Housing Market Monitor

Group Economics
Netherlands

10 April 2018

Housing market tightens

Philip Bokeloh
Tel. +31 (0) 20 383 2657
philip.bokeloh @nl.abnamro.com

-

- **Strongest price rise in seventeen years**
- **Transaction volume falling on supply constraints**
- **Tight conditions subdue mood in housing market**

The housing market is tense. The number of properties for sale is falling steadily. As a result, buyers have less choice, must decide faster and bid higher to stand a chance of success. In these conditions sellers have the upper hand, as is reflected in the soaring prices. As prices continue to climb, properties are becoming less affordable. Affordability will be further eroded if interest rates rise. Whilst the ECB is gearing up to adopt a less accommodative monetary policy, we do not foresee a dramatic rise in interest rates just yet. Against this background, prices can rise further in the near term. Based on the extremely strong surge in the first two months, we have raised our price forecast for 2018 from 6% to 8%. Our forecast for 2019 has been left unchanged at 5%. The decline in transactions, flagging confidence and the prospect of higher interest rates suggest that the pace of price increases is set to slacken. We have also left our transaction volume estimates as they were. Amidst the current supply constraints, transactions are harder to realise. This is already visible in the volume of house purchases, which declined in the first two months of the year - the first such fall in years. We expect this downward trend to continue, not just this year but also next.

Price and transaction forecasts

	Transactions (% y-o-y)	Prices (% y-o-y)
2017	13	7.6
2018	-5	8 (6)
2019	-5	5

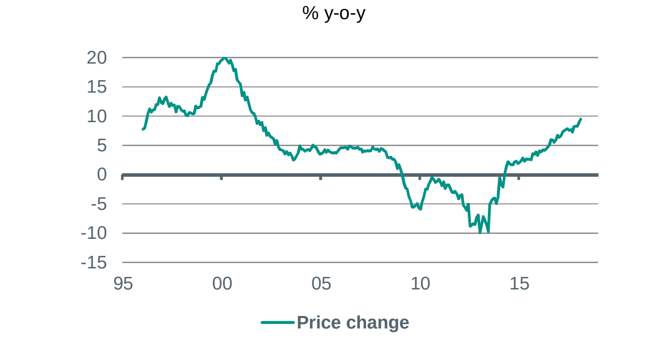
Source: ABN AMRO Group Economics

House prices soar

House prices continue to spiral upwards. According to Statistics Netherlands (CBS)/Land Registry, house prices were 9.5% higher on average in February than in the same month a year ago. It's a long time since prices rose that fast. We have to go way back to the year 2001 to find a comparable acceleration.

Prices are now in touching distance of the pre-crisis level. But significant differences remain between the regions. While prices in the Randstad conurbation and the major cities are hitting new records, the recovery elsewhere in the country is more sluggish.

House prices at 17-year peak



Source: Statistics Netherlands (CBS)/Land Registry

The fastest price rises are occurring in the higher price brackets, mainly due to strong home mover activity. Thanks to the price recovery, they are no longer thwarted by negative equity. In fact, many now have positive equity which they are using to trade up to a more expensive home.

Internationally, too, house prices are on the rise. The central bank of Dallas estimates that house prices in the developed economies rose by an average of 4.6% year-on-year in the fourth quarter. The Netherlands was among the clear front-runners with 8.3%. Only Ireland saw even faster price rises.

Mortgage rates remain ultra-low

One chief driver of the global price surge consists of the ultra-low mortgage rates induced by central bank monetary policies. Central banks are keeping official interest rates at modest levels and buying up debt to stimulate the economy and fan inflation.

However, with the economic recovery now well and truly underway, central banks see less need for further stimulus. The US central bank stopped buying bonds some time ago and has already implemented several interest rate increases in view of the tightening labour market and, recently, the extra public spending plans.

The European Central Bank (ECB) is expected to follow the American example in due course, starting with a reduction in the monthly bond purchases in preparation for interest rate increases further in the future. But Frankfurt is in no rush to taper its policy, particularly as inflation was only 1.1% in February, still well below the ECB's 2% target.

