Rabobank

Dutch Housing Market Quarterly

May 2009

Economic Research Department

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Introduction and summary

The Dutch housing market is currently under pressure. The credit crisis has taken its toll on consumer confidence, resulting in fewer transactions taking place. The first quarter of 2009 had the lowest number of house sales in 10 years. There is a clear division between vendors who are under pressure to sell and those who are not. Those not under pressure can afford to wait for a price they find acceptable, whereas vendors who need to sell are forced to drop their price. This further influences the price development of houses. On the buyers' side of the market, two anxieties are central: fear of unemployment (and loss of income) and fear of double housing costs (fixed expenditure). As long as these fears prevail, the number of buyers will remain low, especially as they in turn will have difficulty selling their own house. The current improvement in affordability cannot be seen as a long-term trend. Over time, affordability will again deteriorate, partly due to higher interest rates.
New construction output is currently also down in the wake of the turbulence in both financial markets and the real economy. The Dutch government has responded by presenting a 'green crisis package', designed to stimulate the construction sector as well as encourage energy saving housing. Rabobank has reacted positively to this quality incentive. Furthermore, the measures for the construction sector are well timed. Effects on the housing market will be slight, however, since there will be little relief in the short term for the low number of transactions.
The mortgage market is likewise under pressure, with the number of mortgages issued down. However, net mortgage debt is still rising, although this is offset by considerable net assets. On average, Dutch households show a healthy balance sheet.

Since there is no single Dutch housing market as such, Rabobank has divided the market into 21 regional sections, based on the relocation patterns of the Dutch population. The regions are located around a large or medium-sized city in each case. Often people move house within a region.

In the Netherlands, the rental housing market and the non-rental market are two fairly distinct entities. The part-selling market constitutes an important link between these two. Here too, current market developments are clearly felt. Tenants are more reluctant to purchase a house, which pushes down the turnover rate. However, once the market picks up, there will be good opportunities for part-selling rental accommodation.

In view of the current deterioration in the housing market, the Rabobank envisages a nominal house price drop of 5% for 2009, and a nominal drop of 1% for 2010. Downward risks for sentiment among house buyers and for market dynamism continue to prevail.

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Second hand housing market

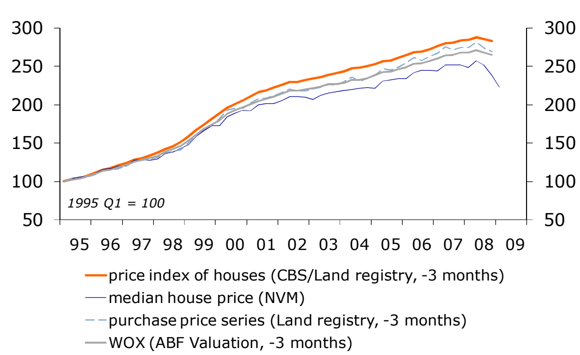
Further decline in house prices

During the first quarter of 2009, house prices continued the downward trend seen in the last quarter of 2008 (Figure 1). The NVM (Netherlands Association of Real Estate Brokers) published a median house price for the first quarter of € 218,000, which represents a drop of € 15,000 in one quarter. A certain price drop compared to the previous quarter was not unexpected, since seasonal factors mean the first quarter of the year is always the least favourable for house price development. However, the reported price decline was greater than anticipated. Prices were reported to have fallen by twice as much as we had envisaged in our last Housing Market Quarterly (February 2009).

This can largely be explained by the so-called composition effect. In order to understand how this works, it is important to emphasise that the measurement of house prices is based on transactions. The current market situation is characterised by two key factors: there are fewer transactions than in recent years (Figure 2), and in the more expensive price bracket the drop is more pronounced than in the other segments. The median house price reported by the NVM has been chiefly affected by this second aspect. With a shift in the transaction distribution, as is currently the case where the dearer segment has lost ground, the median price shifts accordingly – in this case downward. A similar composition effect is reflected in the house price figures published by the Dutch Land Registry.

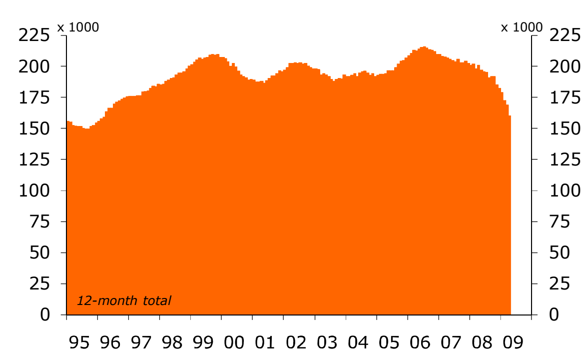
Significantly, a sharp division is currently developing on the vendor side of the market between vendors who are under pressure to sell and those who are not. House sellers who are not under pressure to sell can afford to hold off for an acceptable price, or even withdraw their house from the market. Despite the prevailing lower prices, there is little scope for negotiation with this group. The opposite is the case among vendors who are under pressure to sell, whether

Figure 1: Declining house price indices NL



Source: ABF Valuation, Land Registry, NVM, Statistics Netherlands, Rabobank

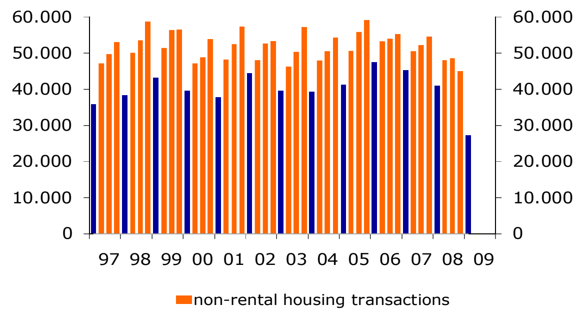
Figure 2: Further drop in number of transactions



Source: Land Registry, Rabobank

for personal relationship reasons, a growing family, double housing costs, or having to relocate to a different region for a job. These vendors are more likely to make concessions in the negotiation process. Accordingly, in the current market, they will probably sell their house quicker than vendors who are not under pressure, but at a lower price. These developments result in fewer transactions and lower house prices. This is not surprising, since we know that the registration of price developments is based on the transactions that do take place. Clearly then, this process will have a negative impact on the recorded price development.

