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Dutch Residential Mortgage Market
2018-Q4 Quarterly Update

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Introducing our quarterly reports

In this quarterly report we discuss developments in the Dutch housing market and the broader economy. Several indicators became less positive during the quarter but there were also positive developments as analysis by the Dutch National Bank showed that more people are getting permanent contracts and that wage growth is expected to pick up in the coming years. As always, we welcome the opportunity to discuss the housing market or investing in Dutch mortgage loans with you.

Jasper Koops,
Portfolio Manager

Comment

We have mentioned in recent quarters that the price divergence in the Dutch housing market between the large cities in the Randstad and the rest of the country has been increasing. This quarter we have looked at how people in the 4 main cities in the Netherlands have started to look at alternatives outside of the big cities.

The data shows that a high proportion of people have left the main cities within 4 years of having their first child. Furthermore, the steep price increases in recent years have meant that fewer mortgages are underwater, thus enabling people to move.

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Dutch Residential Mortgage Market 2018-Q4 Quarterly Update

1. Executive Summary

House price increases slowing down: Dutch house prices increased 1.5% during 2018-Q4, significantly less than in the previous quarter (2.7%) as prices even decreased 0.6% MoM in December 2018. Price increases are much steeper for new (17% YoY as of 2018-Q3) than for existing dwellings (9.2% same period).

Decreasing number of property transfers: approximately 57,000 houses were transferred in 2018-Q4 in the Netherlands, a decrease of more than 14% compared to 2017-Q4.

Strong migration trends: CBS published migration data from 2017. We compare it to data from 2012 as we find an increasing amount of net migration from the main cities to smaller Randstad cities.

Confidence is quickly decreasing: Dutch consumer confidence decreased significantly during the quarter as consumers became less positive about the past and future economic situation.

Labor markets are getting increasingly tight: the unemployment rate reached a lower level than the previous low in 2008 as tension increased in the labor market. The Dutch National Bank noted that a higher proportion of people are getting permanent contracts and that wage growth is expected to pick up in the coming years.

Swap rates decreased significantly: mortgage spreads became much more attractive during the quarter as mortgage rates largely remained flat, but benefited from swap decreases of more than 20 basis points in the quarter.

Lowest number of quarterly NHG loss declaration in 9 years: the 174 submitted loss declarations in 2018-Q3 marked a 40% QoQ decrease.

Monetary policy: the ECB decided to keep the rates unchanged. The Inflation estimate for the euro area for 2019 was lowered from 1.7% to 1.6% while the GDP growth estimate for 2019 was lowered from 1.8% to 1.7%.

Large increase in funding spreads: spreads in covered bond and RMBS markets increased by more than 20 and 10 bps respectively during the quarter.

2. Market update

The following sections provide an update on the macroeconomic outlook, Dutch mortgage loan interest rates and spreads, the RMBS market, the Dutch mortgage loan and housing market, mortgage (related) regulation, and other relevant developments.

Macroeconomic update

The most recent economic updates of the Central Bureau of Statistics ("CBS") on key economic indicators indicated a slow-down in GDP growth as it retraced from 3.1% YoY in 2018-Q2 o 2.4% YoY in 2018-Q3 (published with one quarter delay, Figure 1). CPI increased slightly from 1.9% YoY in September 2018 to 2.0% YoY in December 2018. The change in the Harmonized Index of Consumer Prices (HICP) was more noteworthy as December 2018 was the first month since February 2018 where the Netherlands recorded higher price increases than the Eurozone (Figure 2). Unlike the CPI, the HICP does not consider costs related to home ownership.

- Inflation in the Netherlands was higher than in the Eurozone -

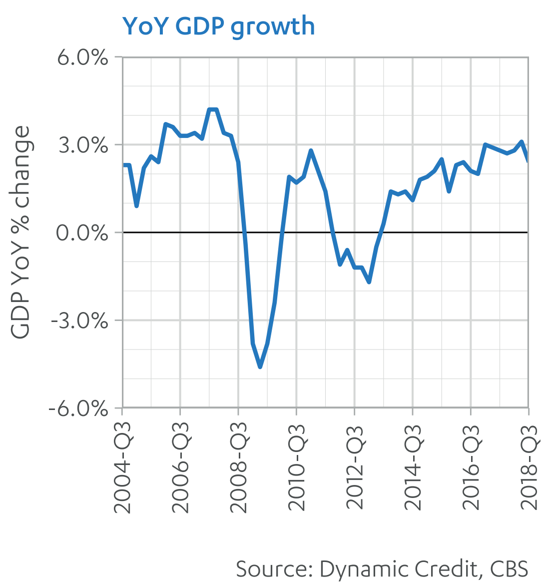


Figure 1: Dutch GDP growth. As of 2018-Q3

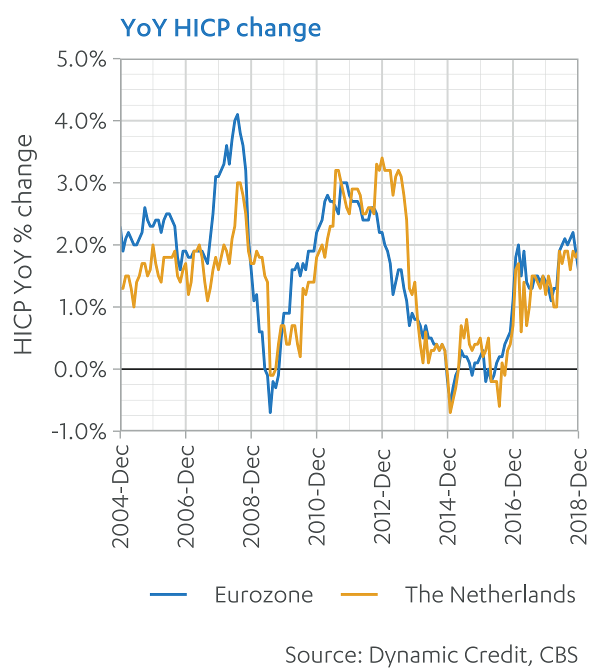


Figure 2: HICP change. As of December 2018

- Prices in the housing market expected to increase at a slower pace in 2019 damping expected increases in household spending -

The Dutch National Bank ("DNB") published its Economic Outlook in December 2018. The GDP projections are less optimistic than in their June outlook as they have lowered their forecast from 2.2% to 1.7% for 2019. The DNB expects inflation (HICP) to pick up in 2019 due to an increase of the reduced VAT rate from 6% to 9% and higher energy taxes kicking in.