Monetary rebalancing will dampen the pace of house price increases. Since 2012, property price appreciation has persistently accelerated in the developed economies. This relentless upward momentum weakened for the first time in the third quarter, when prices rose 4.8% after the 5.5% increase in the preceding quarter. The Netherlands, where prices are still gathering pace, was an exception to this trend.

In a recent study into the impact of rising interest rates[1], the Amsterdam School of Real Estate concludes that the amount that people can borrow based on their income will fall if interest rates rise, even if incomes go up 3.1% as forecast in the coalition agreement. Their model also calculates that the inflation-adjusted price level will be about 6 percentage points lower than in the baseline scenario if mortgage rates rise by 1%. This price adjustment, however, will not occur with a shock but over a series of years.

Confidence dips

The prospect of higher interest rates has somewhat deflated the optimism surrounding the housing market. At the end of 2016, the Homeowners' Association (VEH) Market Indicator fell back from its peak to stabilise at a still historically high level.

Rising prices reduce affordability

Net housing expenses / net income (%)

Source: Calcasa

In recent months, this confidence indicator has signalled a renewed dip. One reason is affordability which, according to the Calcasa yardstick, has slightly deteriorated in the past quarters. Due to the sustained price increases, net housing costs as a percentage of net household income rose last year from 14.0% in the first quarter of 2017 to 14.8% in the fourth quarter.

Apart from the prospect of higher interest rates and reduced affordability, the weakening confidence indicator is also due to the supply constraints. In recent years, supply has shrunk as the pace of purchases accelerated. According to home search website *huizenzoeker.nl*, there were only 70,000 existing properties for sale in February, 43,000 less than a year ago.

Less supply means less choice for buyers. According to the Dutch Association of Real Estate Brokers (NVM), there were only four properties for sale for each buyer in the fourth quarter versus six a year earlier. And at the end of 2013, buyers could take their

---

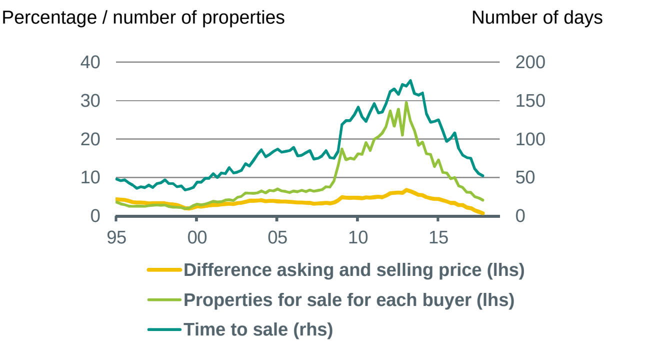
1 Conijn J., Francke J., Schilder F., Vries P. de, 'Effecten mogelijke rentestijging in de koopsector', January 2018.

pick from as many as thirty properties. All in all, therefore, buyers are having a harder time finding a suitable home.

In addition, the limited supply is forcing buyers to decide faster to secure the property of their choice. Properties sold in the fourth quarter were on the market for 52 days on average, almost a month shorter than a year ago and over four months shorter than in 2013.

Added to this, buyers must now bid more to stand any chance of success. According to the NVM, the difference between the asking and selling price has narrowed to only 0.7% - even less than in the late 1990s when house prices went through the roof, rising no less than 20%.

Signs of tension in the housing market



Source: NVM

To boost their chances, many buyers are waiving the inclusion of mortgage or inspection contingency clauses in the purchase contract. This can have serious financial consequences if the property turns out to have structural defects or if they fail to get a mortgage in time.

In order to alert buyers to the risk of omitting these contingency clauses, industry organisations have recently added mortgage and inspection contingencies to their model purchase agreements. But buyers are not obliged to include these clauses in the final contract.

