# Dutch Housing Market Quarterly

February 2011

*Economic Research Department*

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## Introduction and Summary

The second-hand housing market continues to struggle, failing to recover in the fourth quarter of 2010, with the average house price falling 1.1% on a quarterly basis. Prices fell by 2% throughout the entire year, though with considerable variation across the board. While house prices recovered fairly strongly in the north of the Randstad urban belt, the opposite was the case in parts of the provinces of Overijssel, Drenthe and in Zuidwest-Gelderland.

The number of sales remains historically low. In the fourth quarter of 2010, house sales fell by over 7% compared to a year earlier, to some 126,000 (12-month totals). This means sales totals are fluctuating at the lower end of a bandwidth that was reached over a year ago (between 126,000 and 130,000 transactions). Not only are sales at a low level, houses also remain longer on the market.

December showed a sharp decline in forced sales compared to a year earlier. This is an indication that households are still able to meet their mortgage payment obligations, possibly thanks to the recovery on the labour market. Likewise a positive development is that there were 3,000 fewer houses on the market in January than in October. However, it is too early to call this an upturn in the sector, as there was a similar drop in January in previous years. Nonetheless, it may be a sign of some recovery in the market, which together with the unchanged policy on mortgage interest relief leads us to expect a good first quarter for the Dutch housing market. However, or the rest of the year, we fear that new policy measures and other market factors may hamper further recovery.

We envisage a decline in the affordability of purchasing a house in 2011. This will be due to changes to the maximum financing burden percentages, the possible tightening of repayment conditions and the expected rise in mortgage rates. The reduced affordability will in turn have a downward effect on prices, leading to an expected 2% price drop in 2011. At the same time, the number of transactions will likely remain unchanged (around 130,000), partly due to the increased pressure on vendors to sell properties that have been on the market for some time.

Despite a decline in the number of properties on the market, there are still a lot of houses for sale. However, this is offset to a certain extent by the sharp decline in new housing completions, ensuring that the supply does not expand further. Accordingly, new housing output is not expected to recover for some years, particularly in view of the low number of building permits issued. Consequently, 2011 will be another tough year for the construction sector.

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# Existing homes market

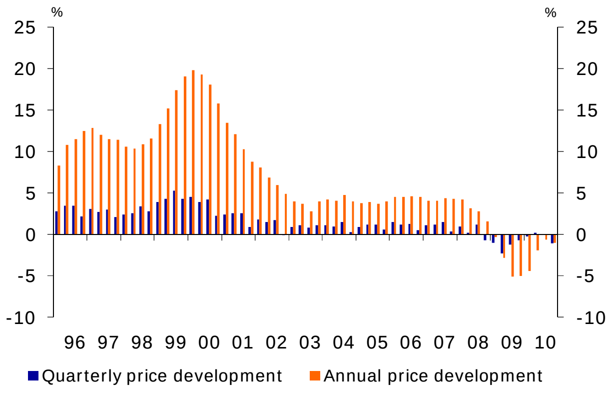
**The sting is in the tail**

For a long time it seemed 2010 would be the year when house prices would stabilise. Up to and including the third quarter of the year, the Existing Homes Price Index (PBK-index) of Statistics Netherlands / Dutch Land Registry fluctuated around the level of late 2009. The second and third quarters showed slight quarterly increases, of 0.3 and 0.1 percent, respectively. However, these were fully cancelled out by a price drop of 1.1% in the fourth quarter, compared to the third (figure 1). On balance, the average house price declined by 2% in 2010 compared to the 2009 average. Besides the negative contribution of the fourth quarter of 2010, this decline can be largely attributed to carry-over effects from 2009 (-1.7%).

The price drop in the fourth quarter of last year marks a new low for the PBK index. The current price level averages almost 7% below the level reached in the third quarter of 2008, when the index registered an all-time high (figure 2). The PBK index is expected to register a further drop in 2011, of 2 percent.

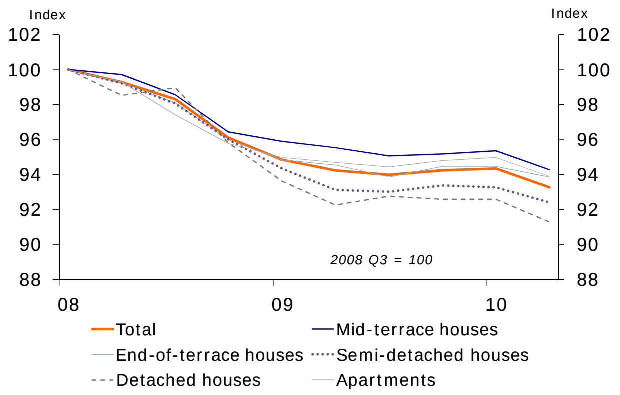
The first quarter of 2011 may well show a slight revival, thanks to the unchanged policy on mortgage interest relief of the Rutte cabinet. This may have created an incentive for some house-seekers to become active again on the market, although any change will only be visible in the index after a lag of some three months. The delayed effect is caused by the fact that house sales are registered by Statistics Netherlands/Land Registry at the time of transfer of ownership and not at the time of sale. Later in the year, we expect other factors to gain the upper hand, such as the large supply of houses, the anticipated interest rate rise and growing difficulties for first time buyers to get a foot on the property ladder.

**Figure 1: House prices decline in fourth quarter**




Source: Statistics Netherlands

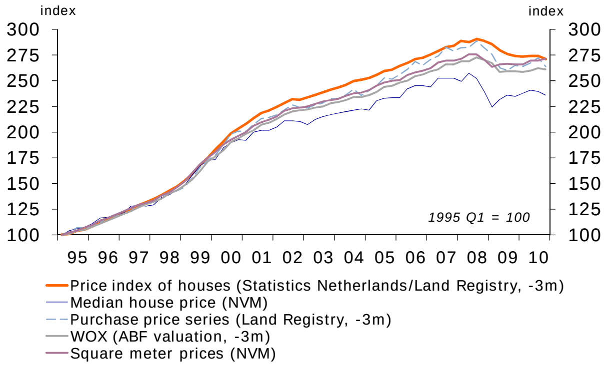
**Figure 2: Development by house type**




Source: Statistics Netherlands

Moreover, the sharp decline in late 2010 has contributed to a negative carry-over effect of almost 0.7%.

**Figure3: Price development of different indicators**




Source: Statistics Netherlands, NVM, ABF valuation, Land Registry

**Carry-over effect**

In the Housing Market Quarterly we publish both year-on-year changes and annual data. For the year-on-year figures, two periods are compared, for example the fourth quarter of 2009 and the fourth quarter of 2010. In the case of annual data, the average levels of two years are compared, and this is where carry-over effects may play a part. Thus, the quarterly pattern in, for instance, 2009, may affect the annual figure for 2010. If the value of the index in the fourth quarter of 2009 is lower than the annual average for that year, then a negative carry-over effect occurs (and vice versa). This is because the average value without changes in 2010 is lower than the previous year. The extent of the carry-over effect in this example is determined by the fluctuations in the index for 2009.

Other indicators show a similar picture (figure 3). The purchase price series of the Land Registry, the WOX series of ABF Valuation and the median house price of NVM (Dutch Association of Real Estate Brokers) all show a price drop in the fourth quarter. An exception is the price per square metre of the NVM. In its recent quarterly report, the NVM reports that since February 2010, estate agents are being encouraged to be more accurate in measuring living space. This may have resulted in a change to the number of square metres given as opposed to the price. The NVM is currently investigating the effects of this development on the series. There is a possibility that a break with trend has occurred, which means earlier values can no longer be compared with current figures.

The PBK index shows a price drop across the board. Prices declined both in the cheaper price bracket – terraced houses and apartments – and in the more expensive segment – semi-detached and detached houses. The price decline took place within a bandwidth of 0.7 and 1.4 percent, vis a vis the third quarter of 2010 (figure 2). Moreover, the number of sales remains low, which means the price analysis is based on a thin market.