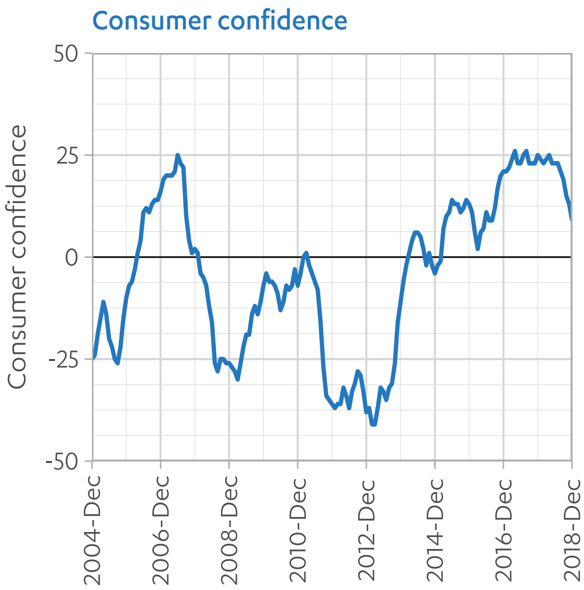
Dutch consumer confidence decreased sharply from +19 in September to +9 in December 2018 (Figure 3). The willingness to buy decreased from +8 in September to +3 in December as consumers are getting less positive when asked whether it is a good time to make large purchases. Consumers are also becoming less positive when asked about the economic climate as this category went from +34 in September to +17 in December as consumers were less positive about the past and future.

Unemployment. The employed labor force increased by 13,000 per month on average during 2018-Q4, a decrease compared to 22,000 per month in 2018-Q3. The unemployment rate decreased slightly from 3.7% in September to 3.5% in November before increasing slightly to 3.6% in December 2018. The November figure was slightly lower than the low in 2008 before the crisis. DNB reported in its December 2018 Economic Outlook that the unemployment rate is expected to remain at 3.6% in 2019 as tension in labor market is already very high.

The ratio of number of unemployed to number of vacancies has now gone from more than 7 in 2013 to 1.3 in September 2018 as the number of vacancies has been increasing while number of unemployed has been dropping.

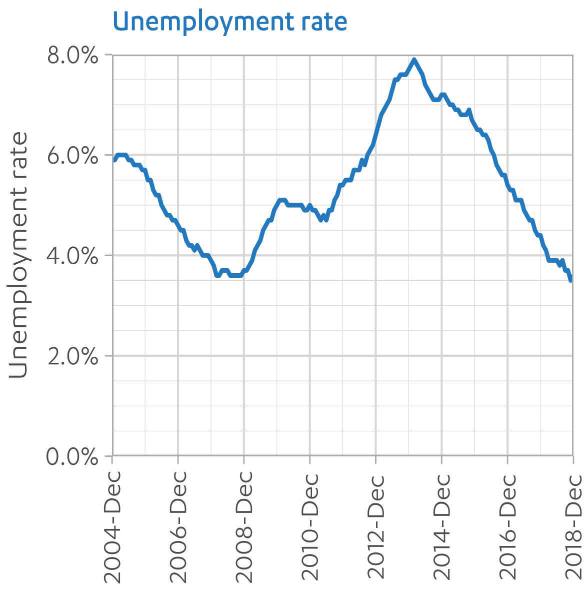
The gross labor force participation rate increased from 70.8% in September 2018 and 70.1% in December 2017 to 70.9% in November 2018.

- Number of unemployed people to number of vacancies approaching 1 -



Source: Dynamic Credit, CBS

Figure 3: As of December 2018



Source: Dynamic Credit, CBS

Figure 4: As of December 2018

Eigen Huis Market Indicator [1]

Vereniging Eigen Huis ("VEH") measures consumer confidence in the housing market every month. They do that based on questions about interest rates, prices, and the general market. Over the past 3 months, the index has decreased from 105 in September 2018 to 101 in December 2018 (Figure 5). In comparison, the index was at 111 a year ago. The indicator can take values ranging from 0 to 200, 100 indicating a neutral value. A higher value indicates a more positive sentiment.

- Confidence is rapidly decreasing -

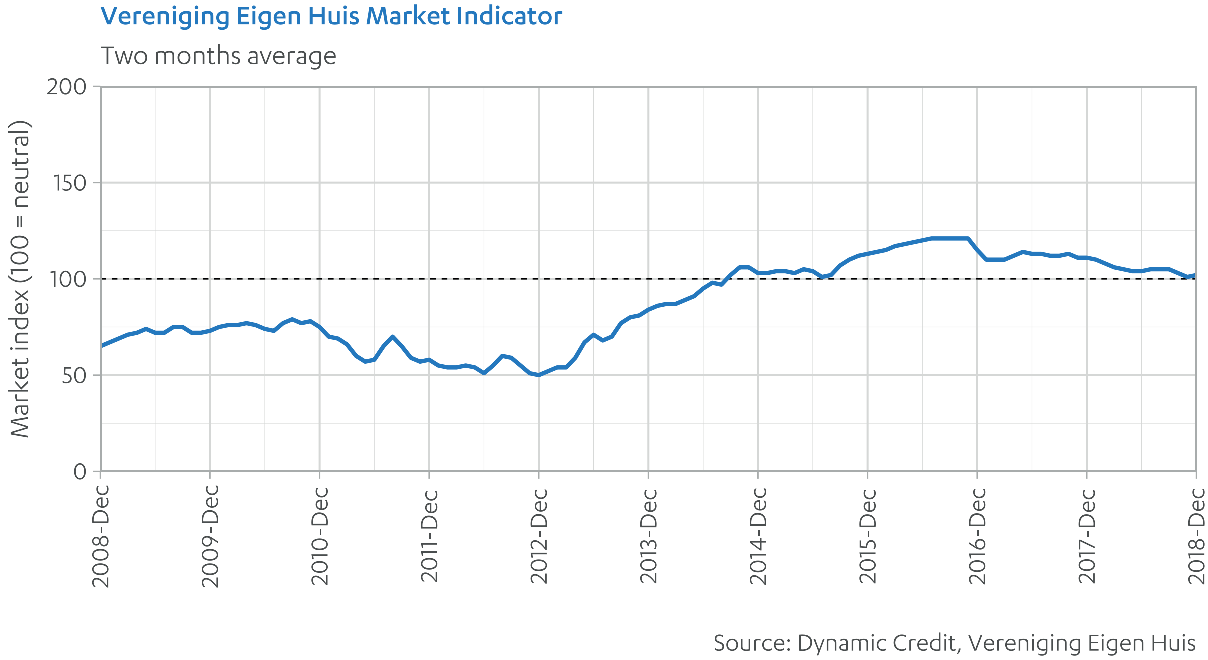


Figure 5: Vereniging Eigen Huis Market Indicator. As of December 2018

- Only 15% think it is currently a favorable time to buy a house -

VEH reports that only 15% of the Dutch people think that it is currently a favorable time to buy a house. This compares to 20% in 2018-Q3 and 33% in 2017-Q4. Furthermore, 51% think the situation will deteriorate further in 2019. The two main reasons are unaffordability and limited supply. VEH also notes that 80% of the of the Dutch people believe that house prices will continue to increase.

