Housing market monitor

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New cabinets' policies less favourable for private rental investors

- Reducing the housing shortage and increasing construction has been made a policy priority
- However, it remains unclear how the government intends to realise the higher construction ambition.
- It also waits to take decisions on the owner-occupied taxation
- Low mortgage interest rates continue to boost house prices: price estimate for 2022 +12.5%, for 2023 +5%

House prices continue to set records, mainly due to low mortgage rates. Although the decline in mortgage rates has been halted by increased inflation, we believe that mortgage rates will remain low on balance. This means that house prices continue to rise. After a 15% increase in 2021, we think that house prices will increase 12.5% this year and 5% next year. The rise in prices will slow down, because the positive effect of the low interest rate is already largely incorporated in house prices. Besides interest rates, house prices are also receiving some support from wages. Wage growth remains positive thanks to the tight labour market and the economic recovery that lies ahead once the lockdown measures are reversed.

The number of transactions, on the other hand, is expected to decrease in the coming years. After a 5% decline in 2021, a 10% decline will follow in 2022. A recovery may follow in 2023. We expect a rise in transactions of 5%. House purchases are strongly determined by available supply. Currently, there are hardly any houses for sale and new construction is lagging behind, so that fewer and fewer transactions are taking place. Homeowners are postponing the moment of sale because they first want to find a suitable home for themselves. With the current price increase, it can also be worthwhile to wait. As soon as the price rise has subsided sufficiently and new housebuilding starts to pick up, more houses will gradually be offered and the number of transactions will start to rise again from 2023 onwards.

The tumultuous development in the housing market is forcing the government to take measures. Too many people are sidelined. The coalition agreement therefore devotes a great deal of attention to the housing market, but on closer inspection the measures are disappointing. There will be a Minister of Housing. However, it is unclear which additional powers he will be given. The government acknowledges that climate change has consequences for housing construction, but does not draw any firm conclusions from this. The cabinet does change the direction of the rental market. Rutte IV is friendly to housing corporations, but turns away from private investors, a radical departure from Rutte II, which decided the exact opposite. Finally, the cabinet does not dare to make a decision about the tax system. The tax treatment of owner-occupied homes will therefore remain unaffected, while studies commissioned by the Ministry of Finance indicate that this is unsustainable.

Finding a suitable, affordable home is becoming increasingly difficult

The mood regarding the housing market is now less positive. The Dutch Home Owners' Association's market indicator dropped from 105 in January to 100 in November, the neutral value whereby the number of optimistic respondents equals the number of pessimistic ones. Almost three quarters of respondents think that it is not a good time to buy a house, citing the high price level and the limited supply of houses as reasons for this.

There are hardly any houses for sale. According to the Dutch Association of Estate Agents, the supply in the third quarter was less than 17,000 houses. The scarcity indicator, which compares the supply with the number of transactions and thus indicates from how many houses buyers can choose, stood at one and a half houses in the third quarter. In fact, buyers have no choice. Whoever finds something suitable must decide quickly. The houses sold by estate agents were on average on the market for 23 days.

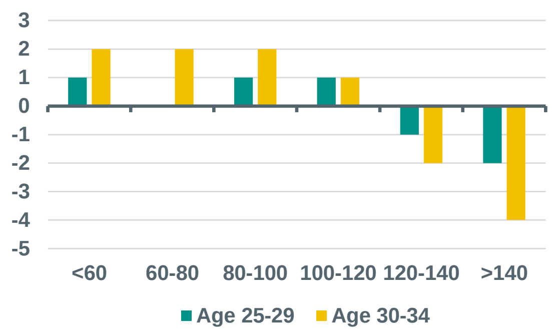
Diminishing optimism about the housing market

Market indicator (index 100 = neutral)

Source: Dutch Home Owners Association

Young people buy smaller houses

Difference in percentage of homes bought by area in square metres (2021 versus 2017)



Source: Land Registry

Due to the quick turnaround, the number of transactions is still relatively high, despite the tight supply. According to CBS/Kadaster, a total of 232,000 homes were sold from December 2020 to November 2021. However, this is lower than in April when the annual number peaked at 251,000 transactions. The decline in the number of transactions partly reflects the reduced enthusiasm to buy, but mainly the great difficulty buyers have in finding something suitable in the current tight supply.

