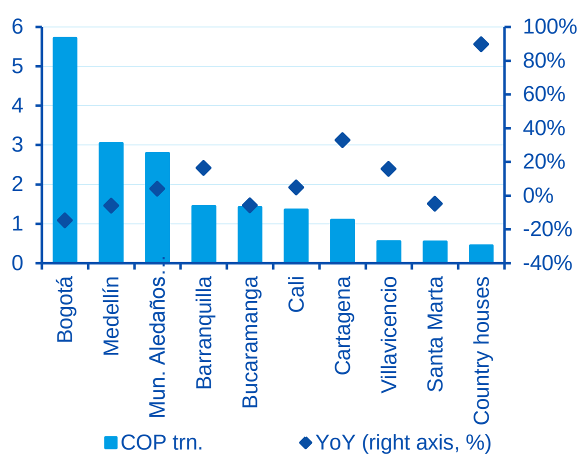
According to Camacol figures, housing sales in the 13 regions which are tracked grew at an annual rate of 11% in 2014, led by the low-value segment. Social housing sales increased by an annual 26.8% and those belonging to the non-social housing segment fell 3.5% YoY. By regions, some medium-sized cities (Caribbean, Cúcuta, Cundinamarca municipalities, Neiva, Pereira and Ibagué), plus Cali, took the lead. By contrast, some cities with lots of momentum in the past reported slowdowns (Medellín, Cartagena, Tunja, Manizales, Pasto and Bucaramanga). Nevertheless, in Cartagena, the rest of the Caribbean region and in Neiva, the number of high-value projects is growing, and the fall is accounted for by the slower momentum in social housing, whereas this segment is flourishing in Bogotá, Cali and Pereira (Figure 3.5).

Figure 3.5
Housing sales by city ('000s of units and annual variation, 2014)



Source: La Galería Inmobiliaria, Camacol and BBVA Research

Figure 3.6
Value of sales by cities (COP trn and annual variation, 2014)



Source: La Galería Inmobiliaria and BBVA Research

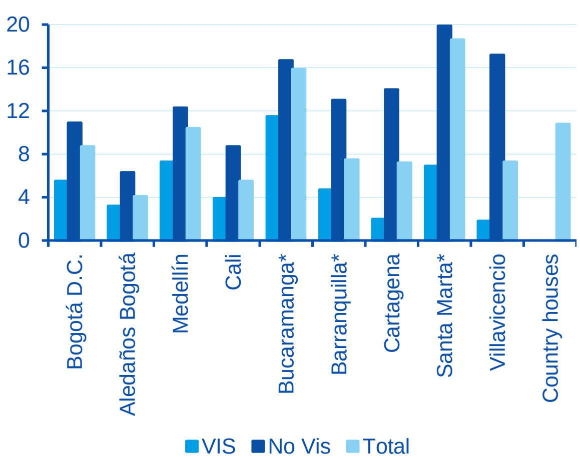
We see a similar result in **the consolidated figures from La Galería Inmobiliaria to December. Total sales grew by an annual 4.5% last year, but if we exclude VIPA programme (social) housing, then we would have a 9.2% fall over the same period.** Furthermore, when we compare by value, rather than by units, total sales grew by 1.6% YoY and fell by 6.0% if we exclude VIPA. The sharpest falls, even including VIPA homes, occurred in Bucaramanga (-17.4% in units), the municipalities around Bogotá (-10.7%), Bogotá (-7.3%) and Medellín (-4.3%). When we do not include VIPA housing, the falls in those cities are the steepest, with Cali going into negative territory and Santa Marta coming in at zero. In other words, the effect of public policy on these last two cities is spectacular, thanks to speedier ground adequacy process and the fact that the local governments made a serious commitment to building VIPA housing.