1 Eigen Huis Market Indicator 2018-Q4

Interest rate developments

Across all major risk classes and all major fixed rate periods, the top six most competitive rates have increased from the end of 2018-Q3 to the end of 2018-Q4 by 4 bps on average. The relatively popular 100% LTV classes generally had smaller increases than other LTV classes meaning that the spread pick-up for high LTV vs low LTV continued to decrease. For the 30- and 20-year fixed rate periods, the difference between 100% and 80% LTV rates tightened 5 and 8 bps respectively. This could be the result of the several new lenders that have entered the market in recent years with a focus on the long fixed rate period high LTV segments, as mentioned in our previous report. For an overview of the evolution of mortgage rates, see Figure 6 below.

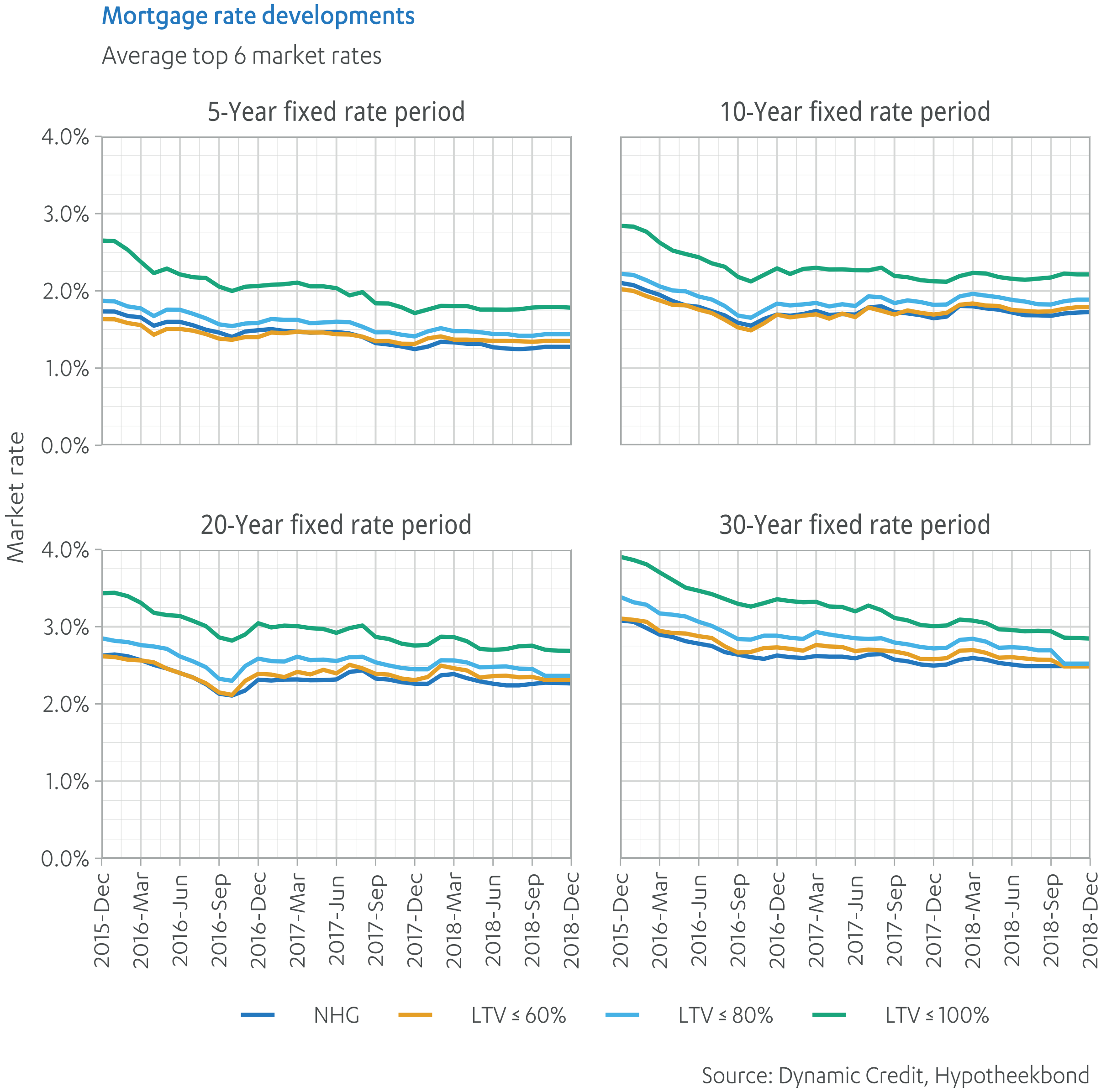


Figure 6: Average top-6 mortgage rates (excluding action rates) for mortgage loans with different fixed rate periods for four risk classes.

For a breakdown of the rates (compared to swap rates), see Figure A5 to Figure A8 in the Appendix.

Spread developments[1]

The table and graphs below show spreads over swaps for the 5-, 10-, 20- and 30-year fixed rate periods for NHG and various non-NHG mortgage loans. For a more detailed view of the rate decomposition and spread evolution throughout time, please see figure A1 to A8 in the Appendix.

The information in the table/graphs can be interpreted as a representative gross spread for newly originated Dutch residential mortgage loans over time.

Spread development for average of top 6 mortgage rates						
Fixed rate period	Risk class	2017-12-31	2018-09-30	2018-12-31	QoQ	YoY
5-year	NHG	1.08%	0.99%	1.21%	0.22%	0.13%
	60% LTMV (non-NHG)	1.14%	1.07%	1.28%	0.21%	0.14%
	80% LTMV (non-NHG)	1.24%	1.15%	1.37%	0.22%	0.13%
	100% LTMV (non-NHG)	1.54%	1.52%	1.72%	0.20%	0.17%
10-year	NHG	1.04%	0.93%	1.18%	0.25%	0.14%
	60% LTMV (non-NHG)	1.08%	0.99%	1.24%	0.25%	0.16%
	80% LTMV (non-NHG)	1.21%	1.07%	1.34%	0.27%	0.13%
	100% LTMV (non-NHG)	1.52%	1.43%	1.67%	0.24%	0.15%
20-year	NHG	1.24%	1.10%	1.29%	0.19%	0.06%
	60% LTMV (non-NHG)	1.29%	1.19%	1.44%	0.25%	0.15%
	80% LTMV (non-NHG)	1.43%	1.30%	1.56%	0.27%	0.13%
	100% LTMV (non-NHG)	1.76%	1.61%	1.79%	0.18%	0.04%
30-year	NHG	1.38%	1.25%	1.43%	0.17%	0.04%
	60% LTMV (non-NHG)	1.47%	1.34%	1.56%	0.22%	0.10%
	80% LTMV (non-NHG)	1.62%	1.47%	1.70%	0.23%	0.08%
	100% LTMV (non-NHG)	1.93%	1.72%	1.90%	0.18%	-0.03%