Figure 3: Historically low number of transactions Q1 2009



Source: Land Registry, Rabobank

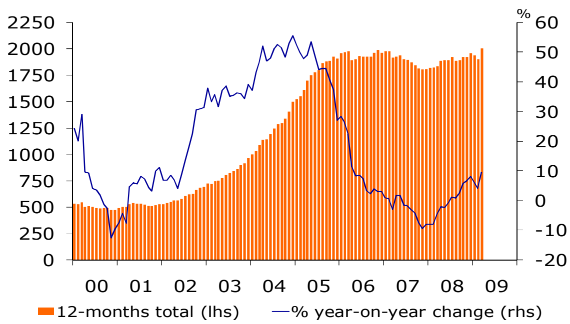
Fewer transactions: buyers determine the market

During the first quarter of 2009, the Dutch Land Registry recorded a total of 27,218 house transactions. This represents a drop of 33.6% compared to the same period last year. Furthermore, it is the lowest number of transactions in the past ten years (Figure 3). This development did not come as a surprise, since it is customary for the lowest number of transactions to take place in the first quarter, in keeping with the seasonal pattern. Furthermore, we could already tell from the fourth quarter of 2008 that transaction numbers were currently under pressure. The salient feature of the current market situation is a lack of confidence among potential house-buyers. Two main fears are central to this. The first is a fear of becoming unemployed and losing income. In general, the expectations in this regard are not very positive. Currently some 4% of the Dutch workforce is unemployed. By the end of this year, this figure will have climbed to over 6%, and by late 2010 we expect the jobless figure to have reached almost 9%.

Despite these gloomy predictions, it must be said that the vast majority of Dutch employees will not lose their jobs. Admittedly, however, the personal lifestyle consequences will be considerable for those who do lose their jobs and are unable to generate additional income in the short term. Uncertainty about employment leads potential house-buyers to adopt a cautious attitude.
The second fear affecting house-seekers is related to the possible double housing costs. Specifically, people are anxious about having to pay high fixed costs. Houses are on the market for longer, which means that those moving along the property ladder incur a higher risk of owning two houses for a lengthy period and having to pay double costs. Just a few years ago the conventional wisdom was to buy first and then sell. Now, however, Dutch households have become much more cautious and hesitant. In 2006, at the top of the market it was quite normal to buy a second house before selling the first one.

Although no changes have occurred in the system, house-buyers now often opt for the reverse procedure. Accordingly, the demand for a new house only takes place after the existing house has been sold. This makes sense for the individual, but is disastrous for the market in general. After all, if everyone waits to buy a house until their old house has been sold, there will be no buyers and the system will stagnate.

Figure 4: Forced sales stable for now



Source: Land Registry, Rabobank

Forces sales follow with a lag

The Land Registry also records the number of forced auctions. These totalled 539 in the first quarter of 2009, which is 10% more than in the same period last year (+ 49 transactions). Thus the 12-month total amounts to 2,010, which differs little from preceding years (Figure 4). If we compare the total number of forced sales to the total number of house transactions, then the ratio rises to 1.19%. Although this is somewhat higher than the ca. 1% of recent years, this increase can be largely explained by the current lower number of transactions.

It is important to realise that forced sales occur relatively infrequently. They take place as a last resort and only when there is no prospect of improvement in the financial situation of the home owner. Usually personal difficulties are behind this, such as a broken relationship or job loss. Since we expect unemployment to rise further this year and next year, the Rabobank envisages a rise in the number of forced sales. Nonetheless, the extent of this should not be exaggerated. Not everyone who loses their job owns a mortgaged house. And older workers in particular who have a long history with one employer and a relatively high income are less at risk, especially when the mortgage sum and the monthly repayments are relatively low. For this group, a drop in income will not lead directly to unmanageable mortgage costs. Besides, unemployment is often only a temporary situation. Jobseekers generally succeed in finding another position within a reasonable period. Accordingly, payment difficulties may be only of a temporary nature.

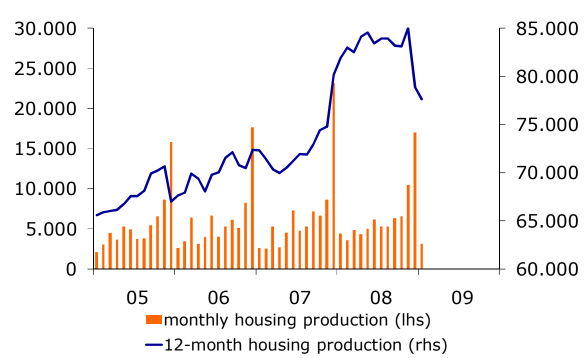
Nonetheless, the Rabobank expects to see an increase in the number of forced auctions. This increase tends to take place about a year after a turnaround in the employment situation. Forced sales may, however, rise sooner than one might expect because some banks may have little scope for payment deferral on account of the credit crisis. Although the consequences of a forced sale may be considerable on an individual level, the Rabobank expects that they will remain limited for the Dutch housing and mortgage market as a whole.

New completions start to slide

After numerous advance reports, a drop in new housing output has actually commenced. Compared to 80,193 new housing completions in 2007, there were only 78,882 completions in 2008. Although the decline is limited to 1.6%, 12-month production had been running at well over 80,000 for the entire year until December. This means the drop in December was particularly acute, when considerably fewer completions were registered compared to December 2007. On the basis of the number of building permits issued, combined with reports from the market about the mothballing of new construction projects, we can conclude that this decline in output is only the beginning of a further slide to some 72,000 completions this year and about 65,000 in 2010. In this respect there are no differences between the rental and non-rental segments of the market (Figure 6). Nor is this surprising, since developers of rental and non-rental houses are dependent on each other for integrated spatial development.

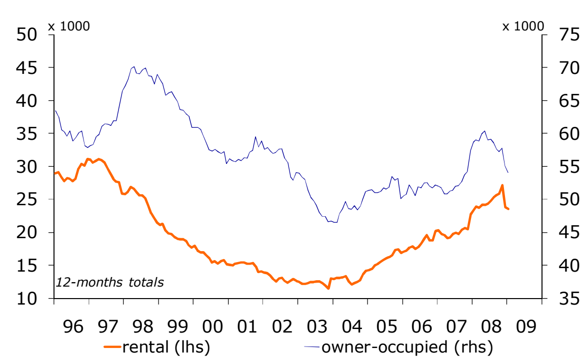
In response to the current market situation, the Dutch government presented a 'green crisis package' in late March, designed to stimulate the construction sector as well as to encourage energy saving improvements to houses. The Rabobank has reacted positively to this investment in sustainability, which can mainly be seen as a substantial contribution to improving the quality of the existing housing supply. This stimulus will help to make homes more attractive, thus possibly reducing the qualitative mismatch on the Dutch housing market. However, there is a downside to these plans too: In the current market situation the number of transactions is under pressure. By investing in existing houses now, householders will be less inclined to want to move house. After all, having endured the hassle of renovation, people will want to benefit for a while from the improved quality of their house. Thus, although this measure is highly desirable and is well-timed for the construction sector, its impact on the market dynamic is less timely. In the short term it will make no positive contribution to the number of transactions.