**Further drop in number of transactions**

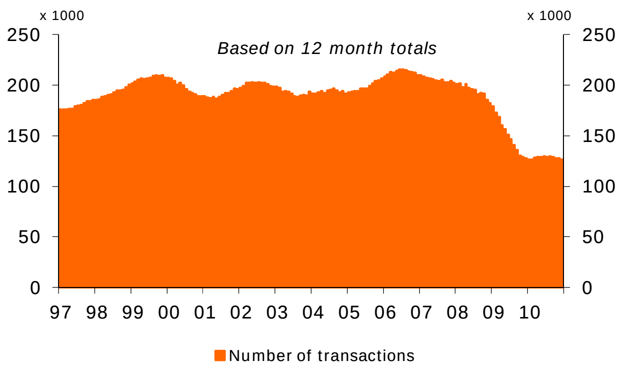
Since late 2009, annual house sales have fluctuated within a bandwidth of 126,000 to 130,000. In December 2010, Statistics Netherlands/Land Registry recorded 126,127 transactions, which is at the lower end of the range and represents the lowest point for some time (figure 4). This is because the number of transactions in the fourth quarter declined by 7.4% compared to the same period a year previously. In the fourth quarter of 2010 34,093 homes changed hands, compared to 36,811 in the fourth quarter of 2009. However, there was considerable diversity within the various market segments. Compared to a year ago, sales of semi-detached houses were down by 0.5%, and sales of apartments were down by 10%. In the other three segments, 6% to 7% fewer houses were sold. The fact that both prices and transaction numbers have reached a new low is a sign that the housing market has further deteriorated. The mismatch between demand and supply continues.

**Effects of policy changes not yet known**

Because house sales are not registered by Statistics Netherlands/Land Registry until the time of conveyancing, we cannot draw any firm conclusions from the fact that the new cabinet has left the mortgage relief facility unchanged. After all, there is a lag of three to four months between the time of purchase and transfer of ownership. This means that house sales that have been agreed since last September will mostly only appear in the figures of Statistics Netherlands/Land Registry in the first quarter of 2011.

In contrast to Statistics Netherlands/Land Registry, the NVM registers house sales at the time the agreement is signed. Accordingly, NVM data come out three to four months earlier. On the downside, the NVM figures don't include house sales that take place without an NMV affiliated estate agent. Nonetheless, on the basis of the NVM data we can cautiously conclude that there has been a slight rise in the number of transactions during the fourth quarter of 2010.

**Figure 4: Low number of transactions**




Source: Statistics Netherlands

**Figure 5: Number of houses on the market**

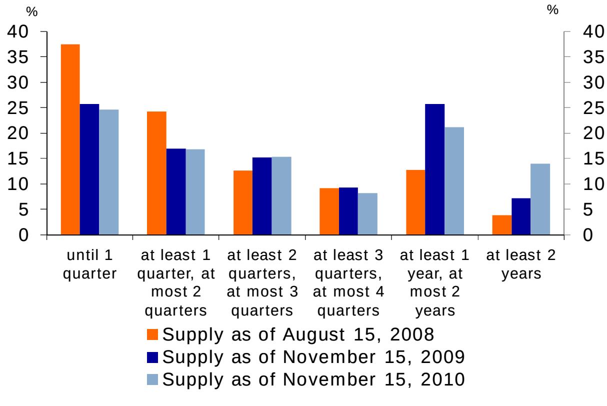

Source: Huizenzoeker.nl

However, it is too early to speak of a firm trend. Not all indicators that correspond to the NVM data period point sufficiently clearly in the same direction. For example, in December 2010 there were over 181,000 houses on the market (figure 5): over 5,000 more than three months earlier and 21,000 more than a year ago. Although there was a drop in the number of unsold homes in January compared to (-3.000), this is insufficient to indicate a turnaround. In previous years the number of houses on the market likewise declined in January only to rise further later on.

Not only were there more houses for sale last December, but they also took longer to sell. According to the NVM, in the fourth quarter, houses were on the market for an average of 249 days. This compares to an average of 243 days in the third quarter of the year. The rise in duration was particularly marked in the cheaper segment. In the case of apartments, the length of time on the market rose from 202 days in the third quarter to 214 in the fourth quarter. Mid-terrace houses went from an average of 187 days to 200 days.

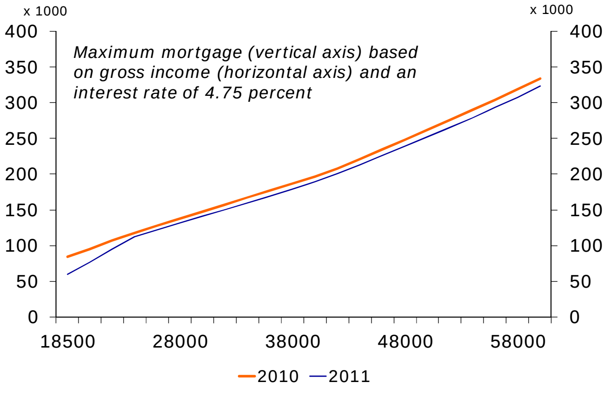
Homes are taking longer to sell, and at the same time there are a growing number of houses on the market for over two year, and now accounts for 14% of all houses on the market. This compares to 4% at the start of the crisis (figure 6). This group is fed mainly by houses that were put up for sale at the start of the crisis. This can be concluded from the fact that the number of houses for sale for ‘more than a year’ increased exponentially from November 2009. Now, a year later, this group feeds into the group of houses for sale for ‘over two years’.

**Figure 6: Homes take long to sell**




Source: NVM

**Figure 7: Borrowing less with the same income**

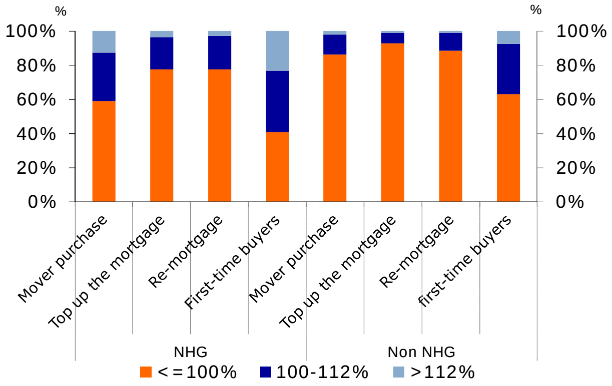



Source: Nibud

**Effect of policy changes in 2011**

On 10 November 2010 Nibud (National Institute for Family Finance Information) announced the new maximum financing burden percentages for 2011. This percentage enables the maximum mortgage covered by the National Mortgage Guarantee (NHG) to be calculated, on the basis of income and interest rate. The new measure means that in 2011, households will be able to borrow less than in 2010, given the same income and interest rate (figure 7). The reason is that a larger percentage of disposable income is earmarked for healthcare and pension premiums, leaving less to spend on a mortgage.

**Figure 8: Ratio of mortgage to collateral per category**




Source: Rabobank

Households with a gross income of less than 24,000 euro will thus experience the greatest difficulty in applying for a mortgage. In some cases they will be only able to borrow 20% less than before. Those earning a gross income of between 24,000 and 40,000 euro will be able to borrow 4% less on average; and those earning over 40,000 will be able to take out a mortgage of 3 percent less, on average. Since first-time buyers are mainly in the first two categories, they will have the greatest difficulty in entering the property market, particularly since they are relatively most dependent on external financing (figure 8). In the case of over 59% of NHG mortgages issued to first-time buyers, the mortgage amount exceeds the value of the property. This can be seen in figure 8 in the fourth column from the left. The dark blue and light blue section refers to the share of mortgages that are issued on the basis of collateral that is less than 100% of the value of the property.[1]

In the case of mortgages that fall outside the NHG guarantee, the share is almost 37%. The fact that first-time buyers will find it more difficult to enter the property market in 2011 will have a knock-on effect on the whole market, with potential house vendors unable to move up the property ladder, since they are unable to sell to newcomers.

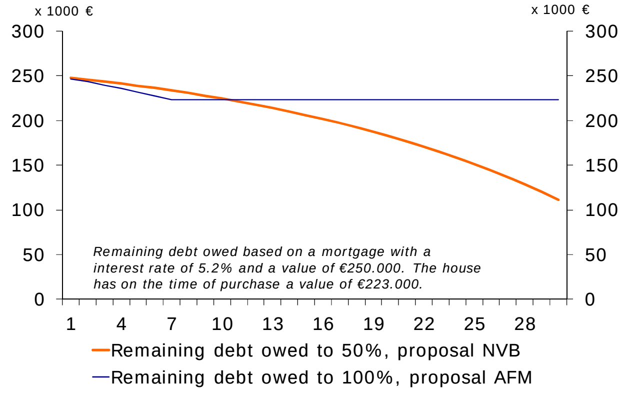
[1] The NHG assumes a maximum borrowing capacity of 112% of the purchase value, including renovation costs. Rabobank (non-NHG) assumes a maximum borrowing capacity of 125% of the asking price. In order to compare the data, the NHG figures have been adapted. If all the boxes are filled in correctly, the difference is slight. The main difference can be found where there have been renovations, when there is less certainty.