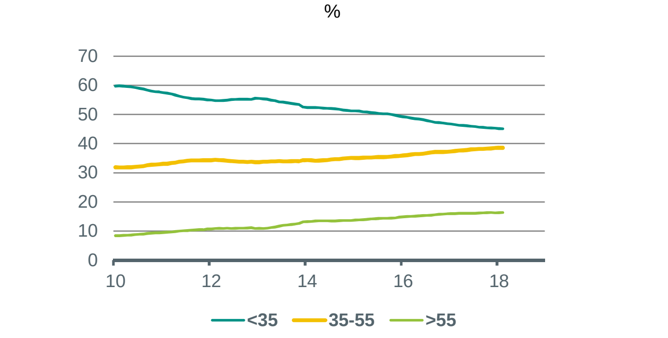
Falling transaction volume

In the current buoyant market, sellers are seizing the opportunity to raise their asking price. According to *huizenzoeker.nl*, the average asking price was EUR 364,000 in March, 12.7% higher than a year earlier. Asking prices thus appear to be rising faster than transaction prices, making transactions harder to conclude.

This drag on sales is already visible in the transaction volume. After the record level last year, the number of transactions fell back slightly in January and February, the first such decline in years. The total number of properties sold was 32,000, over 2,000 less than in the first two months of 2017.

The clearest weakening can be seen in the Randstad and the larger cities, where the shortage is the most acute and sales started to decelerate earlier. As the housing stock in the cities consists largely of apartments, it is logical that the share of apartments in total sales is falling while the share of detached houses, which tend to be situated in more rural areas, is increasing.

Young people have smaller share in house sales



Source: Land Registry

The share of young people in property sales is steadily falling. In 2009 the under 35s still accounted for 60% of the transactions, but their share has now shrunk to 45%. Even so, the number of transactions involving this age group increased from 73,000 annually in 2009 to 110,000 in 2017.

Moderate regulatory tightening

The number of transactions is mainly depressed by the lack of properties on the market. Another factor is the further tightening of the mortgage rules at the start of this year. Buyers are now only allowed to borrow 100% of the value of the collateral, as opposed to 101% last year. This means that they must contribute more of their own savings to buy a home. Young first-time buyers who have not yet had much chance to save are suffering the most from this restriction.

The less favourable tax treatment of home ownership will also play a role in the slowing sales. The highest rate taxpayers can now only deduct their mortgage interest at a rate of 49.5%, half a percentage point less than last year. In addition, those left with negative equity after selling their home are no longer permitted to deduct the interest on the residual debt. Interest on negative equity incurred in the 2012-2017 period can be deducted from tax over a period of fifteen years at maximum

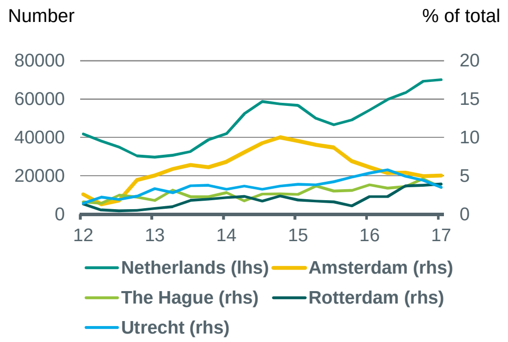
New-build sales rising

While the sale of existing properties is under pressure, new-build sales continue to gather pace. NVB data indicate that 36,000 properties were sold in the twelve months until end of February, 10% more than in the same month a year ago. Despite this increase, the sales volume is still lower than before the crisis when 40,000 new-builds were sold annually.

The decline in the number of transactions is not due to lack of demand. There is no shortage of that. Buyers are queuing up for the new-builds coming onto the market.

According to the project developers' association Neprom, three quarters of new-builds that went on sale in the third quarter found a buyer in the same quarter. The extremely short selling time of 55 days for apartments and 81 days for single-family homes indicates that the market is tense.