Figure 5: Slump in building output



Source: Statistics Netherlands, Rabobank

Figure 6: Both rental and non-rental output hit



Source: Statistics Netherlands, Rabobank

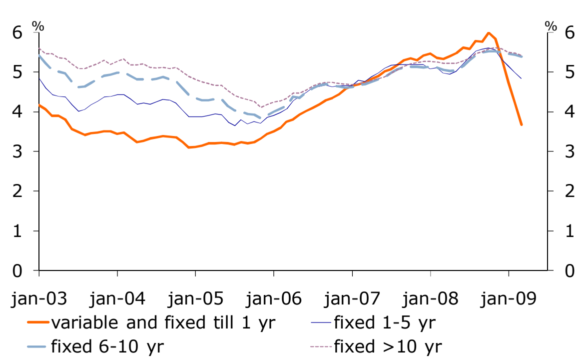
Slight drop in mortgage interest rate

Both the variable mortgage interest rate and fixed interest rates registered a drop in recent months. The shorter the fixed interest term, the greater the drop (Figure 7). However, mortgage rates are lagging behind the decline in the European Central Bank's policy rate and risk-free capital market rates. This is a consequence of the ongoing problems on the financial markets, which are generating higher financing costs for the banks. Although some further reduction could take place in the variable interest rates and short-term rates, any decline in long-term interest rates with fixed periods of over 10 years will be very limited.

Money market rates on a downward slide

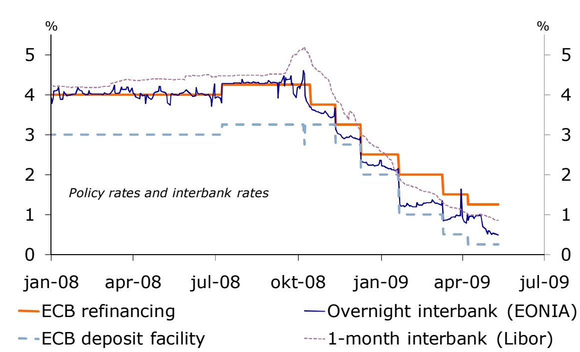
Since October 2008, the European Central Bank (ECB) has cut the refinancing rate by 3.25%-points to 1%. At the same time it has modified the way it supplies liquidity to the banks. Banks with inadequate collateral can now borrow an unlimited amount every week at the refinancing rate. In normal times, the ECB ensures that the interbank daily rate remains in the region of the refinancing rate. However, the more expansive policy has brought the interbank daily rate below the refinancing rate (Figure 8). Yet this very low short-term interbank rate has only a limited effect on the variable mortgage rate. This is mainly because only a small part of the banks' financing consists of money borrowed from the ECB. The main source of their financing consists of savings deposits and money borrowed on the financial markets. Since the crisis has made all kinds of market financing more expensive and less accessible, competition among financial institutions for savings deposits has increased. Hence, the decline in savings rates is lagging behind the decline in the interbank rate. The relatively high funding costs for banks means relatively high mortgage interest rates. We therefore expect that the variable mortgage rate will reach a bottom of some 3% in the coming months, and will remain there for some time.

Figure 7: Mortgage rates down



Source: DNB

Figure 8: Money market rates very low

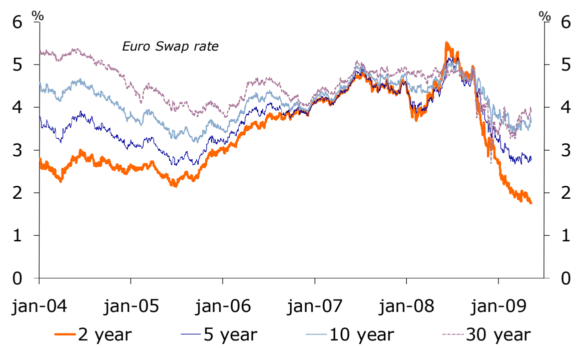


Source: Reuters EcoWin

Capital market rates at a low ebb

After a spectacular nose-dive since September 2008, capital market interest rates stabilised in recent months, or rebounded slightly (Figure 9). The 2-year and 5-year swap rates plummeted quickest, falling below the previous low of 2005. We expect rates to reach a bottom in the coming months. Although the low policy rate combined with poor economic prospects will continue to exert downward pressure during the coming period, the heavy-handed interventions by central banks and governments should increasingly start to bear fruit. The large-scale monetary expansion of central banks may push up inflation expectations, resulting in higher interest rates. Together with large quantities of newly issued government securities, this should result in interest rates being somewhat higher at the end of this year than is currently the case.

Figure 9: Capital market rates at a low ebb



Source: Reuters EcoWin

As is the case with the low policy rate, the decline in longer term market rates is likewise only partly reflected in lower mortgage interest rates. This is because banks have to pay a risk premium if they take out long-term loans on the capital market. The government, by contrast, is seen as risk free, and the swap rates shown in Figure 9 reflect this. Owing to the turbulence on the financial markets, the risk premiums for companies and banks have shot up. The average risk premium for companies with a creditworthiness rating of A to AAA has jumped from under 0.4%-points in the period from January 2004 to August 2007 to over 1.85%-points since 15 September 2008. Because of these high risk premiums as well as the high deposit interest rates mentioned earlier, fixed-term mortgage interest rates have declined much less rapidly than the risk-free capital market interest rates. Looking ahead, we expect that a further drop in fixed period mortgage rates will be very limited, particularly those with longer fixed terms.

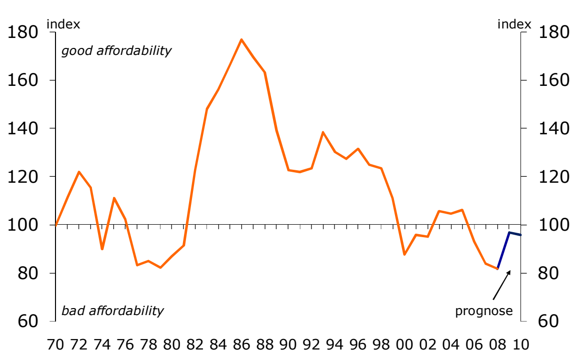
Although we predict that variable mortgage rates will be lower than fixed interest rates for the coming period, this is not in itself sufficient reason to opt for a variable mortgage. In our *2009/08 Report "Mortgage term: variable or fixed interest?"* we explore in more detail the pros and cons of mortgages with a variable rate compared to fixed interest rates.