Another issue is the debate about reducing the mortgage debt. The proposal by the AFM (Financial Markets Authority)[2] will oblige homeowners with a mortgage that exceeds the value of their property to reduce the mortgage debt within seven years to below 100% of the purchase price. This proposal would only apply to homeowners who have a non-NHG mortgage. In the alternative proposal of the banks, as presented by the NVB, all home owners would have to reduce their net mortgage debt within 30 years to 50% of the market value of the house at the time of purchase.[3] The main difference between these proposals, is that in the AFM proposal, households will have to redeem their mortgages at a faster pace, while the banks' proposal requires that considerably larger sums are redeemed (Figure 9).

The NVB proposal has three main advantages vis a vis the AFM proposal. First, the long-term risks for the consumer are reduced, since the ratio between the mortgage amount and the property value improves over time. This will have a significant, positive influence on financial stability in the long term. Second, the monthly payments in the NVB proposal remain stable and in the early years are significantly lower than in the AFM proposal (Figure 10; for the purposes of comparison, we assume the maximum annual payment for an income of €49,000). This is an important advantage, since households are at their most vulnerable in the early years, both on account of collateral that changes little in value and income that has not yet increased appreciably. A third advantage of the NVB proposal is that it incurs less administrative charges.

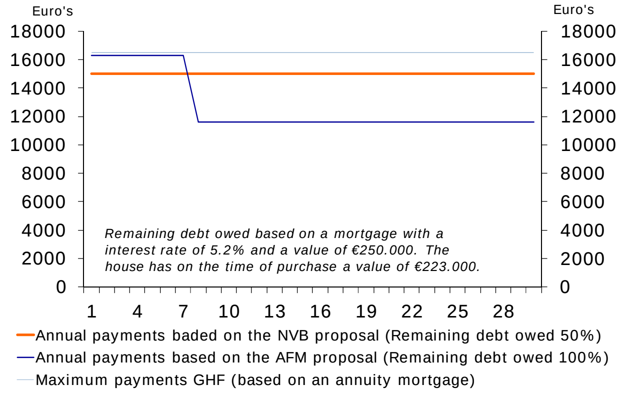
[2] AFM (April 2010), Feedbackstatement Consultatiedocument toetskader hypothecaire kredietverlening (http://www.afm.nl/nl/professionals/regelgeving/thema/toetskaderhypotheken.aspx)
[3] NVB (February2011), Normen voor hypothecaire kredietverstrekking (http://www.nvb.nl/scrivo/asset.php?id=573433)

**Figure 9: Remaining debt**




Source: Rabobank

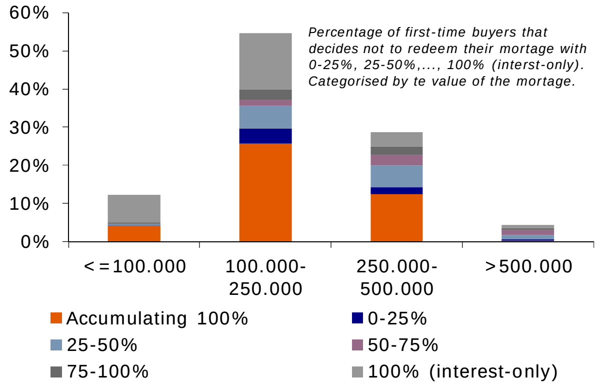
**Figure 10: Gross annual charges: a comparison**




Source: Rabobank

As is the case with the financing burden percentages, it is mainly first time buyers who will be hampered by these measures. This is because newcomers to the housing market are largely dependent on external financing and because they often opt for a mortgage based on interest-only terms.

**Figure 11: How do non-NHG newcomers pay?**




Source: Statistics Netherlands/Land Registry

The current data show that 9 percent of newcomers will be affected by the new AFM measure. This group is composed of the percentage of first-time buyers who don't have a NHG mortgage (35% with Rabobank), multiplied by the percentage of first-time buyers that now opt for an interest-only mortgage (26%; figure 11). In the banks' proposal the absolute number of newcomers affected will be higher, since the include NHG mortgage holders. The group will be further increased since the plans include newcomers who had originally opted for a mortgage of which less than 50% had to be repaid. Current data indicate that this accounts for 16% of new market entrants.

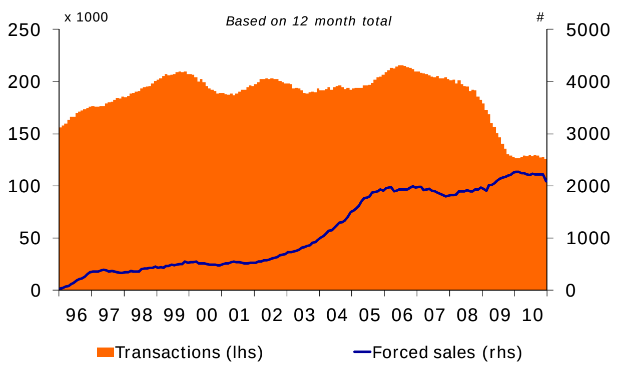
Despite the fact that a larger group would be affected by the new measure in the NVB proposal, the direct impact of the banks' proposal is likely to be smaller, since monthly repayments rise less sharply in the initial period. (Nominal) wage rises result in a pro rata reduction in monthly costs. Under both proposals, financing options for first-time buyers (as well as existing homeowners) will be reduced, although the NVB proposal will cause less disruption to the dynamic on the housing market.

### Abolution of stamp duty?

Elco Brinkman and Wienke Bodewes, chairmen of house-builders associations Bouwend Nederland and NEPROM respectively, recently called for a temporary moratorium on transfer tax for first-time buyers. This would enable newcomers to access the housing market more easily, thus facilitating movement along the property ladder and enabling people to trade up in line with their income. It is also claimed that this will not sap funds from the exchequer, but in fact will generate revenue, since those trading up will pay stamp duty. Furthermore, an increased number of house sales will boost sales of durable consumer goods which typically go hand in hand with moving house.

We endorse the view that this measure would lead to a temporary boost to the number of house transactions. However, it will not constitute a lasting solution to the problems on the housing market.

**Figure 12: Forced Sales**




Source: Statistics Netherlands/Land Registry

### Expectation for 2011

Falling prices combined with a decline in transactions are an indication that the housing market remains under pressure. Adding to the pressure will be the new financing burden scale of Nibud, which will have the effect of reducing the maximum mortgage sum issued under the NHG. Further pressure may possibly come from new AFM repayment requirements. First-time buyers, and as a consequence those trading up as well, will feel the effects. On balance, we don't expect a strong recovery for the housing market in 2011. Instead, the market will have to find a new equilibrium. This means that prices are likely to drop by 2%, with transactions remaining around the current level of 130,000 for the year.

### Fewer forced sales

There were 128 forced sales in December, putting the 12 month moving average at 2,086 (figure 12). This represents an improvement on the 12-month average recorded in September (2,220). This is due to an improvement in December, when there were 137 fewer forced sales, year-on-year. The improvement can largely be attributed to the economic recovery and the accompanying drop in unemployment. Although activity on the housing market is still subdued, the decline in forced sales heralds a positive development, showing that households are in a good position to meet their payment obligations.

The low percentage of forced sales in the Netherlands (0.05% of the existing private housing stock on an annual basis) can be attributed to a number of factors. These are the country's comprehensive social safety net, the long-term fixed mortgage rates issued by many mortgage lenders and measures to prevent excessive leverage accumulation.

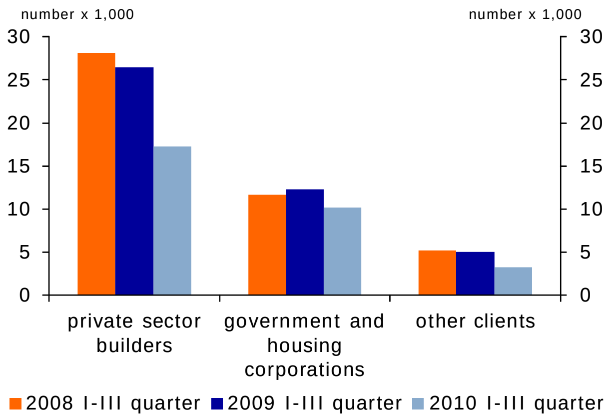
In the future it will become easier for individuals to participate in executor's auctions, thanks to internet access. The Justice Minister, Yvo Opstelten, submitted a draft bill for advice to the Council of State on 31 January 2011. The proposed legislation aims to ensure that houses sold at auctions are not bought up by a select group but are accessible to a wider public, thus allowing the market to work better and improve price transparency.

## New Completions

In the first 10 months of 2010, almost 36,000 new homes were completed - 30% less than the same period a year earlier. The decline took place almost entirely in the non-rental sector, reflecting the steep drop in hew home sales in the second half of 2008 and the first half of 2009 (over 45% on an annual basis). The decline in construction output is most marked in the private sector, but investment by housing corporations has also been eroded (figure 13). Because they are saddled for longer with unsold property, the housing corporations have less capital available for investment. Furthermore, the decline in property prices impacts negatively on the value of their holdings, reducing their (future) borrowing capacity.

