Could Namibia Be Headed For A Housing Bubble?

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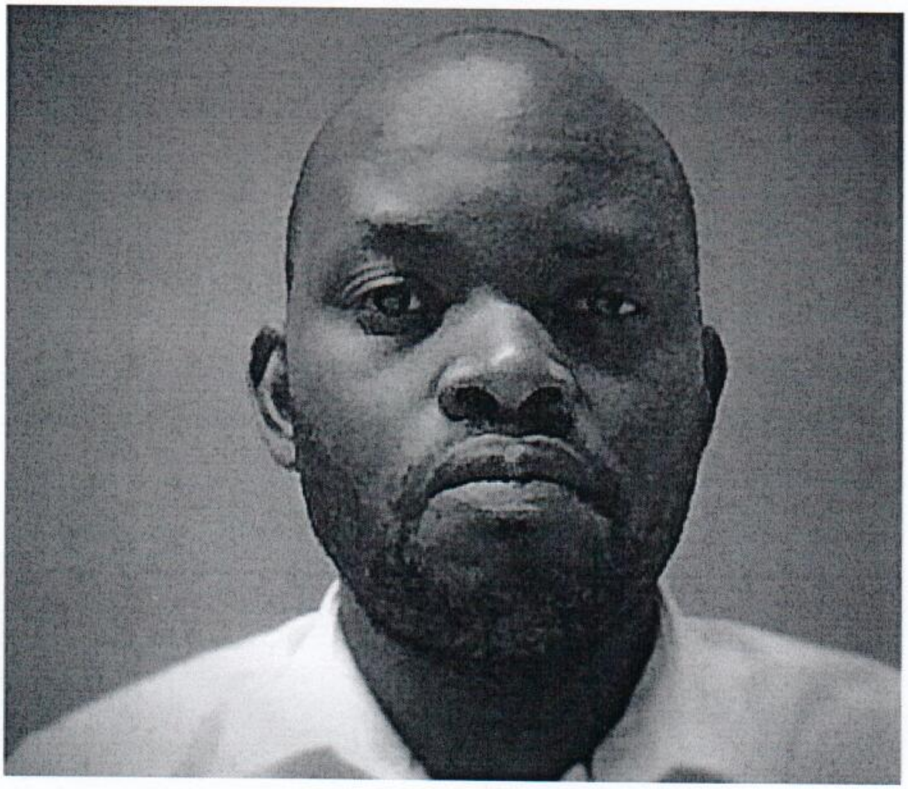

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A BUBBLE exists when the price of an asset is over-inflated, relative to some benchmark. Could Namibia be headed for a housing bubble, as was the case with the United States of America (USA), resulting in the 2008 world financial crisis? Commentators and analysts have written scantily about a possible housing bubble in the Namibian housing market.

Referring to the recent American housing crisis, perhaps we could understand the local dynamics. The term housing bubble came to prominence in the immediate aftermath of the 2008 global financial crisis. Were there any distinct red flags that preceded the crash? Just like tsunamis or earthquakes, financial crises are not easy to predict with certainty.

What is, however, interesting to consider is what led to America's housing bubble. Some of these factors could indeed be used as warning signs for the Namibian housing market.

Research shows that the following factors caused the US housing bubble: (i) low mortgage interest rates, (ii) low short-term interest rates, (iii) relaxed regulatory standards for mortgage loans and (iv) irrational exuberance by market players.

For instance, from 2002 to 2004, the Federal Reserve Bank of America, which is the equivalent of the Bank of Namibia (BoN), pushed the federal funds rate (our repo rate) down to historically low levels in an attempt to stimulate economic growth from the 2001 recession. Over the course of 2001, the Federal Reserve Bank lowered the federal funds rate 11 times, from 6,50% to 1,75%. However, in the mortgage market, this meant that payments were cheaper because their interest rates were based on the short-term treasury bill yields, which are based on the federal funds rate. Unfortunately, this in turn lowered commercial banks' incomes, which are based on interest-bearing loans. Consequently, many prospective homeowners who previously could not afford conventional mortgages were delighted to be approved for the interest-only loans. This situation created what we now know as sub-prime mortgages, which are loans essentially meant to be offered to prospective borrowers with 'bad' credit records.

As many unqualified borrowers entered the mortgage market, demand increased. As prices kept rising, many people bought homes for resale. They exhibited irrational excitement, a hallmark of any asset bubble.

While we cannot make comparisons between the American and Namibian housing markets, a few lessons can be learnt. Firstly, a large part of the

Namibian population, who qualify, depend on mortgages to finance their house purchase. Namibia has a well-functioning and developed mortgage market. Nonetheless, approximately 15% of Namibia's population can access traditional, collateralised home loan facilities. Secondly, most citizens, even if gainfully employed, simply do not have the financial means to enter the formal property market. Average housing prices, even for modest sized properties, far exceed affordable costs for most Namibians.

What is the current state of the Namibian mortgage market and the residential housing market? The first place to start is to scrutinise the number of residential units on the market for sale. The catchphrase in residential sales advertisements is "selling under valuation". This is uncharacteristic, as it contradicts the belief that property appreciates in value with time. Does this mean that residential properties have been over-valued in the recent past? Alternatively, is the residential property market simply self-correcting?

This situation may mean two things: either there is an oversupply of overpriced properties on the market by developers, or individual incomes have not caught up with the current house prices. Residential prices are bound to drop if the supply of property in the long-term outstrips effective demand. When that happens, then the housing bubble bursts.

A recent study by the Institute for Public Policy Research citing a ministerial statement reveals that the housing backlog in Namibia could be in excess of 100 000 units. The report, however, notes that despite this huge backlog, property developers are constructing residential units that are unaffordable to the majority of Namibians.

Apart from the sustained increase in house prices over the last few years, which are in fact declining, there are no indications of a housing bubble, US-style.

The local mortgage lenders are risk-averse. In the quest to limit risk in their home finance portfolios, commercial banks target only low-risk salaried borrowers. The BoN has been tightening regulations on mortgage lending, especially for secondary properties requiring prospective buyers to put down a deposit. Additionally, the BoN repo rate has been maintained at 6,75% over the last few years, with no indication to lowering it. No amount of financial engineering, such as securitisation, by local commercial banks, would allow individuals/businesses who do not meet the requirements for mortgages to apply for one.

Additionally, the Namibian market seems to be self-correcting, as evidenced by the significant discounts on properties on sale. This means that buyers, sellers and mortgage lenders are not exhibiting irrational, exuberant tendencies. All key actors in the market realise that property prices will not continue to skyrocket.

Namibia finds itself in a precarious situation, where the demand for housing outstrips supply, especially the supply of decent low to medium cost housing, of which there is an acute shortage. Therefore, the crisis in Namibia and specifically Windhoek may not be a looming housing bubble, but rather the inadequate supply of serviced land, limited finance options for low-cost housing and limited finances to municipalities to service land for housing.

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