Temporary improvement 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 a statistical index, and does not take account of changes in income situation, for instance as a result of unemployment. The index makes a distinction between affordability for first-time buyers (110% financing) and those who want to trade up (70% financing). 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.

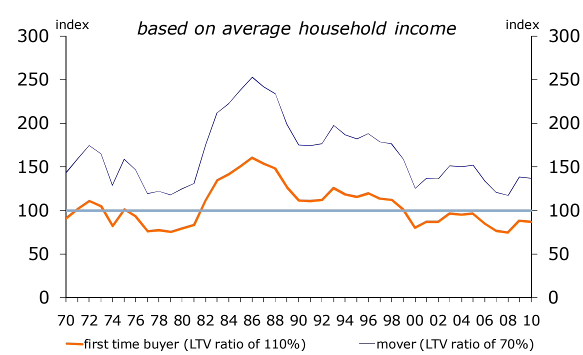
The affordability of purchasing a house in the Netherlands is improving considerably this year (Figure 10). However, this improvement will be temporary. It is chiefly due to lower financing costs. House prices have dropped by several percent and mortgage rates are lower than was the case a few months ago. Interest rates at the short end of the curve have fallen more sharply than those at the long end (see previous paragraph). Income development will also contribute to affordability this year. According to data from Statistics Netherlands (CBS), wages agreed under the collective wage agreement rose on average by 3.7% in the first quarter of 2009 compared to the same period in 2008. This is because the majority of the collective agreements date from before the recession. However, these developments are not permanent in nature. House prices will not continue to drop – the essential mismatch between demand and supply on the Dutch housing market will prevent this. Equally, mortgage rates will rise again. Moreover, more recently agreed wage rises are considerably lower, which means future wage development will be much more restrained. In view of these developments, it would appear that 2009 is the right year for first-time buyers to purchase a house (Figure 11). Not because houses are now so affordable, but because affordability can be expected to deteriorate again next year.

Figure 10: Temporary improvement in affordability



Source: CPB, Land Registry, Reuters EcoWin, Rabobank

Figure 11: Problems far from over for first-time buyers

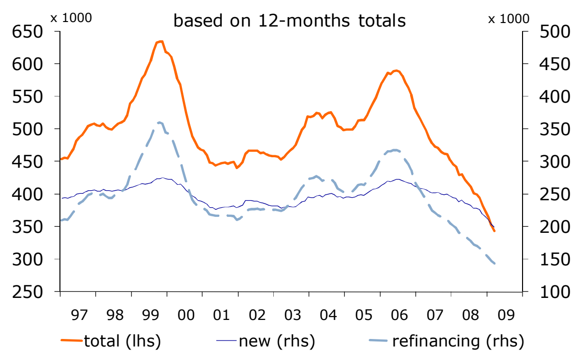


Source: CPB, Land Registry, Reuters EcoWin, Rabobank

Extension of mortgages drops further

Continuing the trend of recent years, the number of mortgages issued during the past few months is showing a further drop (Figure 12). According to the Dutch Land Registry, in the first quarter of 2009 a total of 55,841 mortgages were issued – 35.2% less than in the same period last year. Besides, a distinct change has taken place compared to previous years. Until recently, the decline in mortgage approvals was mainly due to fewer re-financing mortgages, whereas now the number of newly issued mortgages is declining more rapidly than before. This development is running parallel to an overall drop in transactions on the housing market. Another significant break with trend is the fact that the average mortgage amount (-35.1%) is currently sliding as rapidly as the number of mortgages. The main reasons for this accelerated decline are lower house prices and the greater than average drop in transactions in the more expensive market segment.

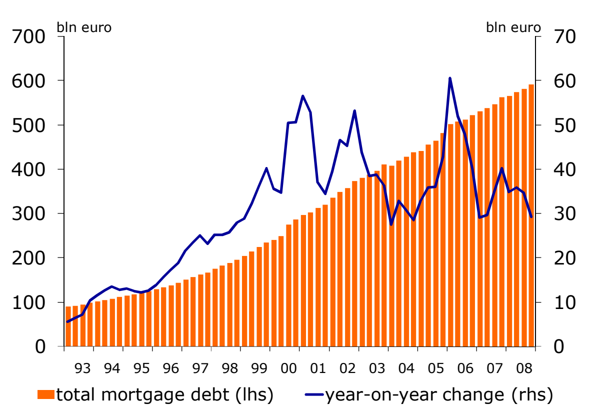
Figure 12: Fewer mortgages issued again



Source: Land Registry, Rabobank

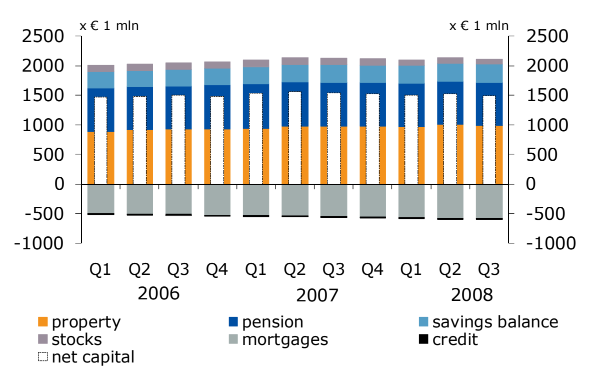
Despite this drop, net mortgage debt rose further to € 592 bn at the end of 2008 (Figure 13). In terms of size, this is virtually equal to Dutch GDP. Although the Dutch tax system has the effect of driving up the gross national mortgage debt ratios, these are very different from mortgage debt ratios in other countries. Dutch householders tend to redeem relatively little of their mortgage, but prefer to have savings instead. Moreover, they borrow very little for consumer spending. On average, Dutch households run a very healthy balance sheet (Figure 14). However, first time buyers with 100% mortgages (no excess value) can be seen as a risk group. This risk increases in the case of interest-only mortgages and limited assets.

Figure 13: Net mortgage debt still rising



Source: DNB, Rabobank

Figure 14: Sound average balance sheet

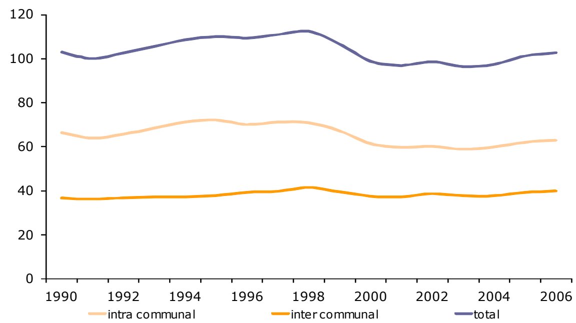


Source: DNB, NVM, Statistics Netherlands, VROM, Rabobank

Regional Housing Markets

People tend to speak of the Dutch housing market, as if it were a homogeneous entity. However, regional differences are considerable, both in terms of demand and supply as well as in government policy[1]. Are there also regional differences in the origin and destination of those who move house? In other words, can we define a number of separate regional housing markets in the Netherlands?