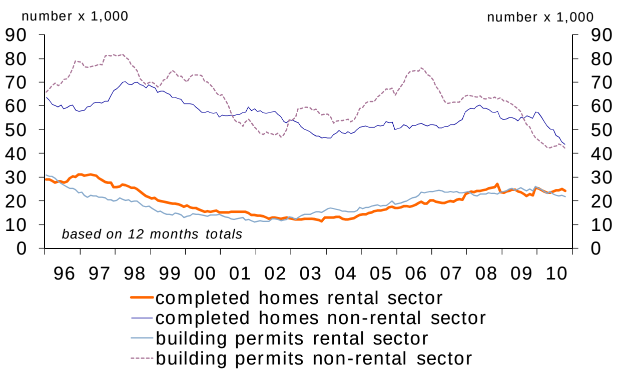
The current situation leads us to believe that there will be no strong recovery in new construction in the coming months. A recovery in housebuilding requires the housing market to first pick up. In January this year, there were an estimated 178,000 houses for sale – almost double the number at the start of the crisis in the fourth quarter of 2008. And sales of new construction projects are progressing slowly. Despite a doubling of sales figures in the first half of 2010 compared to the all-time low of 7,500 in the same period of 2009, sales are still 40% lower on average than in the years 2005-2007. Added to this, the proposed tightening of financing conditions by the AFM and possibly stricter requirements for NHG eligibility will further curtail the borrowing capacity of potential house-buyers. This may put further pressure on the incipient recovery in new home sales in the coming period. A further reason not to expect a surge in new housing output this year can be found in the declining trend in the issuing of building permits (figure 14). On the whole, we expect the number of new housing completions to stabilise at the 2010 level of around 55,000.

**Figure13: New housing completions by client**




Source: Statistics Netherlands, Rabobank

**Figure 14: Sharp drop in building permits, especially non-rental sector**




Source: Statistics Netherlands, Rabobank

## Interest Rate Developments

During the past year, both the average variable mortgage rate and fixed interest rates have declined. They are now almost 2.5% points and 1% point respectively below the peak of autumn 2008 (figure 15). In view of the developments on the money market and capital market, a steady upward climb of interest rates is to be expected during the course of this year.

**ECB keeping a close eye on inflation**

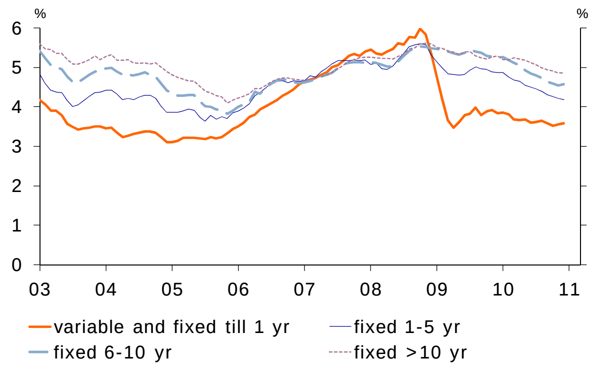
Inflation in the eurozone rose to 2.4% in January this year – well above the ECB's target rate of 2%. The rise was mainly driven by temporary factors, such as higher energy and fuel prices, and does not imply that the ECB will raise its policy interest rate in the short term. For this to happen, the eurozone economy would have to grow faster than current expectations and core inflation would have to continue to rise. We don't expect the central bank to raise interest rates until the end of the year (figure 16). In any case, the economic and financial situation in the peripheral eurozone countries remains precarious. The fact that the banks of southern Europe in particular are dependent on ECB liquidity facilities means that the ECB will cautiously further restrict its extraordinary liquidity provision.

**Market financing important for the banks**

Long-term market financing and private deposits are becoming increasingly important for the banks, all the more because of strict liquidity requirements imposed by the markets and the Basel III conditions that are yet to be implemented. Dutch banks are relatively dependent on market financing, because private deposits are considerably smaller than loans to the private sector (figure 17).[4] On the one hand, the Dutch prefer to lodge their savings with insurance companies and pension funds. On the other hand, mortgages are relatively

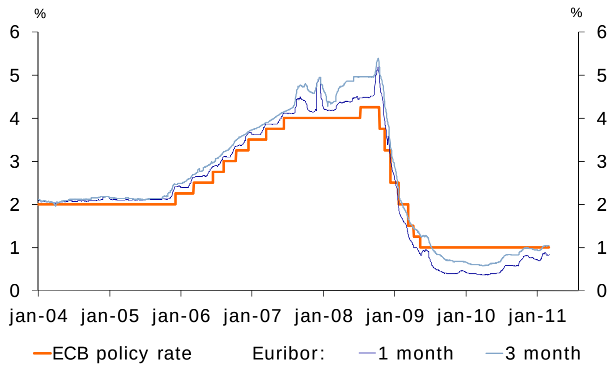
[4] For more information see "*Kredietcrisis neemt de hypotheekfinanciering eurolanden de maat*" [Credit crisis affects eurozone mortgages], Rabobank Special Report 2011/02

**Figure 15: Drop in mortgage rates last year**




Source: DNB

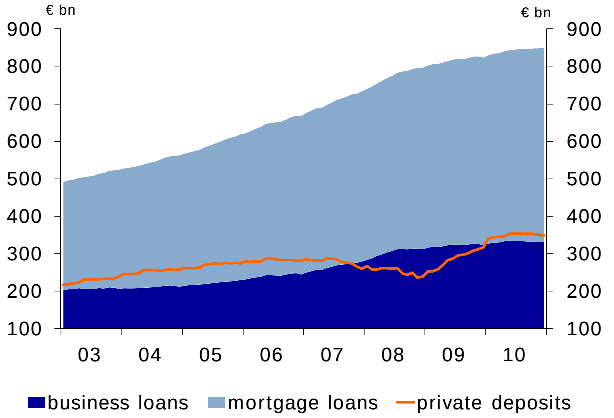
**Figure 16: Rise in money market rates**




Source: Reuters EcoWin, Rabobank

high on account of favourable tax treatment of mortgages for owner-occupiers. According to the most recent data from the Dutch Central Bank (DNB), this so-called *retail funding gap* amounts to some € 500 billion. Market financing conditions for the Dutch banks are improving steadily. A third of total securities issued in Europe (€ 77bn) are now destined for Dutch financial institutions. Last year, € 39 bn worth of debt instruments were issued without making use of the state guarantee. However, risk premiums are still well above pre-crisis levels (figure 18).

**Figure 17: Private deposits insufficient to finance bank credit**

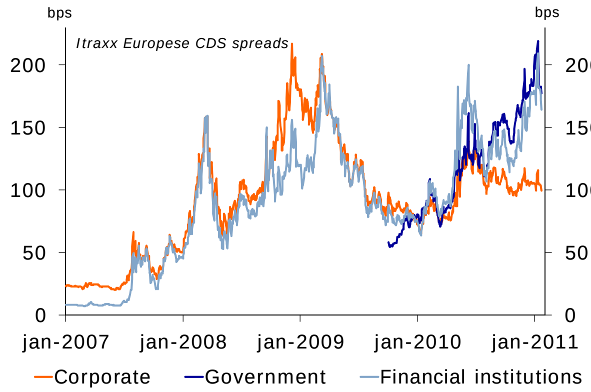



Source: DNB

### Capital market: calm again?

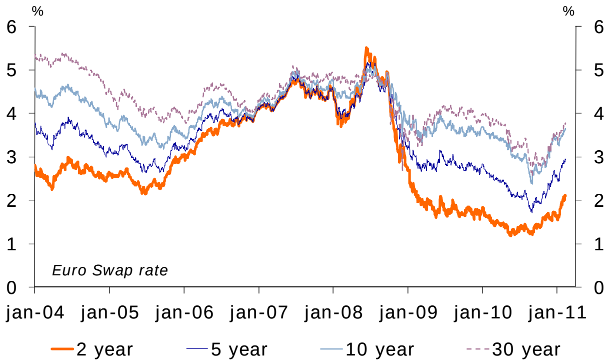
It appears that the relatively strong global economic recovery visible in late 2010 is set to continue into the spring, although at a somewhat slower pace. Although interest rates show strong divergence in the eurozone, the bond issues in Spain, Portugal and Italy appear to have been reasonably successful. This has calmed the acute turbulence for the time being at least. Moreover, the expansion of the financial safety net (EFSF) seems to have removed some of the fears concerning a failure to find a solution to the European debt problems. Together with favourable economic developments, lower risk aversion has led to a slight rise in capital market rates (figure 19). This upward trend is expected to persist for the rest of the year. However, the debt problems in the eurozone periphery remain sizeable, and it is unlikely that an effective solution can be found any time soon. During the course of the year anxiety could well return, and increase risk aversion could push down the 10 year euro swap rate again.