The municipalities near Bogotá also moved more quickly, making up for the shortage of land in the capital. Thus, **of total completed sales in Bogotá and its environs, the city authorities now have only a 50% share, whereas back in 2003 more than 90% of the units were sold by the administration, and in 2010 it held more than 80% of the new market.** However, this change is not unique to Bogotá. The same phenomenon, although less marked, is being repeated in other regions. In Cali, expansion towards Dapa, in Bucaramanga, towards Floridablanca and Girón, and in Medellín towards the southern part of the city (Envigado, Sabaneta) are examples of this trend.

The value of housing sales in Colombia is around COP26trn (vs. 24.5trn in 2013), of which COP8.8trn is concentrated in Bogotá (COP5.9trn) **and its neighbouring municipalities** (COP2.9trn). Medellín remains in second place, despite a reduction in building activity and moderation in its sale prices, with Cali returning to third place, although only just above Bucaramanga (Figure 3.6).

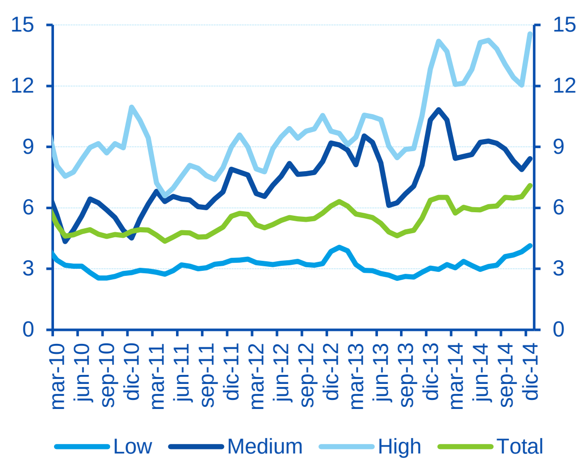
Despite (moderate) growth in sales, **stock turnover (the number of months needed to sell all available supply at the recent number of sales) rose during 2014,** due to the greater supply stock available. Taking the 2013 sales average, existing supply at the end of the year could have been sold within 6.9 months. At the close of 2014, using the average number of transactions from last year, selling off the entire stock would take 7.6 months (Figures 3.7 and 3.8).

Figure 3.7
Rate of housing stock turnover by city (number of months needed to sell available supply)



* Excluding social housing (VIPA).
Source: La Galería Inmobiliaria, Camacol and BBVA Research.

Figure 3.8
Housing stock turnover by home value (number of months needed to sell available supply)



Source: La Galería Inmobiliaria and BBVA Research

This prolongation was not seen across all cities, but turnover times lengthened in Bogotá and its environs, Bucaramanga and Santa Marta (Figure 3.7). In these last two cities the increase was significant, up to 15.9 months in Bucaramanga, from 10.8 months, and up to 18.6 months in Santa Marta, from 16.3 months. This indicator heralds a moderation in construction in these two cities, particularly in non-social housing. By contrast, cities such as Cali and Bogotá (despite the increase in 2014) still have fast rates of turnover, at around six months to sell the entire housing supply. Furthermore, there was an adjustment in Medellín (due to lower supply), Barranquilla and Cartagena (in the latter two because of increased sales), cities where the indicators are now showing turnover rates of under a year.

The time needed to rotate stock, depending on the housing price, fell considerably in the medium price range, remained stable (although with a tendency to grow in the last few months) for the high ranges, and rose marginally for low-cost housing (Figure 3.8).

A necessary slowdown in non-residential supply

Since 2013, the supply of new offices (built and under construction) has grown steadily. Whereas in December 2012 277,000m^2 was available between Medellín and Bogotá, by December 2014 that number had shot up to 481,000m^2. Happily for the market, this increase in supply was accompanied by an increase (although not completely equivalent) in sales, which went from an average between the two cities of 14,000m^2 a month in 2012 to one of 24,000m^2 in 2014. Even so, the turnover times for stock did deteriorate, although they remained at levels that are manageable for developers of this kind of building, which require more time to be spent on the finishes, ICT networks and the internal extras which companies demand. Currently, and if the recent rate of sales holds firm, the supply of offices available would be sold in 19 months, longer than the 17 months it was taking in 2013, and the 16 months on average for 2012.