Figure 15: Internal relocations per 1,000 inhabitants in the Netherlands



Source: ABF-Research

Regional differences, regional markets?

There are sharp regional differences in the Netherlands both in demand for houses and in housing supply. In addition, Dutch government policy on house building locations makes distinctions between regions. However, these regional differences in demand, supply and planning policy would not in themselves be enough to speak of regional housing markets. After all, demand for housing in one region may come from the whole country, and likewise the housing supply in a particular region may exert a gravity pull for the entire country. In that case, the Netherlands would constitute a single housing market.

We can only speak of a regional housing market if the bulk of demand and supply takes place within a clearly defined part of the country. We can determine whether there is a spatial clustering of supply and demand on the housing market by looking at the spatial relocation patterns in the country, i.e. internal migration. Do the Dutch zigzag through the country, or do they tend to move house within clearly defined areas?

Moving house close to home…

An analysis of the geographical relocation patterns in the Netherlands shows that the distance between the place of origin and the place of relocation is crucial. The further apart these two places are, the less movement takes place between them. Most relocations occur within a small radius. In over 60% of cases, people move within the same municipality (Figure 15). This orientation towards the surrounding areas is long-term in nature. The number of within-municipality relocations as a percentage of the total number of removals has remained virtually unchanged throughout the years.

[1] See the Dutch Housing Market Quarterlies of May 2008, August 2008 and February 2009

... with cities as centre of gravity

In addition, the larger the city, the greater the number of relocations to and from it. Cities are the centres of gravity for internal migration. They account for a large share of removals, not only in absolute numbers, but also relative to their population. Urban municipalities represent 46% of the Dutch population, but they account for 55% of internal migration.

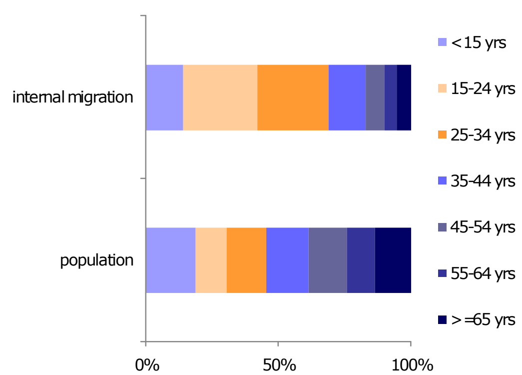
The dominant position occupied by cities in relation to relocations can be attributed to the importance of cities in removal patterns of the most mobile age brackets (15 to 35). While the average relocation rate for the general population is 10% annually, the rate is 20% for young adults. Although this group only makes up 27% of the Dutch population, it accounts for 55% of domestic migration (Figure 16).First-time buyers in this group therefore play a very important part in the Dutch housing market.

Regional centres ...

On account of the low average relocation distance and the dominance of cities in the number of relocations, we can distinguish a number of distinct regional housing markets that are oriented towards urban centres. The centres of these regional housing markets can be determined on the basis of their share of the total number of relocations in the country.

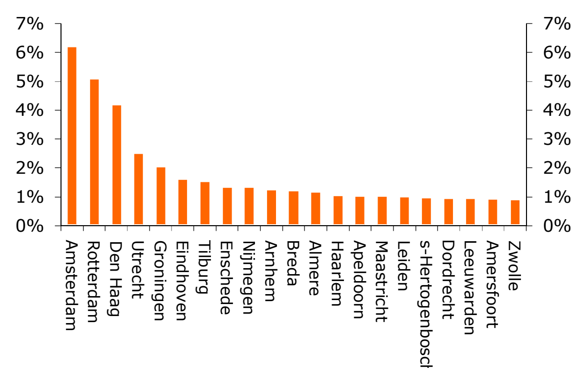
Amsterdam occupies by far the largest share (6.2%), followed by Rotterdam and The Hague. These are followed by Utrecht (2.5%), Groningen, Eindhoven, Tilburg and Enschede which are the largest of the medium sized cities and differ little in terms of share of relocations (Figure 17). The other municipalities can be allocated to one of these centres, on the basis of the destination of the residents who leave the municipality.

Figure 16: Population age profile and internal migration 2002-2006



Source: ABF-Research

Figure 17: Share of municipalities in relocations 1997-2006



Source: ABF-Research

... for regional housing markets

The size of the regional housing markets depends on the number of centres involved; this applies also to the internal cohesion within the regional housing market. The greater the proportion of relocations in a centre, the fewer centres that are defined, and the bigger the regional housing markets. These large regions are furthermore characterised by a considerable degree of internal cohesion. The share of relocations within the region in the total number of relocations from or to this region is large (table 1).

If 5 regional housing markets are defined, in the case of Amsterdam, Rotterdam, The Hague, Utrecht and Groningen, an average of 59% of relocations between municipalities takes place within the same region. For 38 regions, 39% of relocations within municipalities take place within the same region. Taking the within-municipality removals into account, a large number of housing market regions are self-contained. Even regarding all 443 municipalities as regional centres, the share of within-regional (within-municipal) relocations still amounts to 62%.

21 regional housing markets

If the definition of regional housing markets means that at least half of relocations between municipalities take place within a region, then 21 regions are defined. The centres of these regions, in order of share in Dutch relocations are: Amsterdam, Rotterdam, The Hague, Utrecht, Groningen, Eindhoven, Tilburg, Enschede, Nijmegen, Arnhem, Breda, Almere, Haarlem, Apeldoorn, Maastricht, Leiden, 's –Hertogenbosch, Dordrecht, Leeuwarden, Amersfoort and Zwolle (map 1). Including the within-municipality removals, on average 81% of all relocations take place within the region itself in these regional housing markets (table 1).

Table 1: Definition of housing markets

share centre in internal migration	number of regions	average % of migration within region: intercommunal	average % of migration within region: inter- and intracommunal
2,00%	5	59%	84%
1,00%	14	52%	82%
0,85%	21	49%	81%
0,70%	26	45%	79%
0,50%	38	39%	77%
0,00%	443	0%	62%

Source: ABF-Research

Table 2: Incoming and outgoing relocations as a share of the total population (=1)

small - incoming migratie - large	small - outgoing migratie - large	
large	***destination*** Amsterdam Rotterdam	***pigeonhouse*** Arnhem, Leiden Den Haag, Maastricht Eindhoven, Nijmegen Groningen, Utrecht Haarlem, Zwolle
small	***reservation*** Apeldoorn, Enschede Dordrecht, Tilburg	***nursery*** Almere, Haarlemmermeer Amersfoort, s-Hertogenbosch Breda

Source: ABF-Research

These regional housing markets differ both in size and in internal cohesion. The regional orbiting around Maastricht is the most cohesive (87% of relocations take place within the region), and the region around Almere is the least cohesive in this respect (62%). The largest regions, both in surface area and inhabitants, as well as in number of relocations are those around the cities of Amsterdam, with 205,000 house moves annually, Rotterdam (183,000) and Groningen (101,000).