**Figure 18: It costs money to borrow money**




Source: Reuters EcoWin, Rabobank

**Figure 19: Rise in capital market rates**




Source: Reuters EcoWin, Rabobank

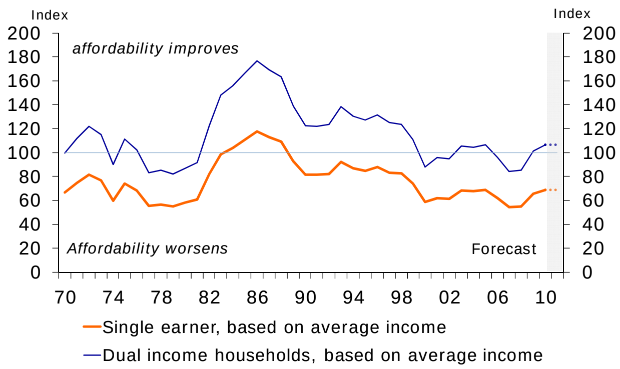
## Affordability

The Rabobank affordability index is a measure of the affordability of purchasing an average house for a household with an average income in the Netherlands. It is essentially a snapshot, which means it does not take account of any changes in, for instance, the income situation as a result of unemployment. If the affordability index is 100, this means that for an average household income and an average priced house, the gross monthly burden is 30% of gross income. If the affordability index exceeds 100, then the gross monthly burden is less than 30% of gross income, and vice versa.

The affordability index for dual income households in 2011 will amount to 106 (figure 20), which means that these households will spend just under 30% of their income on home repayments. This is comparable to the level of 2010, on balance. However, the breakdown of the index shows that some changes have taken place in the various indicators. On the one hand, affordability will increase in 2011, due to the expected decline in house prices. However, this effect will be cancelled out by the expected rise in mortgage rates, pushing up the monthly repayments (for variable-rate mortgages). Average income in likely to remain unchanged. The affordability index for single-income households in 2011 amounts to 69, which implies that it will be difficult for this group with an average income to gain entry to the housing market. The result is the same when the maximum mortgage and the average price of an apartment or mid-terrace house are weighed up against each other (figure 21).

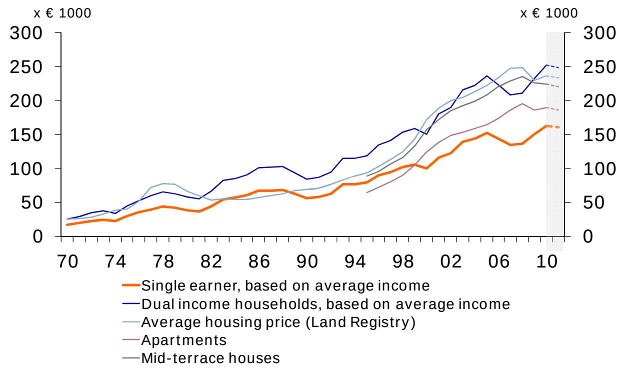
The affordability index is calculated on the basis of the assumption that households spend 30% of their gross income on house-related monthly payments. Other fixed charges will also rise, however, due to an increase in pension and healthcare premiums. This leaves less room for spending on housing, which has not been factored into the equation. In reality, therefore, affordability will deteriorate somewhat in 2011.

**Figure 20: Affordability the same in 2011**




Source: CPB, CBS/Land Reg, Reuters EcoWin, Rabobank

**Figure 21: Maximum mortgage insufficient**



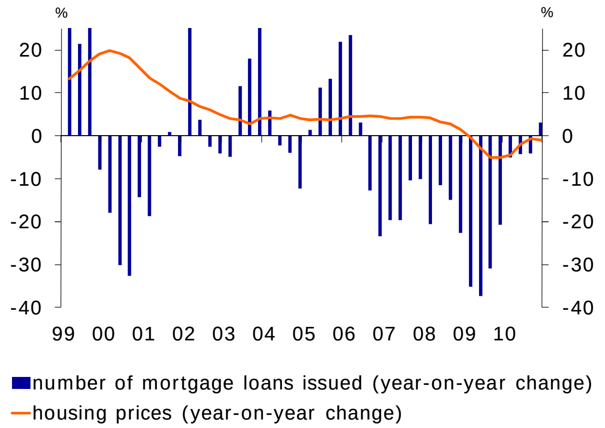

Source: CPB, CBS/Land Reg, Reuters EcoWin, Rabobank

## Mortgage Issuance

According to Land Registry data, over 72,000 mortgages were issued in the last quarter of 2010. This is 19,000 more than in the first quarter of last year, and 3% more year-on-year. This is the first time since the second quarter of 2006 that the number of mortgages issued has increased year-on-year (figure 22). A possible reason for this is that potential buyers, concerned about more stringent requirements for a NHG mortgage as well as the new AFM financing conditions in 2011, decided to pre-empt these developments and bring their mortgage agreement forward. The date on which a mortgage offer is made determines which NHG criteria will apply. Nonetheless, the number of mortgages issued for the year as a whole has hit the lowest level since the mid-90s. Currently, only 250,000 mortgages are being issued annually, compared to a level of 400,000 to 500,000 before the crisis.

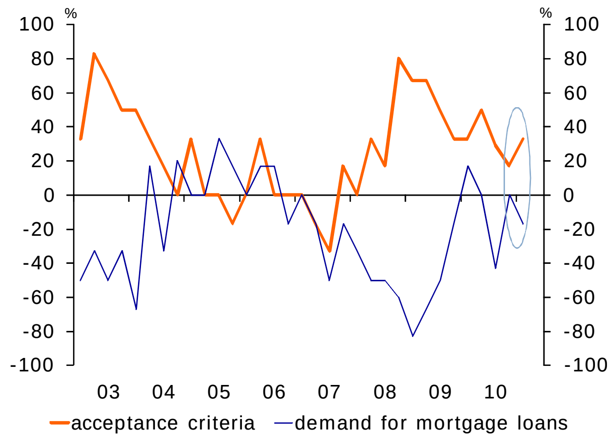
We expect the number of mortgages issued this year to remain around last year's level. The more stringent requirements will make it more difficult for first-time buyers, which will have a knock-on effect on those wanting to trade up. The number of banks that have indicated an intention to tighten credit conditions in the first quarter of this year has increased again for the first time since the second quarter of last year (figure 23). Thanks to a combination of more stringent regulations and income stagnation in 2011, the banks anticipate a fall in demand for mortgages in the first three months of this year. It is questionable whether the intensification of government regulations and of measures that will reduce the borrowing capacity of potential house buyers might not do even more damage to an already fragile housing market.

**Figure 22: Mortgage Issuance**




Source: Statistics Netherlands, Land Registry, Rabobank

**Figure 23: Mortgage credit supply and demand**




Source: DNB

## Impact of the Basel liquidity requirements

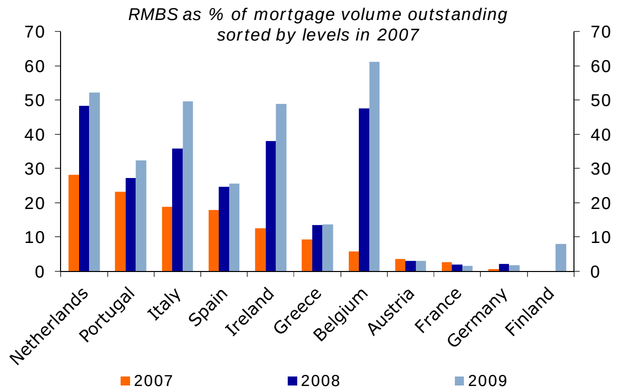
*The proposed (stricter) supervisory rules of the Basel Committee (Basel-III) may possibly have a considerable impact on the Dutch mortgage market. In addition to the requirement for larger and better quality buffer capital, more stringent requirements are being proposed for bank liquidity. Mortgage-backed securities are treated unfavourably in the proposals, while the Dutch mortgage market is highly dependent on these instruments.*

**Residential mortgage-backed securities and covered bonds**

Traditionally banks raise money in the form of savings deposits and use these finds to issue credit, such as mortgages (direct bank financing). In recent decades, with the growing demand for credit, banks have increasingly been making use of residential residential mortgage-backed securities (RMBS) and covered bonds (CB), in order to raise the necessary funds (indirect bank financing). Covered bonds are in fact earmarked bonds. The bank issues a bond which entitles the bondholder, if the bank should default on payment, to be compensated from the income derived from or sale of a specifically indicated package of mortgages. RMBS are very similar to these, except that the yield for the bondholder is directly linked to income from a specific package of mortgages, and the bank is strictly speaking no longer involved.