Table 1: Spread of the average top-6 mortgage rates (excluding action rates) over duration matched swap rates for four risk classes. Source: Dynamic Credit, Hypotheekbond

- Spreads widened significantly QoQ as swap rates decreased -

Key observations

- The average QoQ increase in spread, across all major risk classes and all major fixed rate periods (Table 1) was 22 bps. The moves in spreads result from small increases in mortgage rates and significant decreases in swap rates on average.
- Spreads for all the major fixed rate periods and risk classes have improved over the past 12 months with the exception of the 30-year fixed rate period 100% LTV segment which finished the year with a YoY spread decrease of 3 bps.
- For the 20- and 30-year fixed rate periods, there was a reduction in the spread differential between the 100% LTV (non-NHG) segment and the 60% and 80% LTV (non-NHG) segments.

[1] The EUSWxV3 swap is used, which uses quarterly resets and the floating leg is 3-month EURIBOR.

Figure 7 below shows how the extra spread for high LTV classes has been decreasing for quite some time. The current spread-pickup for the highest LTV risk class versus lower risk classes is currently between 20-40 bps, which is still significantly higher than historically realized losses between 0-15 bps per annum for non-NHG mortgage loans in Dutch RMBS during the period 2005 to 2017[1].

- The spread-pickup of high LTV classes continues to decrease -

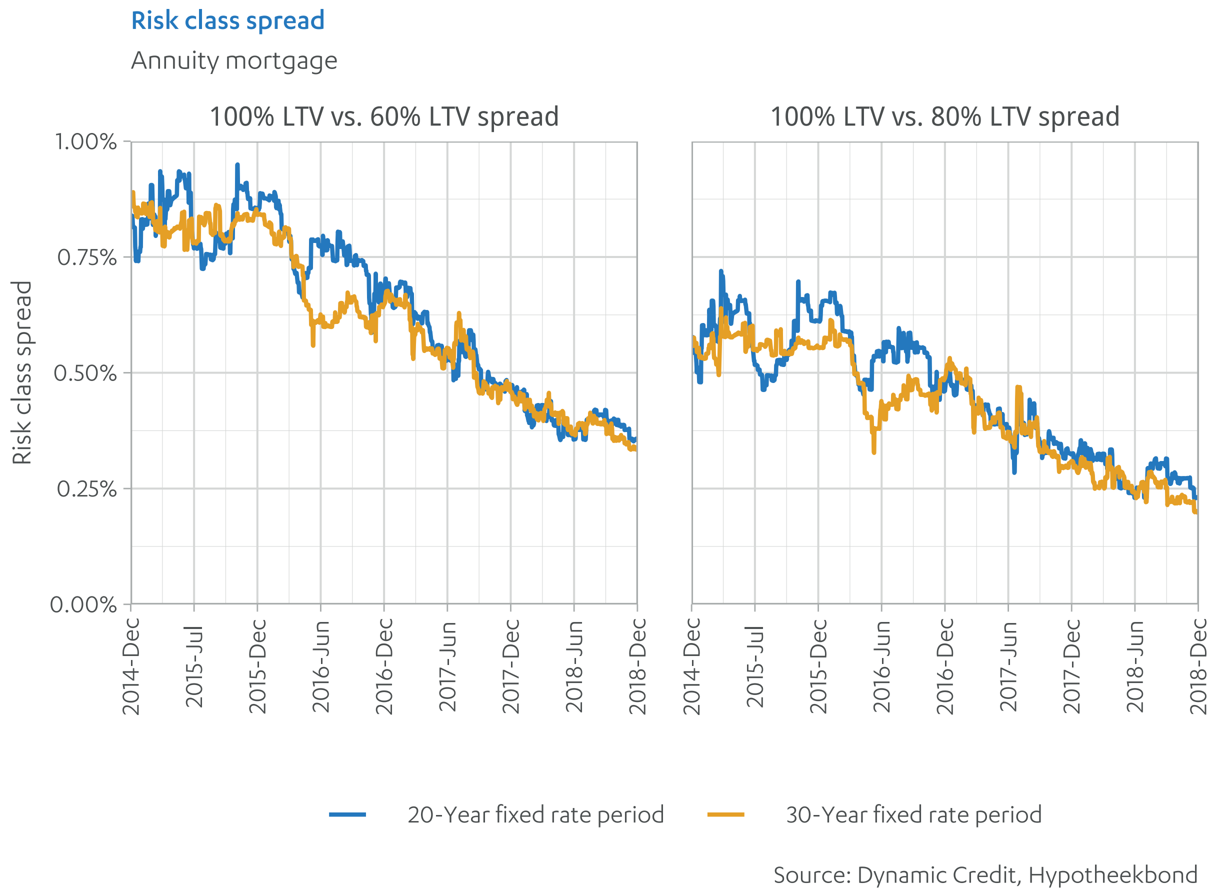


Figure 7: Average top-6 price leader mortgage rates (excluding action rates) over duration matched swap rates. Difference between 100% and 60% LTV (non-NHG) type loans and between 100% and 80% LTV (non-NHG) for 20- and 30- year fixed rate periods.

- The spread-pickup is still attractive relative to historically realized losses -