In the majority of cases the centre is more or less in the middle of a compact or clearly defined region. Interesting exceptions are the towns of Urk, Harderwijk, Venlo, Hulst and a number of municipalities in the Green Heart of the country, that don't gravitate around a nearby housing market, but 'leapfrog' over to Groningen, Utrecht, Maastricht, Breda or The Hague. The large cities of Amsterdam and Rotterdam are very lop-sided in their regions, because there are no independent housing markets in the provinces of Noord-Holland and Zeeland. The Amsterdam housing market envelops the province of Noord-Holland almost entirely, and the Rotterdam region encompasses the islands of Zuid-Holland and Zeeland. The medium-sized towns of Leiden, Amersfoort, Almere, Haarlem and Dordrecht (19,000 relocations annually) form the centre of the smallest housing market regions. According to the criteria used, the 'Randstad' towns of Zaanstad, Delft, Zoetermeer, Haarlemmermeer and Alkmaar, and outside the 'Randstad' the towns of Heerlen, Ede, Emmen en Deventer, do not quite qualify as independent housing markets.

Centres with different characteristics

The cities at the centre of these 21 housing markets in the Netherlands differ in terms of position in the internal migration patterns (of young adults). This translates into a relatively large or indeed relatively small number of incoming or outgoing removals (table 2). Half of these centres – those offering considerable opportunities for higher education, such as Eindhoven, Groningen, Leiden and Utrecht, experience both a high inflow and a high outflow (of young adults). These cities can be characterised as 'nurseries', where young adults cut their teeth on the housing and labour markets, but where they do not put down permanent roots.

Amsterdam and Rotterdam likewise experience a relatively strong inflow, but in contrast to the above-mentioned cities, the outflow is relatively light. It would appear that those who move to these two cities find their ultimate destination there.

Cities with vast new housing estates and relatively few higher education opportunities, such as Almere, Amersfoort and Breda, mainly exhibit a large outflow (of young adults). These cities have relatively high numbers of families and are sometimes called 'cradle towns'.

Finally, in some cities, such as Apeldoorn, Dordrecht and Zaanstad, both inflow and outflow are relatively limited. Despite the availability of higher education, the towns of Enschede and Tilburg also belong to this reserve group. Because of poorer economic dynamics or limited possibilities for housing construction, these towns exert little gravitational force.

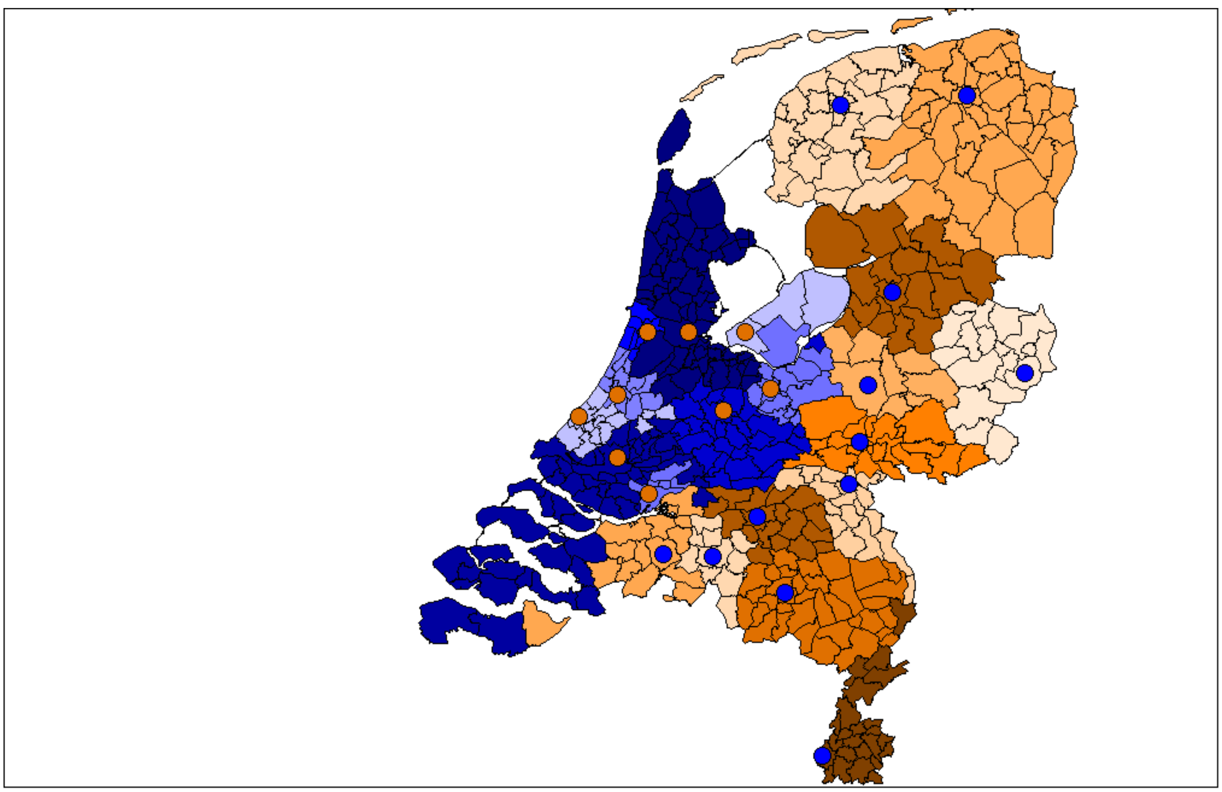
Conclusion

The Dutch housing market can be subdivided, not only according to housing segment, but also geographically. On the basis of the 1.6 million relocations that take place annually in the Netherlands, 21 regional housing markets can be defined, in which internal dynamics are stronger than external factors.

This regional cohesion becomes more pronounced if account is not only taken of relocations between municipalities, but also within municipalities, and it is even stronger, the smaller the number of regions defined.

Each region orbits around one of the large or middle-sized cities. The less stringent the criteria for cohesion within a region, the more the distinctions between housing markets are blurred (particularly in the Randstad urban belt).