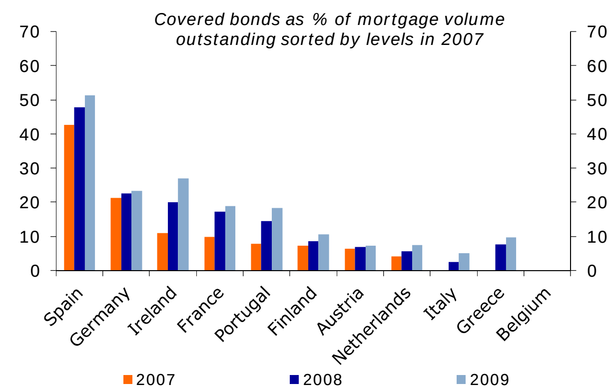
From an international perspective, financing of Dutch mortgages is highly dependent on the market for residential mortgage-backed securities (figure 24) and only to a minor extent on covered bonds (figure 25). Until the crisis, securitisation offered some relief in the tight Dutch savings deposits market, where many deposits are invested in financial instruments via pension and insurance funds, including RMBS, instead of in bank deposit accounts where they would be available for direct bank financing.

**Figure 24: The Dutch rely on securitisation…**




Source: European Securitisation Forum (ESF), ECB

**Figure 25: … and scarely on covered bonds**




Source: European Securitisation Forum (ESF), ECB

**New supervision rules from the Basel Committee**

Besides the requirement for a larger and better quality capital buffer, the Basel Committee has proposed more stringent requirements for bank liquidity. Thus RMBS will no longer be included in the liquid buffers, whereas covered bonds will continue to be included – or at least partly. Only central bank deposits and government bonds will continue to belong fully to the liquid buffers. The implication is that RMBS are becoming less attractive to the banks to purchase and to keep as reserve. Thus it will probably become a challenge to issue RMBS in sufficient volume and at acceptable rates. Prior to the crisis, banks were significant purchasers in the market. Now, however, it will become more difficult to sustain mortgage financing in RMBS-dependent markets such as the Netherlands, which will most likely result in higher mortgage interest rates.

**Impact analysis based on experiences during the crisis**

The experiences gained during the financial crisis have afforded insight into the possible impact of the tighter liquidity requirements on the Dutch mortgage market. The crisis hit the RMBS markets much harder than the markets for covered bonds, both in terms of the premiums demanded by investors to retain the RMBS and in terms of the markets being open to any new issuance of mortgage-backed bonds at all.

Prior to the crisis, investors demanded only a few extra basis points (bp) above the EURIBOR yield for RMBS (5yr) based on the highest quality packages of Dutch mortgages. In late 2008 this had risen to a peak of 400 bp in secondary markets (for comparable British RMBS, the rate was 500 bp); in late 2010 the premiums were still above 120 bp. By contrast, covered bonds experienced a much less steep rise in premiums, and in the case of German CBs, prices have almost fully recovered since.

Throughout 2008 and 2009 the RMBS market was effectively closed for new issues. Securitisation programmes were still carried out, and in many countries even to a greater extent than before the crisis. However, the RMBS launched in 2008 and 2009 were scarcely used for the purposed of financing mortgage portfolios. Instead, banks have been using large-scale RMBS issuance as potential collateral for the ECB in exchange for (emergency) liquidity. Not until the first half of 2010 did we see the securitisation market opening up cautiously again and contributing to the funding of mortgage markets. For covered bonds this had already happened in early 2009.

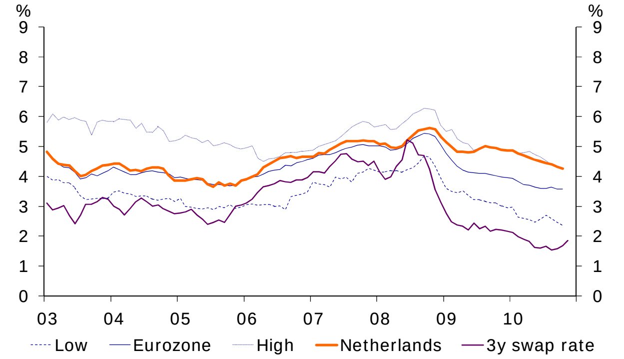
**The Netherlands saw higher mortgage rates due to closed RMBS market**
Figures 26 and 27 compare European mortgage rates on the basis of two fixed-interest periods. Each graph shows the average European interest rate (solid blue line) and the interest rate of the country with the lowest (dashed blue line), and the highest (dotted blue line) mortgage rate. The Dutch rate is shown by the orange line in each case.

The graph shows that European mortgage rates rise vis a vis the relevant swap rate (solid purple line). This reflects the general re-pricing of risk in financial markets, causing financing costs for all European mortgage markets to currently exceed the pre-crisis level. Liquidity now has a price again.

We can also see that Dutch mortgage rates –which until the crisis were reasonably in line with the European average– rapidly rose to among the highest in the eurozone from late 2008/early 2009 (depending on the maturity under consideration). Thus the crisis appears to have hit the Dutch mortgage market differently from most other eurozone countries; the reason appears to be the relatively high dependency of the Dutch market on RMBS.

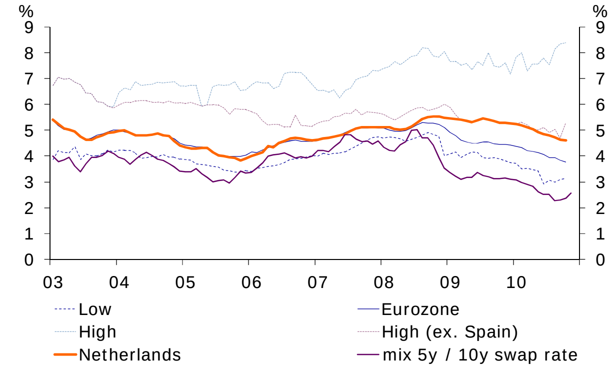
**Unequal international impact of difficult RMBS market**
Further light can be shed on the effect on mortgage rates of dependency on RMBS or covered bonds in national mortgage markets, by comparing the pre-crisis dependency with post-crisis mortgage rates. For the eurozone countries, figure 28 shows the association between RMBS dependency in 2007 and the average mortgage rate in 2009-2010. The various fixed interest periods are identified by different markers with the Dutch marker always the extra large one. For each fixed interest period, moreover, a trend line shows the linear

**Figure 26: Mortgage rates, 1-5 yr fixed interest**




Source: European Central Bank (ECB)

**Figure 27: Mortgage rates, 5-10 yr fixed interest**




Source: European Central Bank (ECB)

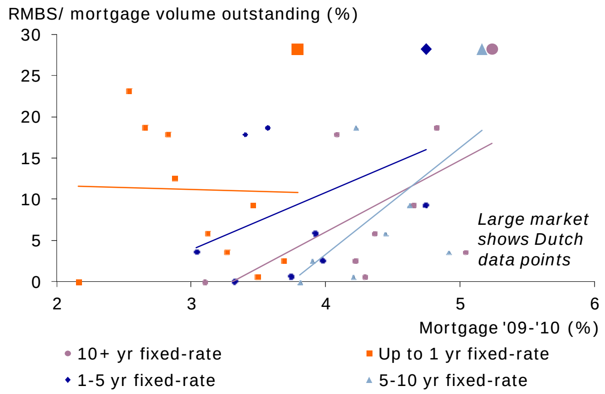
association between pre-crisis RMBS dependency and post-crisis average mortgage rates. In similar vein, figure 29 shows the correlation between outstanding covered bonds and the mortgage rate in 2009-2010.

It is telling that –apart from mortgages with a fixed interest rate of up to one year– there is clearly a positive correlation between pre-crisis RMBS dependency and higher mortgage rates during the years when the market was ‘closed’ in the wake of the crisis. This is visible in the rising trend lines that have been added to the graph for fixed interest periods: the greater the dependency on RMBS for funding before the crisis, the higher the mortgage rates has been on average since the crisis. Even more telling is the fact that there is clearly a negative correlation between pre-crisis dependency on covered bonds and average mortgage rates in the crisis years, which the covered bond markets absorbed much better. Thus the effect of the crisis on eurozone mortgage markets was very unequal. The greater the RMBS dependency, the more severe the effect.