Buying a house is difficult for many groups, especially young people. Their income is generally lower and they are more likely to have flexible contracts, which makes it harder for them to get a mortgage. As a result, they are forced to make concessions more quickly. The homes that young people aged 25 to 35 are buying are becoming increasingly smaller. There is also a difference between first-time buyers and those who are moving up the housing ladder. First-time buyers cannot take along any surplus value and focus on homes with a lower purchase price. But there are fewer and fewer of these. Eight out of ten first-time buyers therefore consider the market unfavourable. At the current, increased price level, single income households do not get in easily either. Their share in the transactions is falling.

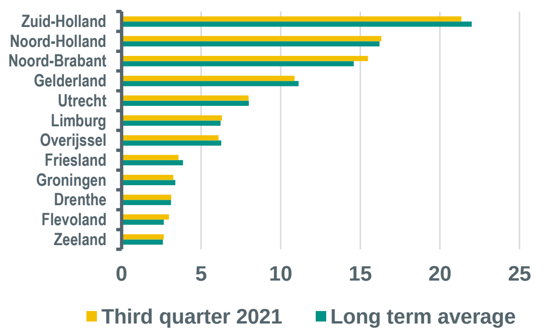
Longing for green surroundings doesn't imply moving to the countryside

The interest in living in a green environment is increasing, but there is no mass exodus from the city. Those who leave the cities usually move to a suburb or another city. Only one in twenty of those leaving the city choose a more rural home, preferably in villages with good facilities and beautiful surroundings. The number lags behind because home movers want to stay connected to the labour market and value the accessibility of their workplace.

The popularity of the Randstad therefore remains undiminished. This can be seen in the share of transactions, which picked up again in the third quarter, and in price developments. Prices are rising quarter-on-quarter as fast as the national average. The latter is also attributable to the four major cities. Prices in Amsterdam and Utrecht, in particular, are rising strongly again.

Regional transaction shares remain stable

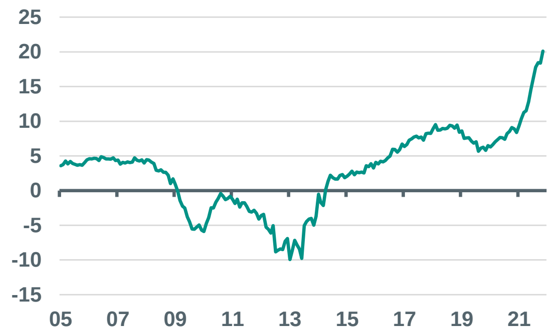
Percentage share



Source: CBS/Land Registry

Price increase is historically high

Percentage change year-on-year



Source: CBS/Land Registry

Higher purchase prices, both for existing and new homes

Although asking prices hardly ever rise anymore, purchase prices are currently going through the roof. Many buyers are forced to bid above the asking price. Eight out of ten buyers do so, with the result that transaction prices continue to rise. In November, the average price level was more than a fifth higher than the same month a year ago, the strongest increase since the beginning of the series. The average selling price in November was EUR 404,000. Last November, the average selling price was EUR 60,000 lower.

The strong price rise has an effect on new-build homes. The price of these is determined by existing construction, as the number of new homes added each year is only a fraction of the total housing stock. In the second quarter, the average selling price of new homes was EUR 442,000. The number of new-build transactions also rose. Since April, however, the number of new owner-occupier transactions has remained at 38,000 on an annual basis.

Government wants to boost house building, but does not clearly indicate how

Because house building has lagged behind demand for years, the government has raised the annual ambition in its coalition agreement from 75,000 to 100,000 new owner-occupied and rented homes. This should bring the one million homes that forecasts suggest will be needed in the next ten years to make up for the housing shortage within reach.

The government takes this task seriously and appoints a Minister of Housing to ensure that this ambition is actually realised. Unfortunately it is still unclear how a minister can make a difference, as the government is not reserving any extra money for manpower, nor is the minister being given any additional powers. That this is necessary is evident from the evaluation of the regional housing deals. In these housing deals, all the parties involved sit down at the table to make joint agreements about new housing construction. This helps to reach agreements more quickly. But since the agreements are not necessarily binding, not all of them are implemented.

Numerous obstacles stand in the way of residential construction

Although it is encouraging that the number of 'hard' construction plans at municipal and provincial level is increasing, it is uncertain whether these will be realised. There are still a lot of obstacles on the road, starting with capacity problems in the construction industry. The shortage of personnel means that many vacancies remain unfilled and wage costs are rising. In addition, construction materials are becoming more expensive due to the lack of raw materials. Because of the continuing cost increases for construction companies, there is a growing danger that construction projects will be delayed and projects compromised.