[1] Source: Fitch Mortgage Market Index 2H17

Dutch RMBS market: Priced RMBS deals

Several new RMBS deals were closed during 2018-Q4

Date	Issuer	Series	Seller	Class	Euro Amount	Life	FXFL	Coupon	DM	Benchmark	M	SP	F	DBR	Retained	Comments
2018-12-11	STRONG B.V	2018	Obvion	A	800.0	6.8	FL		49	3 Mo. Euribor	Aaa	AAA	AAA		N	EUR 800mm; NHG 100%;
				B	33.4	6.8	FL				Aa1	A-	BBB+		Y	
				C	8.4	6.8	FL				Ba1				Y	
2018-11-29	EDML BV	2018-2	Elan	A	307.5	2.8	FL		55	3 Mo. Euribor			AAA	AAA	N	EUR 337mm; WA CLTV 89.3%; WA Seasoning 5m; IO Loans 36.5%; Self-Employed 7.4%;
				B	7.6	2.9	FL		80	3 Mo. Euribor			AAA	AA	N	
				C	6.7	2.9	FL		115	3 Mo. Euribor			A+	A	N	
				D	5.1	2.9	FL		160	3 Mo. Euribor			A	BBB	N	
				E	3.4	2.9	FL		275	3 Mo. Euribor			BBB	BB L	N	
				F	6.7	2.9	FL		475	3 Mo. Euribor					N	
2018-11-23	Dutch MBS BV	XIX	NIBC Bank	A	447.3	3.9	FL		41	3 Mo. Euribor	Aaa		AAA		N	EUR 476mm; WA CLTV 69.5%; WA Seasoning 66m; IO Loans 41.5%; Self-Employed 8.8%;
				B	8.1	5.0	FL		80	3 Mo. Euribor	Aa1		A+		Y	
				C	9.9	5.0	FL		150	3 Mo. Euribor	Aa1		A+		Y	
				D	10.9	5	FL		175	3 Mo. Euribor	A1		A-		Y	
				E	4.7		FL		200	3 Mo. Euribor					Y	
2018-10-31	Saecure	16	Aegon Insurance	A	875.0	4.1	FL		35	3 Mo. Euribor		AAA	AAA		N	EUR 940mm; WA CLTV 80.6%; WA Seasoning 38m;
				B	65.9	5.0	FL								Y	
				C	9.5										Y	
2018-10-18	Lowland Mortgage Backed BV	6	de Volksbank	A1	49.9	5.0	FL		50	1 Mo. Euribor	Aaa		AAA		Y	EUR 2.5bn; WA CLTV 92%; WA Seasoning 48m; 12,097 Obligors; IO Loans 30.3%;
				A2	2,275.1	5.0	FX	1.00%			Aaa		AAA		Y	
				B	62.5	5.0	FX	0.00%			Aa3		AAA		Y	
				C	45.0	5.0	FX	0.00%			A2		AA+		Y	
				D	40.0	5.0	FX	0.00%			Baa1		A+		Y	
				E	27.5	5.0	FX	0.00%					BB+		Y	

Table 2: Priced Dutch RMBS Deals in 2018-Q4. Source: Dynamic Credit, JP Morgan

- Aegon and NIBC returned to the Dutch RMBS market -

ABS comments

Activity in the Dutch RMBS market increased in 2018-Q4 as 5 deals were issued, three more than in the previous quarter. The discount margins were much higher than in previous quarters. The 5 deals brought the 2018 total volume above EUR 30bn with 9.3 bn distributed. See next page for details.

Aegon returned to the RMBS markets for the first time since 2014 with its **Saecure 16 BV** deal. The deal size reached EUR 940 million, with EUR 75.4 million retained. NHG-guaranteed loans comprise 10.4% of the collateral pool. The demand for the senior Class A tranche was healthy, with a subscription ratio above 1.6x and pricing at a spread of 35 bps – at the tight end of the initial price guidance.

NIBC followed in Aegon's footsteps and launched its **Dutch MBS XIX BV** transaction, after 5 years of absence in the Dutch RMBS market. The EUR 475 million deal was met with solid investor demand, with the oversubscription ratio for the senior Class A tranche reaching 1.2x. The Class A notes priced at a spread of 41 bps (versus initial guidance of 40 bps), while EUR 28.7 million of junior notes was retained. The collateral pool had an average CLTV of 69.5%. NHG-guaranteed loans comprise 32.6% of the portfolio, while Interest-Only loans account for 41.5% of the securitized mortgages.

The last deal of the year was **Strong 2018 BV** issued by Obvion. The transaction size was EUR 842million, of which EUR 800 million, the Class A notes, was distributed and priced at a spread of 49 bps. In comparison, the previous deal from Obvion was the EUR 904 million Storm 2018-II BV, which priced in September 2018 with the senior tranche spread at 28 bps.

- Limited issuance of covered bonds in the quarter -

Covered bonds

Covered bonds issuance by Dutch banks in the last quarter of 2018 was relatively muted and amounted to EUR 163 million, including 7 small issuances by Volksbank and 1 small by ING Group.