**Conclusion**

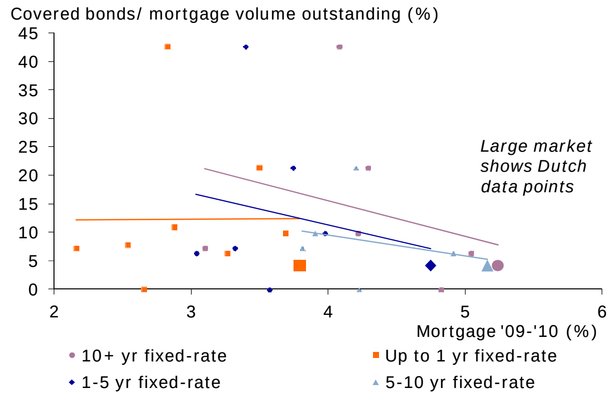
As an RMBS dependent country, the Netherlands was hard hit by the closing down of the RMBS market during the credit crisis. The relatively unfavourable treatment of RMBS in the most recent Basel proposals will likewise weigh heavily on the Dutch mortgage market – probably resulting in higher mortgage rates than in other eurozone markets. Substitution with covered bonds is a possible alternative, but the necessary adjustment would require time.

**Figure 28: ‘RMBS markets’ since the crisis…**




Source: ECB, ECBC, ESF, Rabobank

**Figure 29: …more expensive than ‘CB markets’**




Source: ECB, ECBC, ESF, Rabobank

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## House building programme under pressure?

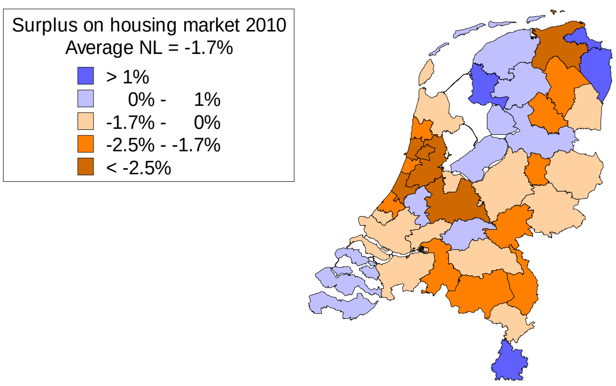
The (house) building sector in the Netherlands has had a tough two years. Uncertainty among potential buyers and tenants has pushed down demand for houses, resulting in a decline in construction output – most markedly so in 2010. As has been stated earlier in this report, a strong recovery in the sector is unlikely in the coming years. Because of regional imbalances, the effect of the lower output is felt differently in the various housing market regions in the country. Particularly in regions where there is a housing shortage, this shortage is highly likely to continue.

### Tightness on the housing market, price and price development

The regional match between supply and demand showed clear imbalances in 2010. In the northern wing of the Randstad urban belt and in most university towns, the housing market is much tighter than in peripheral regions. Demand for housing exceeds supply (quantitative shortage, see figure 30). Furthermore, a certain percentage of the houses do not match demand in terms of description, such as house type or size (qualitative shortage). This second aspect is not limited to the tighter regions. Because of the mismatch between supply and demand, house prices in the shortage regions are considerably higher than in the regions with more ample supply. The median house price recorded by the NVM for the period 2003 to 2010 show that eight of the ten most expensive regions have a housing shortage, whereas eight of the ten cheapest regions have an oversupply of houses.

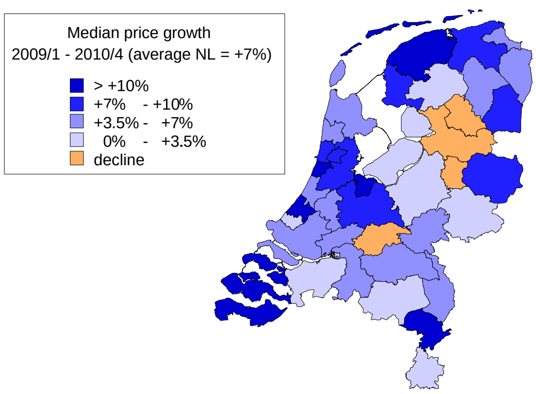
Prices have recovered more strongly in the tightest regions of the Randstad urban belt in the last two years compared to the national average (figure 31). Nonetheless, we see that even a number of regions with ample supply experienced a clear recovery. In view of the relatively large supply in these regions, it appears that housebuyers target the higher quality (and more expensive) segment of the market. Housebuyers' options are largely determined by affordability. And affordability is determined by the house price and the financial scope

**Figure 30: Regional housing surplus 2010**




Source: ABF, processing: Rabobank

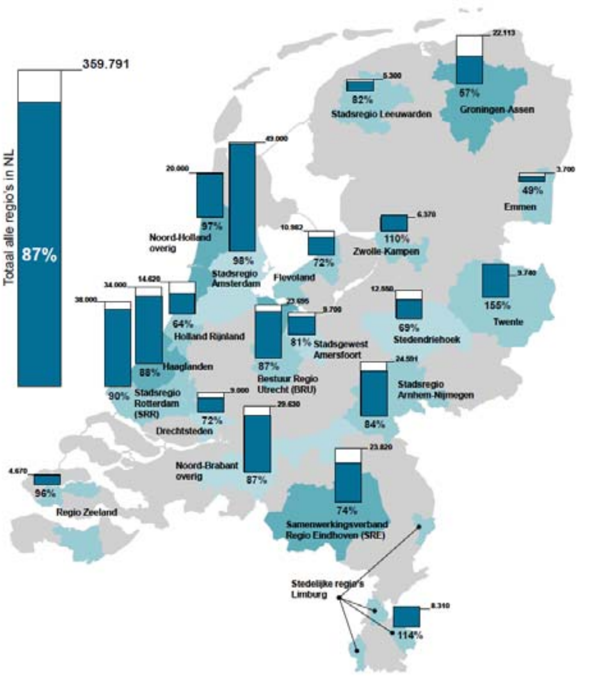
**Figure 31: Regional house prices since early 2009**




Source: NVM, processing: Rabobank

of the household in question. Earlier quarterly reports clearly showed that houses in the most expensive regions are relatively less affordable.
The regional pattern remains consistent. The least affordable regions in 2010 (including the agglomeration of Haarlem, Gooi en Vechtstreek, Amsterdam and Utrecht) were also the least affordable in 2003. Nonetheless, where there is a will there is a way. Research shows that most of those seeking to purchase a house in the tighter markets are ultimately successful. In some cases, they have to compromise on price or on the wishes they may have had at the outset.[5]

**Figure 32: New completions 2005-2009**




Source: Ministry for Housing and Environment

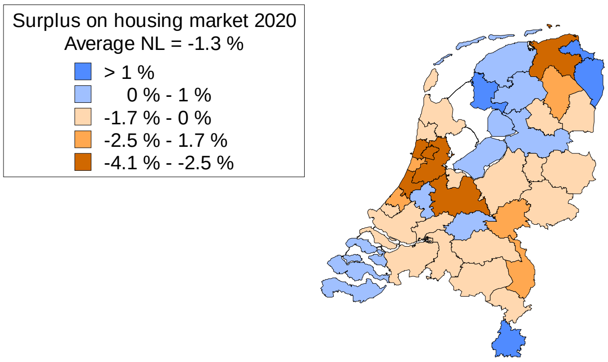
### Aspirations versus reality

In order to address these imbalances, housebuilding agreements were made between the national government and regional authorities for the period 2000-2010, with a view to reducing regional shortages. An overview of the projects completed (figure 32) shows that this was by no means achieved everywhere. This is not a new phenomenon. In 2006, the Environmental Planning Office concluded that sufficient new housing completions were hampered in the period 1995 to 2004 by the economic sensitivity of demand for housing as well as delays in environmental projects.[6] These two arguments still apply. On the one hand factors associated with environmental projects restrict the opportunities for construction. This is particularly true for urban areas. On the other hand, a (temporary) drop in demand for more expensive houses (as in 2002-2003) can negatively impact on the financial viability of house building projects. Therefore, despite the fact that national policy is aimed at reducing the shortage, demand for homes in popular regions continues to exceed the supply. For the period 2005-2009 the national aim was to construct more than 400,000 homes. Ultimately, the number completed was 360,000 (peaking at a total of 83,000 new completions in 2009) – falling well short of the target.

[5] See NRC – 'Het Nederlandse woningtekort? Dat stelt weinig voor' – 2010, Brounen & Neuteboom – Starters in de knel – of Business As Usual – 2009.
[6] See RPB (2006), Woningproductie ten tijde van VINEX.
[7]For example, (regional) shortage of space, societal objections to further urbanization, and (stricter) regulations on living environment quality. See also Rijksoverheid.nl – Verstedelijkingsopgaven 2010-2020.