More building permits issued, particularly outside Big 4



Source: **Statistics Netherlands (CBS)**

The problem rather - as with existing properties - is a lack of supply. New-build activity is failing to keep pace with demand. After sinking to rock bottom in 2013, house construction rebounded. Since then, however, house completions have stagnated again. In view of the number of building permits issued since 2016 and the amount of work in progress at architects, the situation will improve in the coming years, but not sufficiently to meet demand. Also worrying is the low issuance rate of building permits in the large cities. This raises the question whether construction is taking place where the need is greatest.

Compared to a few years ago, project developers are clearly focusing more on home movers. Due to the rising number of completions in the higher price brackets, the average new-build price is rising. In the third quarter, the average price was EUR 312,000, 14% higher than a year ago and above the pre-crisis level.

Some relaxation of the spatial planning policy

One important cause of the lagging house construction is the chronic lack of building plans. Acknowledging this problem, the Minister of the Interior Kajsa Ollongren wants to encourage the regions to give house construction more priority. To this end, expert teams will be set up to help the regions remove obstacles. Moreover, new legislation to accelerate the procedures at local government level is being prepared. Finally, opportunities to revive abandoned construction projects via advance financing will be studied.

One new aspect of Ollongren's approach is that cities with the most acute shortages are now also allowed to consider development on green belt sites on the periphery. Previously, they were obliged to focus on the existing city. This latitude for expansion marks a change in course in the spatial planning policy. However, the minister has stipulated that construction outside the city must only be considered if strictly necessary. The authorities must first look at all available options within the city boundaries.

In addition, the minister intends to send a draft Vision Paper on the National Living Environment to the House of Representatives before the summer. As well as housing construction, this overall vision on the physical living environment will also encompass issues such as mobility.

Such a joined-up approach to housing and mobility ties in with a recently published article about the United Kingdom,[2] which notes that ratios of housing costs to incomes have risen in the past decades because the cost of transport has stopped falling and is now actually rising. According to the researchers, house prices remain stable as long as transport cost improvements keep pace with overall production growth. Before the Second World War, most countries met this condition. But this changed in the post-war era, when the improvement of transport technology stagnated.

Extra investments in infrastructure can therefore alleviate the price pressure in regions where housing markets are tight and thus help to dampen the regional price differences. A recent study of the CPB Netherlands Bureau for Economic Policy Analysis suggests that investments within a radius of 20 kilometres of large to medium-sized cities are probably the most profitable.[3] The researchers claim that urbanisation has a positive impact on wages up to a distance of 80 kilometres. The greatest effect takes place within a radius of 10 to 20 kilometres. A technological breakthrough that would reduce travel times and costs could extend this range.

Growing investor activity

In recent years the government has devoted more attention to affordable rented housing for middle earners with a monthly rent between EUR 700 and EUR 1,000. Supply in this price bracket is limited, which is a fundamental flaw. Because this middle segment caters to the growing need for flexibility due to changing conditions in the labour market and plays a pivotal role between the owner-occupied and social rented segments.

In January a committee headed by the former mayor of Eindhoven Rob van Gijzel presented its recommendations for improving the cooperation between the various stakeholders and tackling the shortage of rented housing in the middle segment.[4] These recommendations pay specific attention to the role of investors, who are more active in the housing market than before. They are more frequently involved in transactions and have increased their share in the housing stock.

A recently published study into the returns on various types of assets justifies the renewed investor interest in the housing market.[5] This international study spanning the period from 1870 to 2015 shows that the total return on rented housing (rental income plus value appreciation) is comparable to that on equities (dividend plus capital gains). But the return on equities is more volatile, as equity prices fluctuate more than the

[2] Miles D., Sefton J., 'Houses across time and across place', June 2017.
3 Verstraten P., Verweij G., Zwaneveld P., 'Opties om de stedelijke productiviteit te bevorderen', CPB Policy Brief, February 2018.
[4] Van Gijzel R., 'Samen bouwen aan middenhuur, Ervaringen van een jaar Samenwerkingstafel middenhuur', National government publcation no. 110203, January 2018.
[5] Jorda J., Knoll K., Kuvshinov D., Schularick M., Taylor A., 'The Rate of Return on Everything', 1870-2015, November 2017.

value of rented housing. Equities thus carry a higher financial risk, so that rented housing offers a more favourable risk-return profile.