Postponement may also be due to the land market. Since the credit crisis, municipalities have cut back on their land positions. Market parties that acquire raw land to secure building rights have taken over their positions. This limits competition in housing construction. As a result, housing production is less efficient, the unprofitable top is in sight sooner and the hard planning capacity sometimes remains unused. The risk that this will occur more often in the future is growing, all the more so because two-thirds of the building order falls in the affordable segment where the margins are smaller: rental homes up to EUR 1,000 monthly rent and owner-occupied homes with a purchase price up to the NHG cost limit[1].

Plot prices rise further

Average price per plot in euros per square metre on an annual basis

Source: Land Registry, edited by ABN AMRO

Many construction plans in sensitive areas

	Number of dwellings (thousands)	Investment needed (EUR billion)
Soft soil	70	30
Soil susceptible to settlement	80	22
Wet soil	160	47
Dry soils	400	120
Saline soils	250	69
Submersible inland dike	580	175
Floodable outer dike	33	8
Combination outer dike	**300**	**88**
Combination inner dike	**820**	**245**

Source: Delta Committee

Housing plans take too little account of the consequences of climate change

Another concern is that part of the hard planning capacity may not be as hard as expected due to climate change. An inventory by the Delta Commissioner reveals, for example, that the majority of housing construction plans take insufficient account of the risks of flooding and subsidence. The danger of extra costs is therefore lurking. Many municipalities are already failing when it comes to recovering the costs of infrastructural facilities from project developers. If the costs of climate change are added to this, it remains to be seen whether all those 'hard' plans for affordable housing will actually be implemented.

The alternative is to build in areas that are less vulnerable to climate change, for example outside the Randstad. However, this is easier said than done. Employment and social facilities are important ingredients in the choice of where to live. At present, the growth in jobs is concentrated mainly in the large cities, a trend that according to the Netherlands Environmental Assessment Agency (PBL) can hardly be reversed. PBL therefore recommends building mainly within the large cities and their suburbs. The disadvantage, however, is that this entails high planning costs, due in part to the laborious public consultation procedures. These are insufficiently streamlined. There is also a lack of financial incentives to counteract NIMBY behaviour and to win over opponents of new construction in their immediate vicinity.

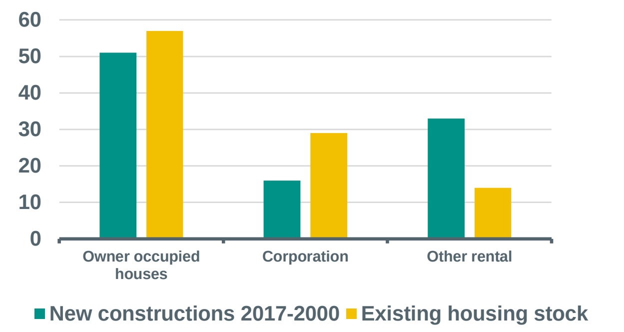
1 The NHG threshold has been raised from EUR 325,000 to EUR 355,000 as of 1 January. At the same time, NHG has lowered the deposit fee from 0.7% to 0.6%.

Rutte IV friendlier for corporations

Finally, what can frustrate the hard construction plans is the dependence on housing corporations. In recent years, they have been less active in building new houses, as the landlord levy has put a strain on their budgets and the market test has sidelined them from building new houses in the mid-range segment. The private sector was left to pick up the tab. Now the Cabinet is abolishing the landlord levy, suspending the market test and trying to channel money from rich to poor housing corporations through project support. However, this is no guarantee that corporations will have sufficient financial resources to build again. Due to the low rents, their income is limited. Moreover, the corporations also have to pay for the extensive sustainability measures, overdue maintenance and foundation problems in the existing housing stock.

Corporations keep away from new buildings

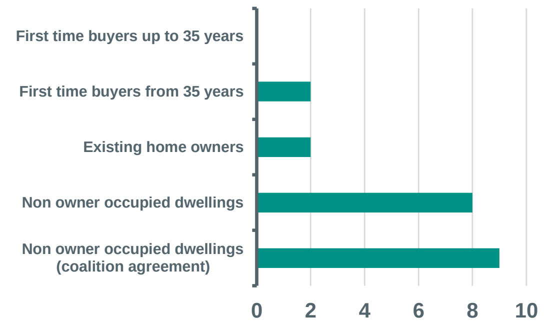
Share by client



Source: Land Registry

Increase in property transfer tax for investors

Transfer tax rate (%)