The supply of commercial premises (built and under construction), which grew significantly in 2013 and the first quarter of 2014, has slowed down a great deal since then, which is a good thing. Turnover times have risen noticeably and supply has had to adjust to slacker demand. At the moment, using figures for average sales in 2014, the commercial properties available would sell in 20 months, a number which seems to match the construction times for commercial blocks and which has adjusted from the turnover time of 30 months registered in April 2014. **The warehouse and storage segment has behaved similarly. Growth has slowed down since the beginning of 2014**.

On balance this moderation is positive, since it came before the fall in oil prices and the lower growth in GDP and exports which the former will cause in 2015. What is more, an important change in the structure of Colombia's commercial offering is taking place: there is a gradual shift from "build to sell" to "build to let", which implies a different type of cash flow, now closer to in perpetuity, and requires greater financial muscle because the recovery of the investment becomes a regular, long-term repayment.

However, the non-residential construction market has yet to develop the pre-sales policies which have proven so successful in the case of housing, policies which have ensured that stockpiling of inventory has been minimal, even in moments of lower economic buoyancy. This is not the case in offices and commercial premises, with some exceptions. Here, construction begins before a high percentage of sales or future rentals have been secured.

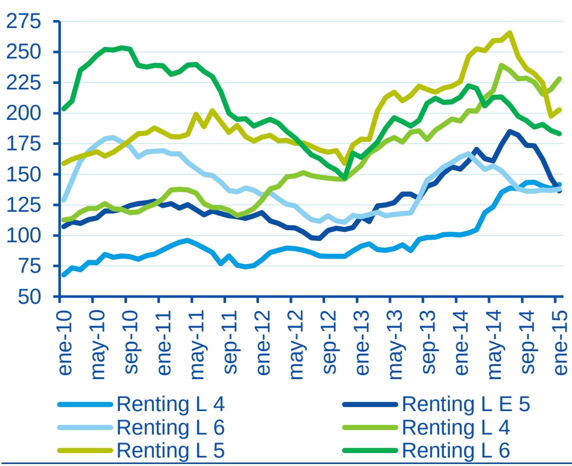
Hotel construction is structured differently, because of the 30-year tax incentive on profits of those who start operations before December 2017. Since the 2002 Law 788 which created this incentive has been in force, 55,913 rooms have been built or refurbished (with an investment of COP3.4trn, according to Cotelco).

Cotelco estimates that Cartagena (3,273 rooms), Bogotá (1,238), Barranquilla (1,025) and Medellín (700) will enjoy the largest increase in bedroom numbers in 2015 and 2016. Altogether, the number of bedrooms is expected to grow by 6,667 over this two-year period in the whole country. However, the closeness to the deadline on profits could be a disincentive for investments towards the end of 2016, given that project planning takes over a year. In addition, the hotel business tends to move in waves. That is, many more rooms than can be met by demand become available, then the number stabilises, and once they have been absorbed by the market, a new building cycle begins, once again generating an over-supply.

Existing housing: turnover is speeding up

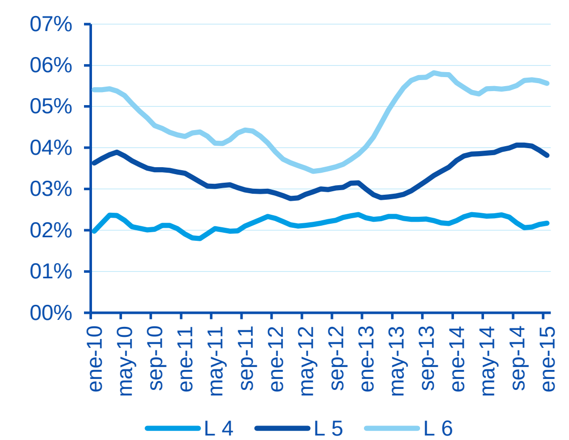
Investment buyers shrank in number in 2014. Whereas in 2013 this percentage was 21%, during 2014 it fell to 19%. The main reduction was in the buy to resell segment, but there was also a smaller reduction among those buying to rent out. The trend determined a reduction in rental values as a percentage of the house price, which is favouring the rental market over the existing housing sales market. Similarly, this is making it possible for those on middle incomes to move into higher-income residential areas, thanks to the lower rental costs. As a result, turnover times for renting or sale of existing housing were shorter in the medium and high cost brackets, particularly when compared with the time needed to sell (Figure 3.9).