Map 1: 21 Housing market regions

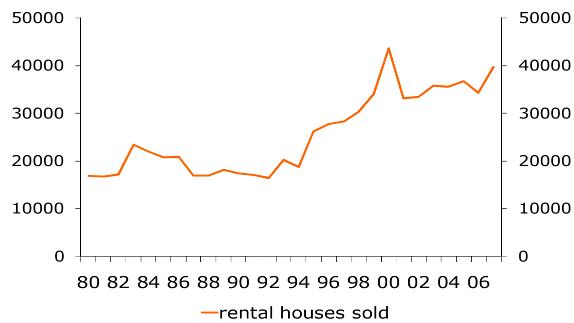


Source: ABF-Research; data processing, Rabobank

Part-selling of properties

Investors may buy portfolios of rented properties – often apartments – with the intention of offering these for sale to private individuals. As such this process constitutes an important link between the rental and non-rental markets. The units can be sold to the existing tenants, or to others once the house is vacant. These investors therefore have two potential sources of income: either directly from existing lease contracts, or indirectly from sales gains.

Figure 18: Rental houses sold 1980-2007



Source: ABF-Research, data processing, Rabobank/ FGH Bank

Part-selling of this nature can be active or passive. When it is active, the owner aims to sell the property as quickly as possible, and will work on the tenants to achieve this for example by offering them compensation for moving out. When the investment is passive, the owner's ultimate aim is likewise to sell the property, but not until it becomes vacant in due course. One reason for this willingness to wait can be the expectation of a considerable rise in value. The passive investor needs to take account of costs for maintenance and upkeep, which will have to be offset against any profits made from a sale.

When non owner-occupier apartments from a large rental portfolio are sold off in single units the vendors are usually institutional investors or housing corporations. There is usually a strategic portfolio-related reason for part-selling. For instance, the proceeds from part-selling can release funds for new investments. Accordingly, part-selling of housing units is important to maintain the dynamic in the market.

Market volume

An analysis of changes in the supply of rental properties can give a good indication of the size of the part-selling market. If we offset the growth of the annual rental housing supply against turnover based on new construction, demolition and other changes, then we see that on average over 25,000 rental houses were sold annually during the period from 1980 to 2007. The past 15 years show a clearly rising trend. This is probably related to the increasing preference for owner-occupier houses, which has become manifest especially since 1995. Since then on average some 33,500 rental houses were sold annually. Despite this rise in the number of rental properties sold, this remains a specialised market. In total, the part-selling market accounts for only 1% of the total rental housing market.

Favourable markets

Part-selling is geared towards the frequent selling of rental properties. Its success depends on the degree of dynamism on the housing market. The supply of houses in this market consists mainly of social housing, comprising mainly cheaper and mid-priced units. Part-selling is therefore chiefly aimed at first time buyers and those lower down the property ladder.

In order to understand the part-selling process, it helps to consider indicators that influence the housing market. A part-selling project depends partly on demographic developments for success, i.e. on the growth of the number of inhabitants and households. It also depends on the housing stock (the number of available units in relation to demand), economic development (disposable income, affordability, and interest rates), price development (house prices and rental prices) and on consumer confidence.

Favourable markets are mainly found in cities with a relatively large rental housing stock and a young population. In these markets the supply of houses for sale is limited and numbers of first-time buyers are high. It is not only the large cities that offer suitable opportunities for part-selling; the medium-sized towns outside the Randstad urban belt also contain favourable markets.

Part-selling also takes place in smaller municipalities. Here too, there are opportunities for successful investment. However, sales turnover may be slower. The size of a part-selling portfolio should therefore be viewed in the light of the total demand in a market.

Factors that determine value

For part-selling, a number of parameters are important in determining the value of a property.

Occupancy turnover

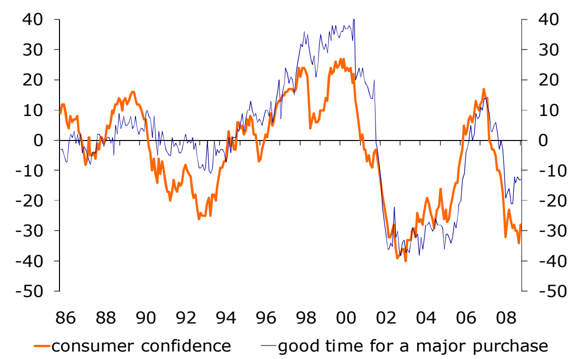
One of the main considerations in relation to part-selling is the occupancy turnover rate, i.e. the rate at which units become vacant and can be sold. This turnover rate depends on three factors: the initial vacancy, sale to sitting tenants and the number of lease terminations.

Unoccupied property value (i.e. sales value when vacant and not rented or in use)

A further important concept for the part-selling market is the question of unoccupied value of a property. The unoccupied value can essentially be compared to the sale value of a property when not rented or in use. The value of a vacant property in this sense is always higher than when the property is rented out. The unoccupied value is used as a basis for calculating potential yield.

Discount factor
The *discount factor* is used to calculate the present value of future cash flows. This interest rate factor is an essential variable for this calculation process. The present value of predicted cash flows is calculated on the basis of this factor.

Figure 19: Confidence low, no major outlays



Source: Statistics Netherlands, Rabobank

Exit yield
For the purposes of calculating the residual value, the exit yield method is often used. In effect this is the same as applying the initial yield method to the end of the period under review. To estimate the residual value, the resulting investment should be corrected for the usual factors such as buyer's costs, remedial maintenance, temporary non-occupancy, and the difference between contractual rents and market rents.

Rental development
The development of rents is important for the business of part-selling. Whether a tenant is prepared to buy depends partly on the development of rents. A potential buyer of a part-selling unit will compare the monthly costs of purchasing the unit to the monthly costs of renting it. In this respect, it is important that the rent for houses below the € 631.73 per month limit are permitted rent increases only equal to inflation. This applies both to housing corporations and to private and institutional investors.

Current market developments
Recession versus demand for housing
The housing market has undergone rapid change in the recent period, with the Dutch economy in recession. Throughout the country the housing market is affected, with less demand for houses, especially since the second half of 2008. This puts pressure on house prices, which have dropped by several percent in recent months. The main reason for the price drop is that house-buyers are much more reluctant to take risks. In particular they spurn the risk of double housing costs. This is why those moving along the property ladder are hardest hit by the crisis, as opposed to first-time buyers. Householders first want to sell their existing house before purchasing another one. For new entrants to the housing market however, the situation has created opportunities: affordability has improved slightly, which makes owning a home more attainable.