Source: Tax Office

Residential investors are less popular

In opting for corporations, the government is revisiting the policy of Rutte II, which restricted corporations and gave free rein to private landlords. The possible outcome of the change is that private landlords will withdraw. The volume of investments has already declined over the past year, partly due to a lack of supply, but also due to measures introduced by Rutte III that make it less attractive to rent out homes, such as the increase in the transfer tax rate, the extension of the buy-out protection to existing buildings and the ceiling on the number of rental points based on the value of the home, which will make it more difficult for landlords to transfer homes from the social to the non-commercial rental segment and may cause previously liberalised rental homes to fall back into the social segment.

Rutte IV is taking this one step further by increasing the transfer tax rate from 8% to 9%, tightening the requirements for the energy label and requiring permits to keep out malicious landlords. Furthermore, the government wants to tax the income from renting out homes more heavily. Higher taxes will affect the return on housing.

According to recent insights, the return on rental homes is less than previous scientific studies on the subject, because these earlier studies did not take such burdens as the transfer tax into account as effectively as they should have done. Moreover, the relationship between the return and the risk that investors run in the form of price fluctuations turns out to be less favourable than thought when the value of individual homes is considered instead of the value of the housing portfolio as a whole.

Cabinet maintains tax preference for owner-occupied homes

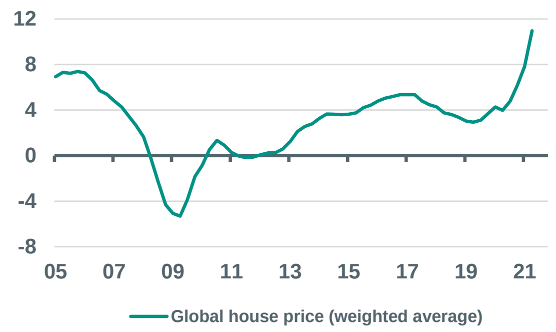
It is noteworthy that the cabinet refrains from changing the tax regime for home owners. The only change the Cabinet is making is to abolish the homeowner's gift exemption. This is in spite of the fact that influential international organisations such as the IMF and the European Commission have long been calling for more far-reaching measures, such as a faster phasing-out of the mortgage interest deduction and the Hillen scheme, and a smoother increase in the notional home ownership tax credit. This is because these regulations distort the labour and capital markets.

DNB and the Financial Stability Committee have also recommended that tax incentives for home ownership be reduced. The government has ignored all recommendations, however, but is not sitting still. With the conversion of Box 3 to real yield and the tax changes for private landlords, the cabinet is paving the way for future changes.

Fiscal adjustments could put a brake on price increases in the Netherlands. This has been shown by Danish research. Surprisingly, it also shows that tax relief has little effect on home ownership as such, but encourages home owners to live larger and more expensively, and to take on more debt. Apart from the finding on home ownership, these effects are also evident in a study of the situation in the United States.

Abroad house prices rise strongly too

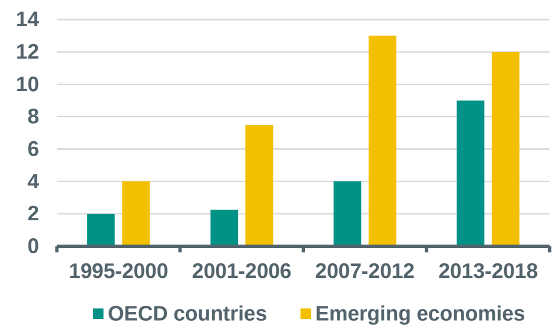
Year-on-year percentage change



Source: Dallas Fed

Macro-prudential instruments used more often

Average number of macro-prudential measures per year



Source: BIS

Growing international concerns about a possible price correction and its financial consequences

The strong rise in house prices is an international phenomenon. In the eurozone, too, prices are rising fast, by 6.8% year-on-year in the second quarter. This is a concern for the ECB, which warns of possible price corrections in its Financial Stability Report, something that also worries the IMF in its most recent report on the Dutch economy. Model results from the IMF point to overvaluation of the Dutch housing market. The IMF therefore welcomes the fact that DNB will impose higher capital buffers on banks when they provide mortgages from 2022, a measure that could translate into higher mortgage interest rates.