Figure 3.9
Time to rental (blues) and to sale (greens) for existing housing (by cost bracket, days)



Source: La Galería Inmobiliaria and BBVA Research

Figure 3.10
Existing housing available on the market, (% by cost bracket)



Source: La Galería Inmobiliaria and BBVA Research

Even so, turnover times will not return to their record lows of 2012 for a while yet, because the purchases made in 2013 and 2014 will continue to enter the market at a high rate. This will be the outcome when the housing bought off-plan is ready and delivered, a phenomenon which is particularly widespread in the Caribbean and, to a lesser degree, in Bogotá. As a result, there has still been a record high supply of existing housing on the market in recent times (Figure 3.10).

The overview: sustained momentum will focus on social housing, with temporary contributions from other types of construction

All the economic indicators we have reviewed coincide in painting a bright outlook for social housing, whereas they anticipate a transition in high-value housing and non-residential buildings over the course of 2015.

***Mi Casa Ya* (My House, Now), a government programme which aims to build 100,000 low-price homes, will give a boost to social housing from January 2015 onwards until 2018.** The public sector will invest COP2.4trn, and business worth COP9trn is expected to be generated. The programme is for families without their own home who have not received a subsidy in the past, with total incomes, including all family members, of between two and four times the minimum wage, who buy a new home in the city for under COP86mn (135 current minimum wage packets). It consists of a subsidy of up to COP12mn for the down payment on the home, and remitting four percentage points of the mortgage interest rate. This last measure reduces the monthly payment by between 30% and 40%, depending on the price of the home, making it more affordable for families, and making it easier to close financing. Likewise, since the programme will concentrate on intermediate cities, it means that these cities' positive performance in recent years can be prolonged.

Altogether, the Government plans to invest COP8trn over the four years between 2015 and 2018 and will push forward the building of around 400,000 homes in all, through this kind of programme. As well as *Mi Casa Ya*, the housing programme for savers will remain open, with the construction of 86,000 homes, the donation of 100,000 free homes and subsidised mortgages for 130,000 new homes. Furthermore, the government will have the benefit of its experience in its first four years. Over this period a record number of homes were built, with around 900,000 housing starts. What is more, for the first time more social housing than non-social housing was built, at nearly 500,000 social housing units, with an investment of around COP8trn.

For their part, **high-value housing and non-residential buildings will perform differently during 2015, partly because of the lower revenues from oil and the moderation in GDP growth and formal employment that this fall in revenues will imply.** Offices and commercial premises will enjoy positive momentum in the first part of 2015, which will be determined by the high number of licences granted at the beginning of 2014 and the first months of the second half. This will help the aggregate value of GDP, as they are the kind of projects whose commercial value makes the largest contribution to construction product. Meanwhile, non-social housing could start to perform better from the end of 2015 onwards and into 2016, since the economy, employment and household incomes will receive a significant boost from the recovery in exports (rise in the oil price and higher demand from the United States), as well as the 5% growth in industry, the first such growth since 2011.