At regional level, Groningen-Assen, Holland-Rijnland and the Stedendriehoek (urban triangle) were furthest from the target production level. A number of development areas (Twente, Zwolle/Kampen and the urban regions in the province of Limburg) were well within target, and the regions of Greater Amsterdam, rest of Noord-Holland and Zeeland were also on track In view of the results from the period 2005-2009, the upshot is that in regions that were already under pressure for housing, such as Leiden and Utrecht[8], no market expansion took place. The Netherlands also has a number of regions with a plentiful supply of houses (see figure 33) that face a very different task, here the emphasis has shifted from new construction to restructuring and improving the quality of the housing stock. The region of Parkstad is a frontrunner in this respect: the plan is to restructure part of the housing stock within the next ten years, which will actually lead to a reduction of the housing supply on balance[9].

**Figure 33: Regional housing surplus 2020**




Source: ABF, processing: Rabobank

### Development plan 2010-2020

Even now that the bulk of the building in so-called VINEX locations has been completed, development continues in the Netherlands. In the urban regions at least, the number of households will continue to rise in the coming decades, and the housing supply is not yet at the ideal level. Although the Primos forecast projects a decline in the total housing shortage in the Netherlands in 2020 to under 1.5%, little expansion is envisaged for the regions with the greatest shortage (see figure 33). Figure 33 is based on completed housing projections of some 725,000 homes between 2010 and 2020. A number of factors raise question marks over the viability of this building target:

- In the previous policy period, house building agreements were concluded between the national government and regions to be developed. However, the targets were not reached in every case. The current agreements on development are based on intent and the guarantees of completion are soft. This decision was informed by the consequences of the crisis on the housing market. Currently, the government simulation measures for the sector are coming to an end.

[8] Rijksoverheid.nl – Verstedelijkingsopgaven 2010-2020
[9] Rijksoverheid.nl – Verstedelijkingsafspraken bestuurlijk overleg MIRT najaar 2009

- In the coming years we will see increased emphasis on inner city development[10]. Experience has shown that these tend to be complex projects in which profit margins are much lower for builders and developers, particularly in brownfield sites.
- It would appear that most of the relatively accessible and cost-effective locations for large-scale building have already been used[11]. Of course Almere has plenty of room for the required upscaling (+60.00 houses). However, without improved access to the rest of the country, this is not considered viable. Another reason is that house seekers in the Randstad urban belt can already find alternatives in Rijnenburg (Utrecht), Bloemendalerpolder (Weesp), Valkenburg aerodrome (Katwijk/Wassenaar) and Braassemerland (Roelofarendsveen).
- Crises tend to lead to a change in the demand for both rental and non-rental housing. After the 'crisis' of 2002-2003 there was a drop in the demand for more expensive houses. A similar effect was seen in 2009 and 2010, with an increase in the supply of non-rental houses as a result. According to house comparison website 'Huizenzoeker', there were over 178,000 houses for sale in January 2011, 34% more than in January 2009. The picture varies from one province to another (table 1, next page).
- According to the NVM, the removal of this 'bulge' in the housing market will have consequences for how the market works in the coming years. There are sizeable regional differences. The number of houses for sale as a percentage of total housing stock in January 2011 was highest in the provinces of Drenthe and Flevoland (table 2, next page). The provinces of Limburg and Zeeland are at the lower end of the scale in this respect.
- In the light of the changed circumstances, regional house development programmes are now being made more flexible; projects are being reviewed and may consequently be prioritised, or in some cases discontinued. This can help to stem the growth of the number of houses coming onto the market. Partly as a consequence of this policy total new housing output for 2010 was only marginally higher than the ten-year low of 2003. In view of the low number of building permits issued (see figure 14 on page 12), a recovery in new completion is not expected any time soon.

[10] See also 'Het eind van een vijftigjarig feestje' (column NVM-site), EIB - Succesvol binnenstedelijk bouwen, 2010
[11] Rijksoverheid.nl – Verstedelijkingsopgaven 2010-2020

**Conclusion**

The Dutch housing market exhibits clear regional imbalances: a number of relatively tight regions in the northern wing of the Randstad urban belt as opposed to regions with ample supply in the north and south of the country. Despite the policy steered by the central government, the number of new housing completions in the period 1995-2009 only partly achieved a degree of relief in the markets under the most pressure. A lot remains to be done in the next ten year period to achieve the task of enabling households to find a home in their desired location.

In the current scenario the central government has set a target of around 725,000 new completions in period 2010-2020. In view of the current situation on the housing market and the expectations for the near future, this attainability of target appears questionable. Falling short of the target is likely to lead to continued tightness on the housing market, particularly in the northern wing of the Randstad urban belt. The need to expand the housing supply is less urgent in a number of (shrinking) regions, where supply is currently ample. In these areas, the task is to prevent oversupply and to retain the existing stock and make it more attractive. Neither of these goals will be easy to achieve, and will require a joint approach, with mutual agreement on setting priorities being of the utmost importance.

**Table 1: Growth of houses for sale January 2009 - January 2011**

| | | | |
|---|---|---|---|
| Noord-Brabant | 45% | Flevoland | 28% |
| Noord-Holland | 42% | Friesland | 28% |
| Utrecht | 42% | Drenthe | 25% |
| Limburg | 40% | Zuid-Holland | 23% |
| Gelderland | 37% | Groningen | 19% |
| Zeeland | 34% | The Netherlands | 34% |
| Overijssel | 33% | | |

Source: Huizenzoeker.nl

**Table 2: Houses for sale as % of total non-rental stock 2010**

| | | | |
|---|---|---|---|
| Drenthe | 5.2% | Noord-Brabant | 4.1% |
| Flevoland | 5.1% | Overijssel | 4.0% |
| Gelderland | 4.9% | Utrecht | 3.8% |
| Groningen | 4.7% | Zeeland | 3.8% |
| Friesland | 4.6% | Limburg | 3.1% |
| Noord-Holland | 4.3% | The Netherlands | 4.3% |
| Zuid-Holland | 4.3% | | |

Source: ABF, Huizenzoeker.nl

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# Key figures

**House Prices**

| Year-on-year change (%) | 2008 | 2009 | 2010 [a] | 2011 [a] |
|---|---|---|---|---|
| NVM (median house price) | -0.3 | -7.1 | 3.0 | -2½ |
| Land Registry (purchase price) | 2.7 | -6.4 | 0.4 | -2½ |
| Statistics Netherlands/ Land Registry (PBK) | 3.0 | -3.3 | -2.0 | -2 |
| ABF Valuation (WOX) | 2.5 | -3.2 | -0.3 | -1 |

**Totals**

| x 1000 | 2008 | 2009 | 2010 [a] | 2011 [a] |
|---|---|---|---|---|
| Sales transactions | 182 | 128 | 126 | 130 |
| Newly built homes | 79 | 83 | 55[a] | 55[a] |

**Totals**

| | 2008 | 2009 | 2010 [a] | 2011 [a] |
|---|---|---|---|---|
| Enforced Sales | 1,961 | 2,256 | 2,086 | - |

**Key economic figures (November 2010)**

| | 2008 | 2009 | 2010 [a] | 2011 [a] |
|---|---|---|---|---|
| GDP (growth, %) | 1.9 | -3.9 | 1¾ [a] | 1½ [a] |
| Inflation (%) | 2.5 | 1.2 | 1.3 [a] | 1¼ [a] |
| Unemployment (%) | 3.8 | 4.8 | 5.5 [a] | 5¼ [a] |

**Rabobank affordability index**

| x 1000 | 2008 | 2009 | 2010 [a] | 2011 [a] |
|---|---|---|---|---|
| Affordability index [b] | 85 | 98 | 106 | 106 |

**Interest rates [c]**

| Level (%) | February 2010 | +3m [d] | +12m [d] |
|---|---|---|---|
| 3-month Eurozone | 1.09 | 1.19 | 1.84 |
| 10-year Euroswap | 3.53 | 3.45 | 3.65 |
| Mortgage interest rate, 5-10 year fixed | 4.57[e] | | |

[a] Rabobank outlook
[b] The Rabobank affordability index is calculated based on the average property price (Land Registry) and average household income (Statistics Netherlands). An annuity mortgage is used with a duration of 30 years and a forced sale value of 80 percent of the market value, and a monthly expense quota of 30 percent. An affordability index greater than 100 indicates that the average house is reasonably affordable. An affordability index below 100 indicates that an average property is not reasonably affordable without injecting personal capital.
[c] Forecasts by Financial Markets Research, Rabobank International
[d] Outlook for +3 and +12 months respectively
[e] September 2010 monthly average, DNB

## Colophon

The Dutch Housing Market Quarterly is a publication of the Economic Research Department (ERD) of Rabobank Nederland. The view presented in this publication has been based on data from sources we consider to be reliable. Among others, these include Reuters EcoWin, Land Registry, NVM, DNB, CPB and Statistics Netherlands.



The Economic Research Department is also on the internet: www.rabobank.com/kennisbank

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