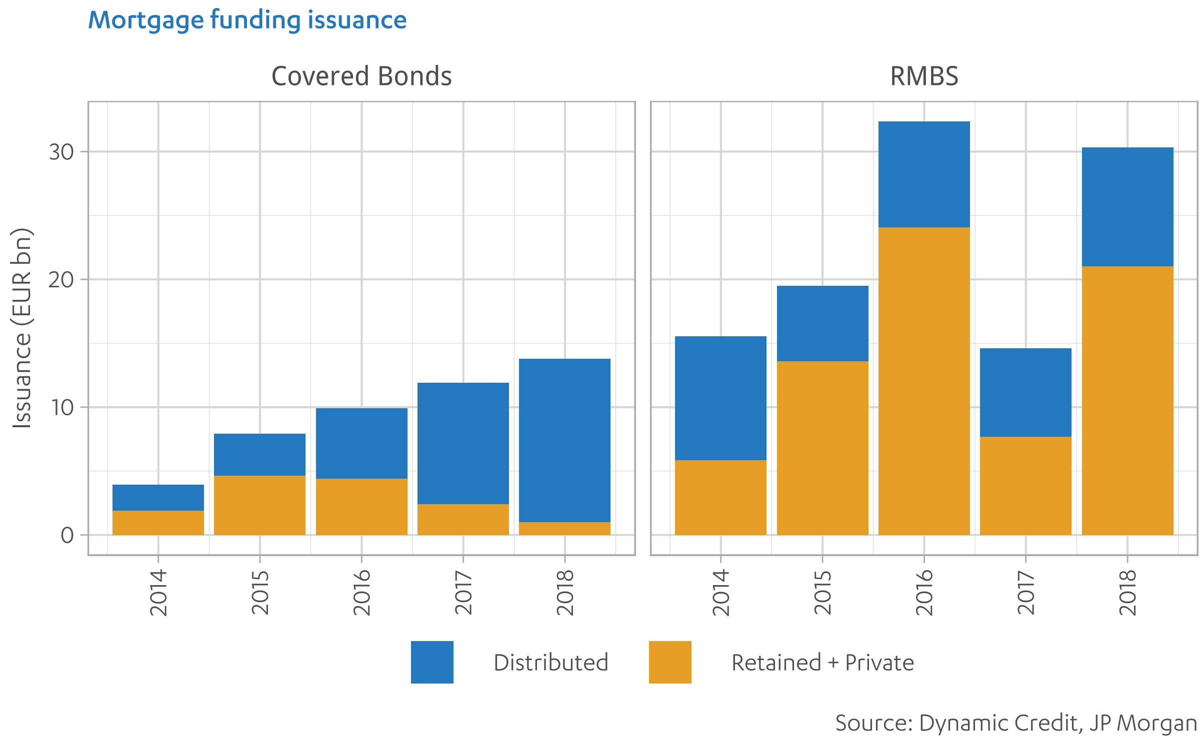
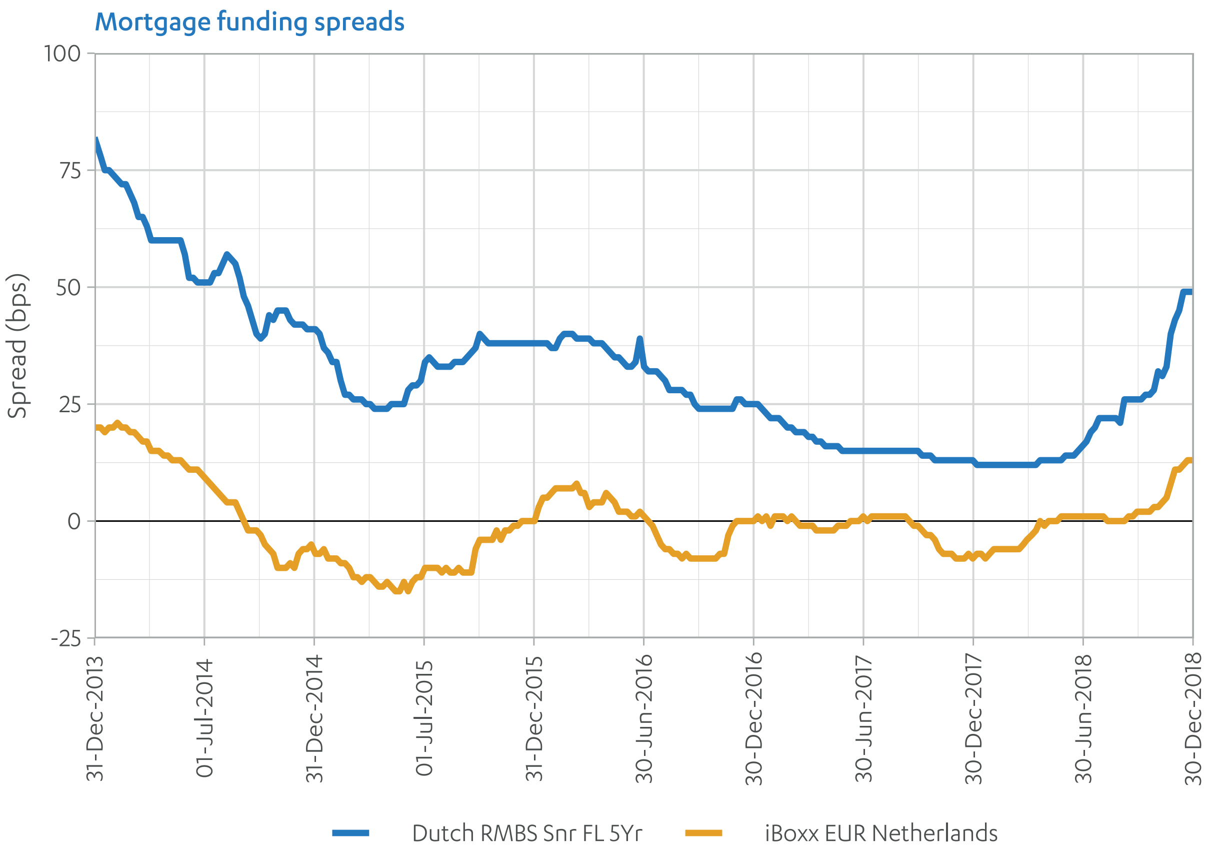


Figure 8: Issuance of Dutch RMBS and covered bonds. As of 2018-Q4.

Mortgage funding spreads

The increased RMBS issuance in 2018-Q4 and the return of long-absent issuers to the securitization market mark a shift between demand for covered bonds and for RMBS. This appears to be the result of the ECB tapering their QE program and decreasing the level of net purchases of covered bonds, using only the reinvestment proceeds to buy covered bonds from the beginning of 2019 onwards. Indeed, as JPM data shows, central bank participation in EUR-benchmark Eurozone Covered Bonds dropped to 23% in 2018H2 from 37% in 2018H1. This, together with market volatility, resulted in an increase in Dutch covered bond spreads to 13 bps – a level unseen since 2014. While the demand for Dutch RMBS remained healthy, the spread on AAAs was not immune to the general turmoil in equity and credit markets, which together with less ECB liquidity contributed to the widening of AAA spreads to 49 bps at the end of the year – the highest level since September 2014 (Figure 9).

- Large increase in funding spreads -



Source: Dynamic Credit, JP Morgan

Figure 9: RMBS spread refers to indicative mid spread (discount margin) for representative generic RMBS bonds. iBoxx EUR Netherlands spread refers to spread versus mid swap rates. The data is as of 2018-Q4

Market entry/exit

No new players entered the Dutch mortgage market during 2018-Q4.

House prices and property sales

The CBS house price index increased 1.5% over the fourth quarter of 2018 and 9.0% YoY. This compares to house price increases of 2.7% QoQ and 9.2% YoY in 2018-Q3. Surprisingly, housing prices even decreased 0.6% in December, the first decrease in years. Even though monthly changes can fluctuate, the last time house prices decreased was over 2 years ago in October 2016.

Close to 57,000 properties were sold during 2018-Q4, only a slight decrease of 0.7% QoQ but a significant 14.6% YoY decrease (see Figure 11 for regional differences). All quarters in 2018 had a YoY decrease in the number of sold properties (Figure 10).