We believe that in 2015 and 2016 investment in building will grow at an average of 5.5% a year, a lower figure than in 2013 and 2014, when it grew by 10.5% YoY. In the medium term, between 2017 and 2019, we believe that investment growth will accelerate to an annual average of 7.2%. The main obstacles to reaching this figure have to do with the allocation of urban land in cities with the most severe space restrictions (such as Bogotá, Bucaramanga and Medellín) and the consolidation of urban transport infrastructure in the major urban centres. This latter aspect has been the most important one in the case of Bogotá, where progress in the construction of various means of public transport has been slow.

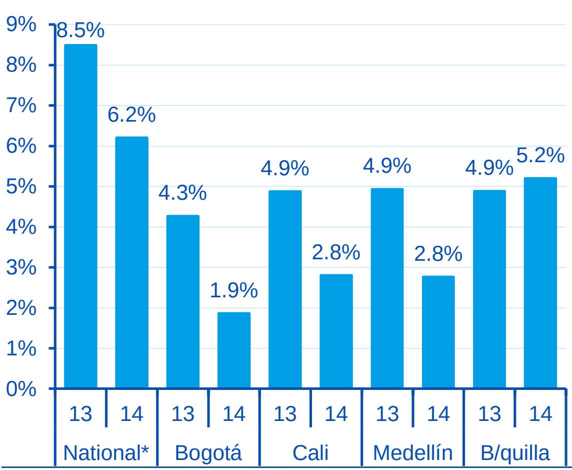
4 Prices and financing

The moderation in housing prices in urban centres is welcome

New housing prices continued to decelerate gradually in 2014. Using DANE data, real prices to the third quarter of 2014 (discounting inflation) grew by 6.2% a year, below 2013's closing figure of 8.5% (Figure 4.1). The urban areas (municipal capitals and nearby municipalities) where residential prices grew least were Pereira (-8.0% in real annual terms), Bucaramanga (1.5%), Armenia (3.1%) and Medellín (3.4%). Prices in Bogotá grew at 6.4%, close to the national average. Cali (8.8%) and Barranquilla (9.7%), meanwhile, grew faster than the average rate. For their part, **used housing prices accelerated last year**, from real 3.6% YoY in 2013 to 7.6% in September 2014. The reason may be the ending of subsidies to the middle class, which biased the purchases towards new housing with interest rate deductions, which did not apply to existing housing.

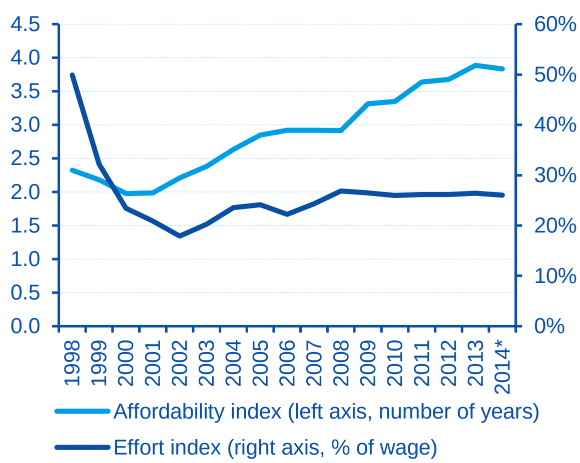
According to estimates from La Galería Inmobiliaria, with figures to December, between 2013 and 2014 prices in Bogotá, Medellín and Cali slowed their growth (to real annual rates of 1.9%, 2.8% and 2.8% respectively), and accelerated in Barranquilla (to a real annual 5.1%). In Bogotá and Medellín, social housing prices slowed most sharply. In the case of Cali it was non-social housing (Figure 4.1).

Figure 4.1
Real prices of total housing and by cities (2014* variation vs. 2013)



* National figures are available to September 2014. Data by cities are from La Galería Inmobiliaria and do not coincide with those provided by DANE.
Source: DANE (national), La Galería Inmobiliaria (by cities) and BBVA Research (calculations).