Moreover, investments in housing are a good risk diversifier due to the low correlation between the movements of house prices and equity prices. Added to this, there is also less correlation between valuations in different countries than with equities.

Rented housing and equities yield comparable returns

	Rented housing		Equities	
	Return	Volatility	Return	Volatility
Australia	12.3	14.6	12.0	17.4
Belgium	14.7	9.9	10.2	23.8
Denmark	12.9	8.7	11.0	18.5
Germany	9.6	11.0	8.5	22.0
Finland	19.2	23.1	17.0	33.4
France	12.7	9.7	8.6	21.3
Italy	10.8	15.0	12.9	31.5
Japan	12.5	11.3	9.9	18.9
Netherlands	10.6	10.5	10.3	22.6
Norway	15.2	8.7	11.1	29.1
Portugal	15.4	11.5	13.6	35.2
Spain	10.9	12.7	11.3	21.0
UK	9.5	10.3	11.4	22.9
US	11.1	8.6	11.1	18.5
Sweden	11.4	7.9	11.1	20.7
Switzerland	8.6	6.2	8.2	18.6
Average	12.3	11.9	11.0	23.4

Source: Jorda J. 'The Rate of Return on Everything'
Yield is yearly nominal average, volatility in standard deviations

Saving estate agent costs

A final interesting publication in this context concerns the remuneration of estate agents.[6] Formerly, estate agents posted properties on the Funda website and charged about 2% of the selling price for their services. Since 2005, however, many estate agents apply a fixed fee of EUR 400 to EUR 1300. This is a much lower fee on average, but they also offer less service. The main difference is that the seller does the viewings himself. This new approach proves to be lucrative for sellers, as properties tend to sell much faster and at a 2.7% higher price.

The authors identify two reasons for the better outcomes when using a fixed-fee estate agent. The first is the personal interaction between the buyer and seller. When the seller does the viewing instead of the estate agent, the buyer gets better information about the property's state of repair and the kind of neighbourhood in which it is located. This information evidently persuades buyers to pay more. The second reason is the more efficient division of roles. If the seller does the labour-intensive viewings, the estate agent can concentrate on his specialisation: determining the value and

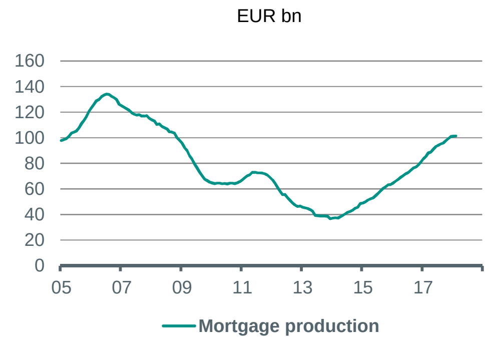
[6] Gautier P., Siegmann A., Vuuren A. van, 'Real estate agent performance and fee structure', February 2018, Vox.org.

negotiating the price. This division of roles reduces the labour costs, making it easier for an estate agent to reject a low offer and organise extra viewings if necessary.

Larger share of home movers and remortgagers in new mortgage business

The changing face of the housing market is reflected in the new mortgage business data. New mortgage volume dropped marginally in January and February, which is consistent with the falling transaction volume. In line with the sustained price increase, however, the average mortgage sum continued to rise. In the twelve months until end of February, 350,000 mortgages were extended for an average mortgage sum of EUR 289,000.

New mortgage business reflects housing market recovery



Source: Land Registry

On balance, new mortgage business rose to EUR 101.3bn, up EUR 16bn on a year ago. This, however, did not automatically lead to a much higher outstanding mortgage amount. The reason was the increase in mortgage repayments which, according to Statistics Netherlands, ran to EUR 672bn in the fourth quarter of last year, EUR 8bn more than at the end of 2016. As a percentage of GDP, the mortgage volume decreased in that period from 94% to 92%.