The economic crisis has put pressure on the sale of newly completed houses in particular. This is not so much reflected in the output figure for 2008, which at over 80,000 completions, is comparable to the level of 2007. It is the expectations for the coming period that give cause for alarm. According to the EIB (economic institute for the construction industry), new housing completions are set to drop by 20% in 2009 and 2010. This will happen despite the fact that higher construction volume is badly needed to reduce the shortage of housing, which still runs at 2%.

Consequences for part-selling
These developments also have implications for the part-selling market. In particular, the occupancy turnover rate has been lower than usual, as a result of the severe lack of confidence in the market. However, in recent weeks there are signs of some stabilisation in the first-time buyers' market. This will restore some life to the market, which is necessary to give some impetus to the part-selling process. Another positive factor is that continuing low interest rates have contributed to a slight improvement in affordability. In contrast to the more expensive housing bracket, the market for this kind of low cost housing appears to be able to hold up.

Medium-term prospects
Housing shortage and regional differences
Developments now taking place may have a large impact on the housing market in the medium term. There is already a country-wide housing shortage, partly because too few houses were built in the past decade. Furthermore, part of the housing stock is due for demolition or restoration. In addition, the population will continue to grow for the next ten to fifteen years, and the total number of households will be further driven up by the growing number of single-person households. In quantitative terms, there is an annual requirement of some 80,000 to 83,000 new housing completions annually. With construction output threatening to fall well short of this level, the housing shortage will become more acute in the coming years. Once the economy picks up, we could see house prices rising very quickly again.

There are growing differences between the regions – a process that was already set in motion before the credit crisis. Mainly for demographic reasons, there are increasing differences in outlook for the various regions. Growth regions, including the northern wing of the Randstad urban belt, headed by the area of Amersfoort/Zwolle (Noordwest-Veluwe) will experience ongoing housing demand for the time being. Other regions, such as Zuid-Limburg, North-East Groningen and Zeeuws-Vlaanderen can expect an easing demand.

Consequences for part-selling
These developments have two major medium-term implications for the part-selling market. Demand for houses will prevail, with both occupancy turnover rate and unoccupied value developing positively in the long term. However, an important consideration for part-selling investment portfolios is that the region

and location of a project should show clear growth and dynamism. These characteristics are most evident in the Randstad and in various larger towns outside the urban belt.

Conclusion and expectations

The financial and economic crisis has crushed buyer confidence in the housing market since the second half of last year. The number of houses sold has plummeted, pushing prices down. The housing market has become a buyers' market. In this respect, differences between 'strong' regions and 'weaker' regions will be further exacerbated during the coming period. Particularly in the Randstad urban belt, a housing shortage still prevails; and although price corrections have also take place here, these will be temporary and are the result of a mismatch in the market. In more peripheral regions the downturn may be expected to have more sizeable consequences. Large-scale new construction will only be possible in these regions if old buildings are demolished.

With regard to the part-selling market, the recession, coupled with low consumer confidence and the slump in house prices mean that tenants are currently less inclined to buy an apartment. Consequently, turnover rates have fallen. Nonetheless, the need for housing combined with the ongoing rise in the number of households will continue to ensure demand for houses. Faced with a drop in new completions in the short term, increased pressure on the existing housing stock can be expected. This presents opportunities for part-selling once the market picks up.

Outlook

Times are tough for the housing market in the Netherlands. The financial crisis has dealt a severe blow to the confidence of potential house-buyers. Fewer houses are being sold, with the expensive segment currently hardest hit. At the same time, the supply of houses on the market is increasing, as is the time it takes to sell them. This is unfavourable for the movement along the property ladder that is so important for dynamism on the Dutch market. House prices are now declining according to all the known indices. Large differences can be observed in the various price brackets – the so-called composition effect. Because the most expensive bracket is hardest hit, this has pushed down both the average and the median price. Indices such as the NVM median price are not corrected for this phenomenon.

It is not only the housing market that is having a bumpy ride. The Dutch economy is shrinking and is in recession, as is the case with virtually all trade partners. For 2009 we expect year-on-year negative growth of 4%, and of 1% for 2010. At the same time, unemployment is rising. For 2010 we envisage a doubling of the 2008 jobless figure. Clearly, there is considerable hardship attached to losing one’s job. Even the prospect of a possible loss of part of the household income can have a paralysing effect on making large outlays, including the purchase of a house.

With confidence at such a low ebb and buyers adopting a wait-and-see attitude, it is not easy to predict the development of house prices. If we don’t correct for the above-mentioned composition effect, the median house price may drop by some 10% or even more this year. However, we believe that this does not do justice to current market developments. After all, the current median-priced house cannot be compared to the median-priced house of six months ago. It is much smaller and poorer in quality. Even if we make a more realistic comparison between houses of the same size and quality, Rabobank still expects a further price drop for 2009, although not to the extent of the above definition. Nonetheless, prices will drop further than we had envisaged in the previous Housing Market Quarterly.

In view of the current deterioration in market developments, Rabobank anticipates a **nominal house price drop of 5% for 2009, and of 1% for 2010.** The downward risk for house-buyer sentiment and for market dynamic outlined in our previous Quarterly continues to exist. Furthermore regional differences will increase. Particularly regions with a shrinking population and a housing stock surplus may experience lengthy selling periods which will drive prices down further. In terms of the various price brackets, the more expensive bracket will be hit harder than the middle and lower segments. However, this deviation is not necessarily caused by current market circumstances. The price development in the more expensive bracket is always more volatile.

Key figures

House Prices

Year-on-year change (%)	2007	2008	2009 [a]	2010 [a]
NVM (median house price)	3.6	0.0	-5	-1
Land Registry (average house price)	5.3	2.7	-	-

Totals

x 1000	2007	2008	2009 [a]	2010 [a]
Sales transactions	202	182	155	165
Newly built homes	80	79	72	65

Totals

	2007	2008	2009	2010
Enforced Sales	1,811	1,961	-	-

Key economic figures (May 2008)

	2007	2008	2009 [a]	2010 [a]
GDP (growth, %)	3.5	2	-4	-1
Inflation (%)	1.6	2.5	1	½
Unemployment (x 1000)	344	305	440	640

Rabobank affordability index

x 1000	2007	2008	2009 [a]	2010 [a]
Affordability index [b]	84	82	97	96

Interest rates [c]

Level (%)	12 May 2009	+3m [d]	+12m [d]
3-month Eurozone	1.30	0.97	1.17
10-year Euroswap	3.53	3.43	3.70
Mortgage interest rate, 5-10 year fixed	5.40[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] March 2009 monthly average, DNB

Colophon

The Dutch Housing Market Quarterly is a publication of the Economic Research Department (KEO) 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 Ecowin, Land Registry, NVM, DNB, CPB and Statistics Netherlands.

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