Figure 4.2
Measures of housing affordability*



* Affordability: average annual household income / average price of a home in Colombia. Effort: Initial mortgage quota / Average annual household income.
Source: BBVA Research

Our housing affordability measurements (the number of years it takes an average Colombian family, spending all its income after housing taxes — with no additional spending on food, travel, etc. — to buy an averagely priced house in Colombia) show that, **for the first time since 2010, there was no increase in the time it took to buy a home.** In fact, the opposite was the case: by this reckoning, the time needed fell from 3.9 years in 2013 to 3.8 years, according to September 2014 figures. This was a result of the moderation in the housing price growth and the Colombian economy's solid macroeconomic performance. Turning to mortgages, **the first down-payment,**

as a percentage of household income, remained constant, at 26%, comfortably below the legal threshold for mortgage loans (30% in Colombia), a signal of low interest rates, which offset the rise in housing prices.

Our outlook for 2015 is for further moderation in the growth of housing prices. This is related to lower demand for medium-priced new housing, which will shrink for at least three reasons. First, the policy of subsidising interest rates on mortgages taken out for sums above the social-housing ceiling has been shelved. Second, housing bought for investment purposes in the past, many of them benefiting from this interest rate cap, will continue to come gradually onto the market to compete with the supply of new builds, limiting the capacity of the latter to raise their prices. Third, the reduction in the price of rentals, expressed as a percentage of the property's price, to levels of between 0.35% and 0.40%, according to some survey results, makes it more cost-effective in the short term to rent than buy one's home.

But it is also connected to the demand for higher value homes. Against a backdrop of lower economic growth and an increase in unemployment, there is a reduction in the household confidence indicator. Specifically, the heightened fear of losing one's job leads to a lower propensity to buy housing, a commitment which requires the household to have a degree of economic stability before purchase. Furthermore, national income will shrink because of lower oil revenues, and some cities with a higher dependence on this fuel, such as Villavicencio and Bucaramanga, will have to put their urban expansion plans on hold.

Mortgage lending remains lively

Low interest rates have supported the financial system's capacity to originate mortgage loans. The bullish valuation of 10-year sovereign bonds, which enjoyed short-term increases, perhaps because of the fiscal uncertainty which the lower oil price has provoked in the market, has been helpful. They then corrected rapidly because of the tax reform, which has guaranteed 2015 public resources and, partially, those of the next three years. Mortgage interest rates were on average 10.9% in 2014, exactly the same as in 2013.

By type of loan, we have noticed a marginal reduction in the interest rate for non-social housing, edging down from 10.8% to 10.7%, even with a higher monetary policy rate, which was on average 81 basis points higher in 2014. **The mortgage rate on social housing continues to be one of the lowest on record, standing at 11.6%, a slight increase over 2013, when it was 11.2%, despite the sharp increase in inflation.** This variable is important because loans for social housing tend to have higher exposure to the "Real Value Unit" (*UVR* in the Spanish acronym), a variable which changes with inflation. In total, average inflation in 2014 was 2.9% and was 2.0% in 2013. In other words, not all the increase in inflation was passed through to borrowers, and even less so in the case of the increase in the monetary policy rate, thanks to the stability of sovereign debt.

Mortgage credit continues to gain share in the economy, now representing 6.3% of GDP (including securitisations and home leasing). This same measure stood at 5.9% at the close of 2013. During 2014, the positive performance in the credit for housing portfolio was driven by the originations made by credit institutions (making up 84% of the whole), which increased the balance of credit by over 20% nominal on average in the course of 2014. Second, the National Savings Fund (11% of the total), which increased by around 15% over the year. And third, the cooperatives and employee funds, albeit with a stake that was not even 5% of total mortgage credit, but with an average increase of 11%. **In total, the financial system currently finances 47.5% of new housing sales.**

By type of loan, there was more activity in non-social housing, whose credit balance continues to be the largest part of the entire portfolio, with 72%. This corresponds to the greater relative weighting of local currency in the portfolio, a typical way of funding higher value housing, with a stake of 79% in the whole vs. 77%