- Dutch house prices decreased in December -

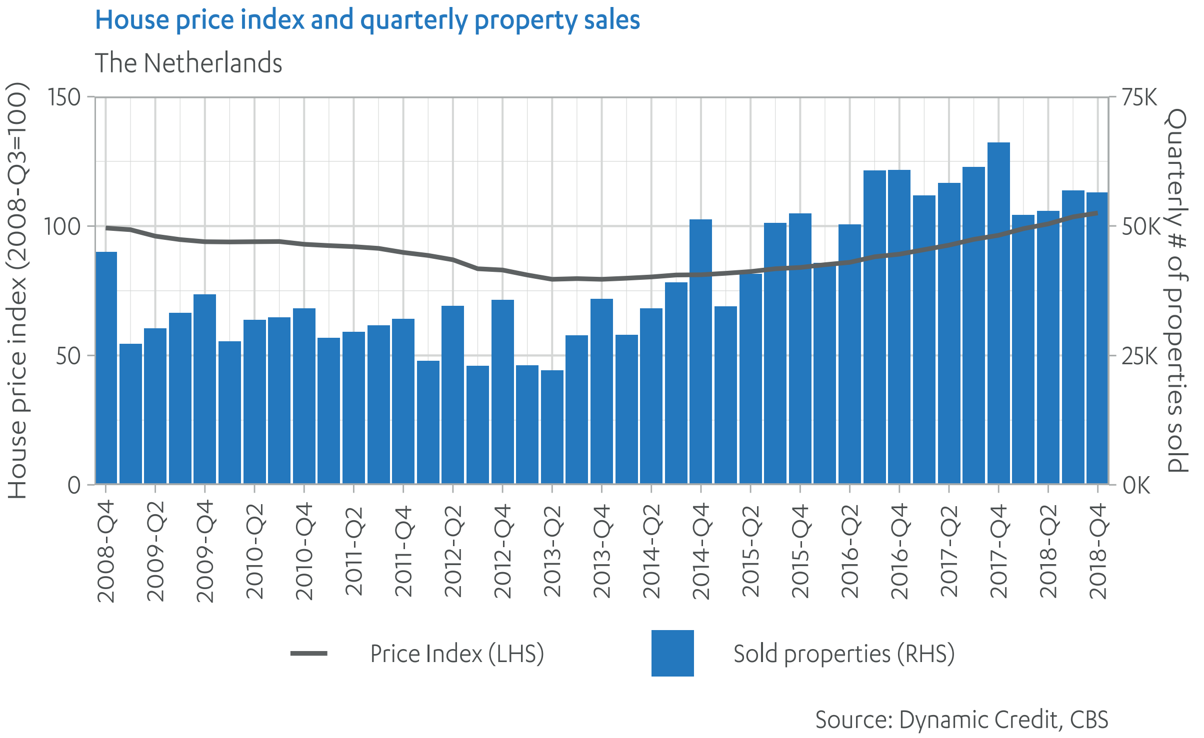


Figure 10: House Price Index of the Netherlands (2008-Q3=100) and quarterly property sales. The data ranges from 2008-Q4 up to and including 2018-Q4.

Regional differences

During 2018-Q4, price divergence between the big cities and the rest of the country stopped as Rotterdam and Amsterdam had lower QoQ house price increases than the national average. Most noteworthy, Rotterdam prices only increased 0.2% QoQ in 2018-Q4 (4.8% QoQ in 2018-Q3). (Figure 11). Prices in 's-Gravenhage continued to increase steeply as they went up 2.7% QoQ. On a provincial level, Utrecht (0.6% QoQ) and Groningen (0.8% QoQ) grew the slowest while prices in Flevoland (2.9% QoQ) and Friesland (2.7% QoQ) are increasing the fastest (Table 3).

- Rotterdam and Amsterdam prices increased less than the national average in the quarter -

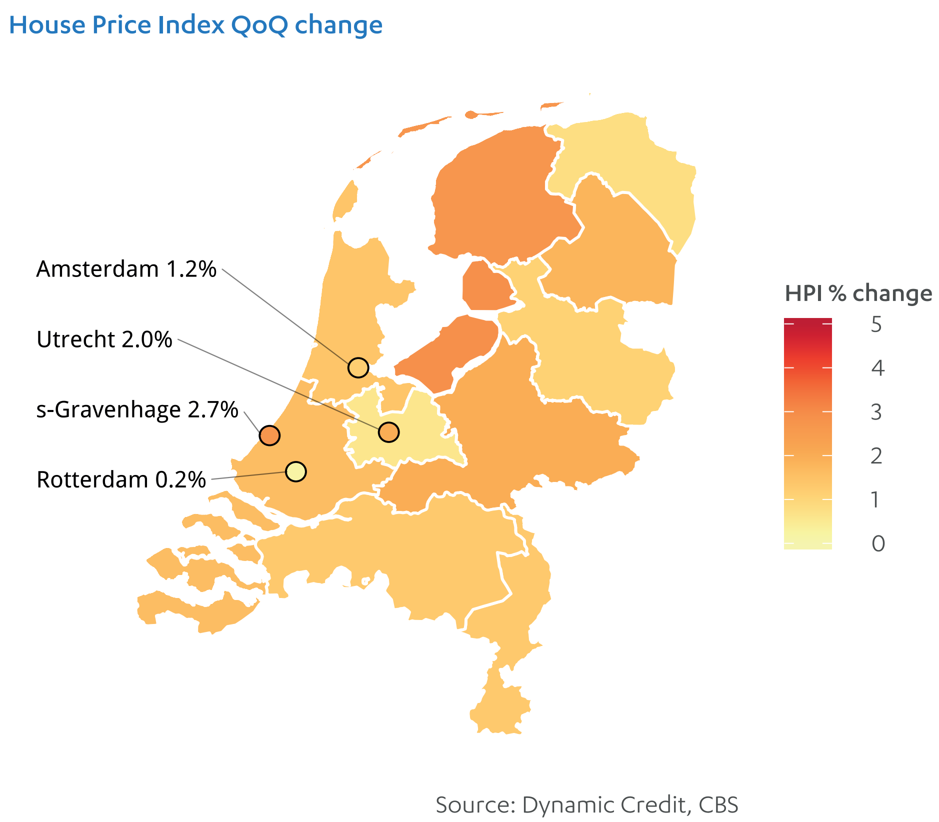


Figure 11: HPI changes in Dutch provinces and major municipalities in 2018-Q4.

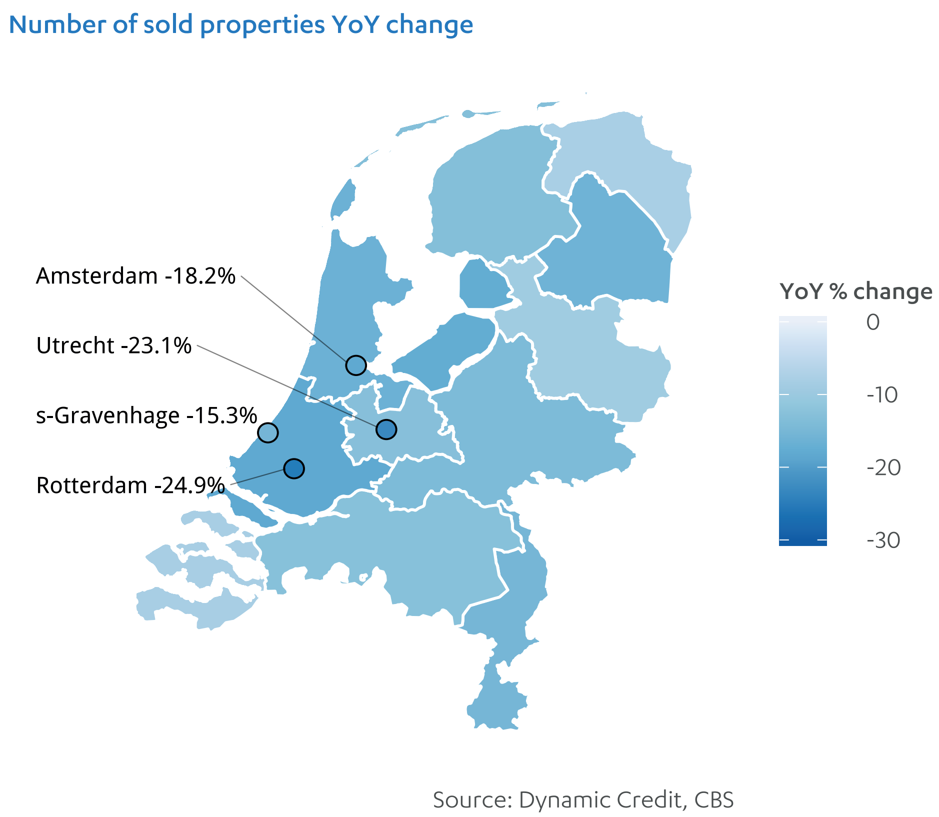


Figure 12: Sold properties YoY changes in the Netherlands as of 2018-Q4.