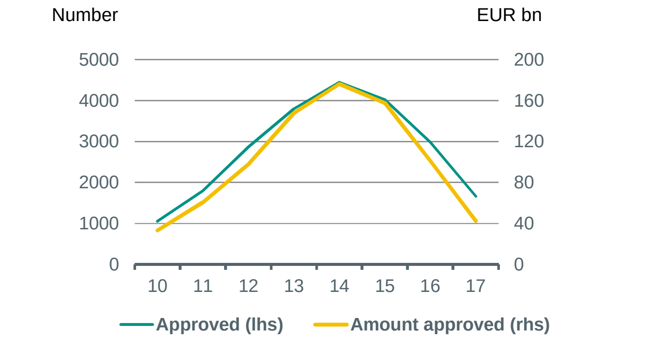
The new mortgage business data also indicate that the share of first-time buyers in property sales is shrinking. According to Land Registry data, first-time buyers accounted for 23% of new mortgage business, the lowest level ever. The percentage early in 2014 was 40. Their share has largely shifted to house movers, who now account for 56% of the new business, some 11 percentage points more than in 2014. In addition, the share of remortgagers has risen from 15% to 21%. The increased share of remortgagers is partly related to the high volume of new mortgage business in the 2005-2008 period, when many borrowers plumped for a fixed ten-year rate.

The current low rates make remortgaging an attractive option. A survey conducted for ABN AMRO Bank showed that most mortgage borrowers are aware that mortgage rates are historically low and that remortgaging can cut their monthly housing costs. Half of the respondents have already got their advisor to calculate what remortgaging can save them. Besides the potential savings, better mortgage conditions can be another factor in their decision whether to remortgage or not. In many cases however, the penalty interest holds them back, even though this can be deducted from tax.

Shifts in the mortgage market

According to the non-profit mortgage cooperative Hypotheek Data Netwerk (HDN), remortgagers are less likely to opt for a fixed-rate period of ten years or more than first-time buyers and home movers. Given their growing share in new mortgage business, this may explain the recent decline in the share of new contracts with a term of ten years or longer. According to the Dutch central bank (DNB), this share had dropped in January to 22% (annualised) of the new mortgage business versus 24% in the middle of last year. Nevertheless, most mortgage borrowers still opt for the security of a long fixed-rate period.

Receding credit risks: less NHG loss claims



Source: NHG

Despite this preference for security, fewer mortgages are being issued with a National Mortgage Guarantee (NHG). The reason is that the maximum NHG limit is lagging behind the average price increase, which means that fewer buyers are eligible for this guarantee scheme. In 2012 nine out of ten buyers opted for an NHG. Last year, that number was less than four. Predictably, therefore, the drop was mainly visible in the regions with the tightest housing markets where prices are rising fastest. But the guarantee scheme remains very popular among eligible mortgage borrowers. Of this group, seven out of ten use the scheme.

Also noteworthy is the growing presence of the self-employed in the housing market. HDN reports that the number of mortgage applications from self-employed people rose by over a third in 2017, with this group now accounting for one tenth of the 375,000 applications. Whilst this is still small given their share in the working labour force, it does indicate that the relaxation of the mortgage criteria for the self-employed in recent years is beginning to have effect.

Banks are also starting to focus more on sustainability. They want to give their customers information on the various opportunities for making their homes more sustainable and the resulting benefits. This is necessary as few buyers and homeowners know that they can borrow up to 6% of their property's value more to pay for certain energy-saving measures.

In addition, banks want to help customers make their homes more energy-efficient. To this end, customers can apply for special loans and set aside specific amounts without specifying in advance which energy-saving measures they propose to take. Finally, some banks give a discount on the mortgage rate for properties that meet the required energy-efficiency standard. In this way, the benefits of energy efficiency become more tangible in the form of lower energy costs, greater comfort and a better climate.

\

ABN·AMRO