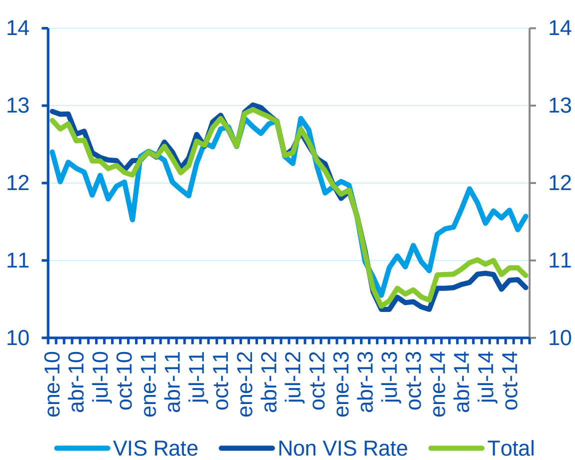
a year ago. The portfolio in UVR, a measure more frequently used in social housing, is growing at a healthy rate, but more slowly than the portfolio in COP. Altogether, there are around 960,000 ongoing loans in the financial system, of which 55% correspond to the social housing portfolio. That is, a higher number of low-value homes are financed, but a higher value of the loans comes from the non-social housing segment.

The mortgage portfolio continues to be one of the best performers, together with the trade portfolio, in terms of timely payment. The percentage of non-performing loans in the mortgage portfolio is just 2.44%, very similar to the average in the last three years. **The financial risk is also low, because of the limited penetration of mortgage credit in GDP**, if compared with similar economies, and because of the low proportion of the home value which is financed by the system: LTV (loan-to-value). So it is that, whereas with social housing nearly 60% of the property's commercial value is financed, in the case of non-social housing, this reaches 50%. These percentages are still well within the limit prescribed by Colombian law, which allows financing of up to 80% and 70% of each type of housing respectively. **Likewise, only 874,000 people over 18 (of those with identity cards registered in the financial system) are currently paying a mortgage**, whereas there are 21.6 million people over 18 who have some kind of financial product.

Since 2010 the financial system has significantly increased the number of loans it has originated for existing housing. Since that time, between 50,000 and 60,000 loans a year have been originated for this type of housing; between 2006 and 2009 there were around 40,000 a year, and prior to 2006 fewer than 20,000 mortgages were granted a year.

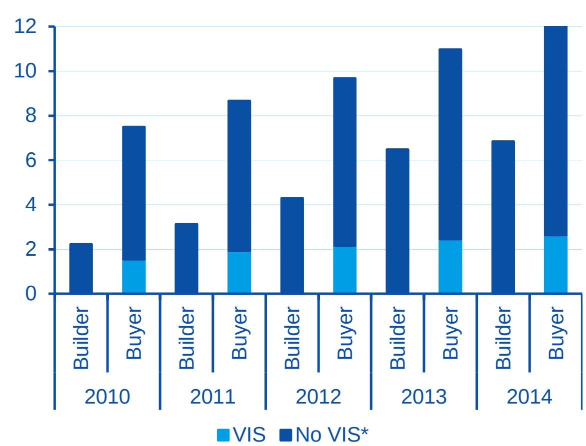
We expect the number of property transactions involving existing housing to increase in 2015, and with them the volume of credit. On the contrary, there may be a deceleration in the financing of high-value new homes, which will not be offset by the greater demand for loans for social welfare projects developed by the government. Altogether, we expect the balance of mortgage loans to continue growing at double-digit rates, although closer to 10% than to 20%.

Figure 4.3
Mortgage interest rates (E.A., %)



Source: BBVA Research and Superintendencia Financiera

Figure 4.4
Loans for housing, disbursements (COP trn)



* A source which does not differentiate between social and non-social housing was chosen for disbursements to construction.
Source: BBVA Research, Asobancaria and Superintendencia Financiera

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Este informe ha sido elaborado por la unidad de Colombia

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