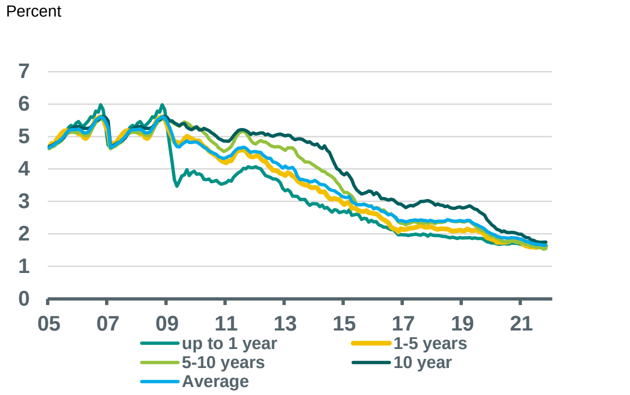
When central banks have little scope to tighten monetary policy because of the weak economic situation, they have to resort to other macroprudential instruments. According to a study by the BIS, central banks are using these more often nowadays. This is because lending standards also have an impact on lending and house prices. However, DNB's instruments on that front are limited. In the Netherlands, the government decides how much mortgage home buyers can borrow on the basis of the collateral and the new government has indicated that it will stick to the 100% standard. Furthermore, the government is advised by the Nibud on how much people can borrow based on their income. For 2022, the income borrowing standard has been tightened somewhat in connection with the higher cost of living. Finally, the new cabinet wants the current rather than the original level of student debt to determine the maximum mortgage, which implies a broadening of the borrowing standard.

Monetary policy remains supportive of housing market

The economic situation continues to give cause for an accommodative monetary policy. The fifth wave of contagion and the reintroduction of restrictions are affecting business and consumer sentiment. Consumption is falling and will not rebound until lockdown measures are eased. Wage growth and savings will provide support. On the other hand, rising inflation is hampering the recovery of consumption. Our latest forecast for GDP growth this year is 2.8%. This is significantly lower than the 4.3% growth forecast for 2021.

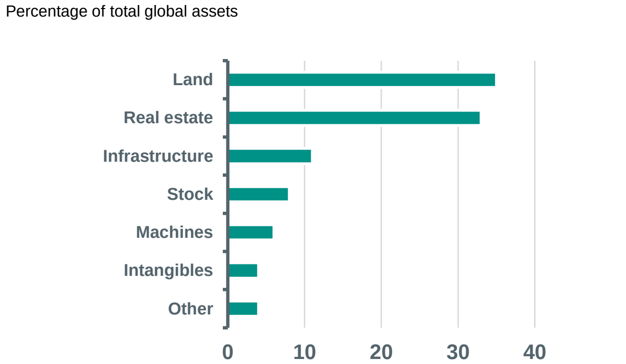
For the coming years, we also expect a very modest increase in the 10-year government yield. While higher energy prices and disrupted supply chains are pushing up inflation, there is no indication yet that these temporary disruptions will lift inflation to a durably higher level and push monetary policy towards tightening measures. That will only happen if wages also rise sharply, but there are no signs of that happening. There is plenty of room on the labour market in most eurozone countries and, with falling membership, trade unions have little bargaining power. Against this background, it is likely that the main reason for the house price rise will remain intact: low mortgage interest rates, partly due to ample monetary policy.

Mortgage interest rates drop to historically low



Source: DNB

Large share of real estate in assets



Source: McKinsey

Low interest rates and associated increased lending contribute to price increase

That there is a link between low mortgage rates and house price development is highlighted in a recent international study on the decoupling of the historical link between GDP and asset growth. The ratio of assets to GDP is now 50% above the long-term average. Two thirds of net wealth is in land and property, the value of which is strongly influenced by interest rates, as they determine the present value of future 'housing services'. Interest rates also have a strong effect on lending, which in turn is strongly linked to house price developments.

Mortgage production last year rose by about EUR 20 billion to EUR 160 billion. Institutional investors account for an increasing share of mortgage production. Fierce competition in the mortgage market contributes to low mortgage interest rates and a wide availability of credit, which creates room for further price increases. The share of NHG in production is falling, as fewer and fewer purchased homes fall into the NHG category. Furthermore, there is a strong preference for long-term loans. A large part of mortgage production is linked to refinancing to reduce interest costs. Loans for home improvement are also taken out more frequently. The net increase in the volume of mortgages is less than suggested by the mortgage production given the large redemptions, for example by people selling their homes. In the second quarter, mortgages outstanding totalled EUR 765 billion, EUR 22 billion more than in the second quarter of the previous year.