Area	Type	HPI (2015=100)	QoQ Price %	YoY Price %	# Sold in quarter	QoQ Sold %	YoY Sold %
The Netherlands	Country	126.7	1.5	9.0	56,535	-0.7	-14.6
Zuid-Holland	Province	130.0	1.6	10.3	11,506	-3.7	-18.3
Flevoland	Province	131.7	2.9	11.3	1,473	0.1	-17.5
Noord-Holland	Province	137.0	1.4	11.0	8,765	-5.1	-16.4
Drenthe	Province	118.3	1.8	7.5	1,834	-1.6	-16.0
Limburg	Province	120.6	1.3	8.2	3,611	3.8	-15.2
Gelderland	Province	123.1	2.0	8.2	6,712	1.7	-14.2
Friesland	Province	122.3	2.7	8.7	2,238	0.7	-13.3
Utrecht	Province	129.0	0.6	7.6	4,331	-2.5	-12.8
Noord-Brabant	Province	121.4	1.3	7.6	8,735	2.8	-12.7
Overijssel	Province	121.1	1.1	7.5	3,894	5.4	-9.3
Zeeland	Province	113.7	1.6	5.6	1,590	2.3	-8.1
Groningen	Province	121.1	0.8	6.9	1,846	-3.0	-7.9
Rotterdam	Municipality	143.3	0.2	13.0	1,649	-15.0	-24.9
Utrecht	Municipality	141.5	2.0	10.7	1,080	-19.3	-23.1
Amsterdam	Municipality	151.2	1.2	12.5	2,325	-9.6	-18.2
's-Gravenhage	Municipality	141.2	2.7	12.2	1,753	-4.8	-15.3

Table 3: House prices and number of property sales changes in Dutch provinces and major municipalities 2018-Q4. Source: CBS.

Steeper price increases for new construction

CBS publishes price increases for new construction with one quarter delay. The 2018-Q3 numbers show that the price level for new construction homes had increasesd 17% YoY, significantly more than existing homes. Rabobank has previously argued that this might be because a larger share of newly build is no longer sold via a lottery but instead to the highest bidder.

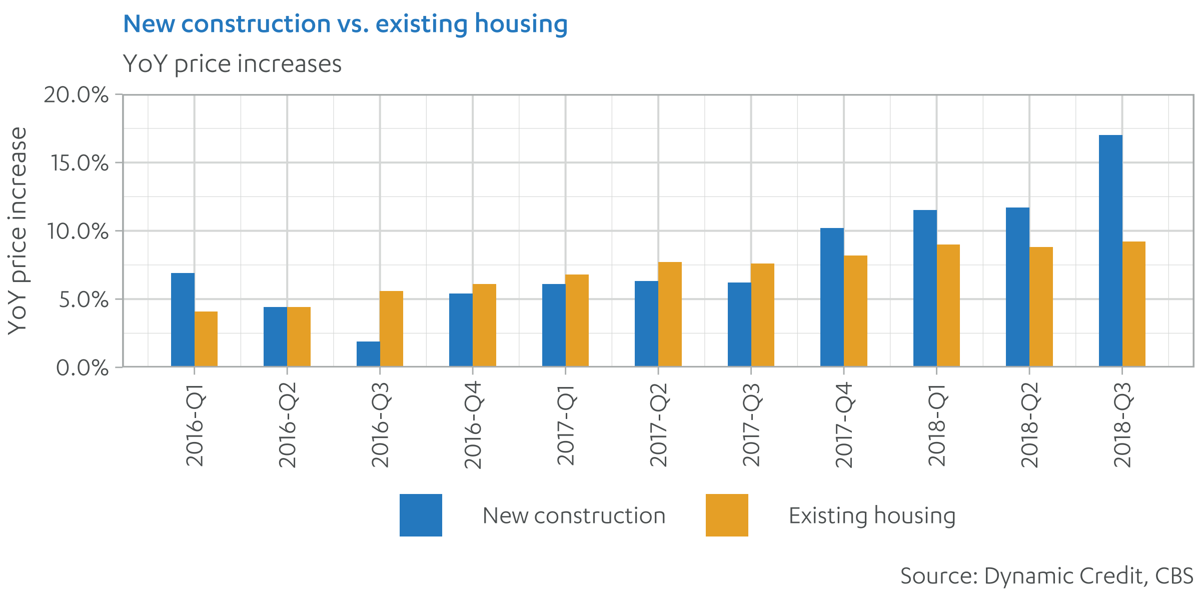


Figure 13: New construction vs existing construction.

Supply and demand developments

The Dutch Association of Real Estate Agents ("NVM") uses a tightness indicator they refer to as the "Krapte Indicator". This indicator divides the supply of houses by the number of sales to indicate the "tightness" or "krapte" of the housing market. As the outcome of this indicator is not always intuitive, we analyze the supply and sales volume separately (Figure 14 below),in a similar way as done by Rabobank[1]:

- The average supply, indicated by the average percentage of owner occupied properties for sale during a certain year, continued to decrease. As a result of a strong recovery of the housing market during the past years, potential homebuyers in 2018 could only choose from around 1.1% of the housing stock in Noord-Holland, compared to around 5.5% in 2012. The 1.1% for Noord-Holland is significantly lower than the national average of 1.6% (was 1.7% when we did the same analysis after 2018-Q2) .
- Annual sales, indicated by the percentage of owner occupied properties sold in a certain year, have been decreasing in 2018. A record high 5.6% of the housing stock nationally was sold in 2017, but only 4.9% (annualized) was sold during the first three quarters of 2018 (5.1% annualized after 2018-Q2). This tendency is clear in all Dutch provinces. At these sales volumes, an owner-occupied property is sold on average every 20-21 years compared to every 28-30 years in 2012.

- Turning point reached in 2018 as sales are decreasing -

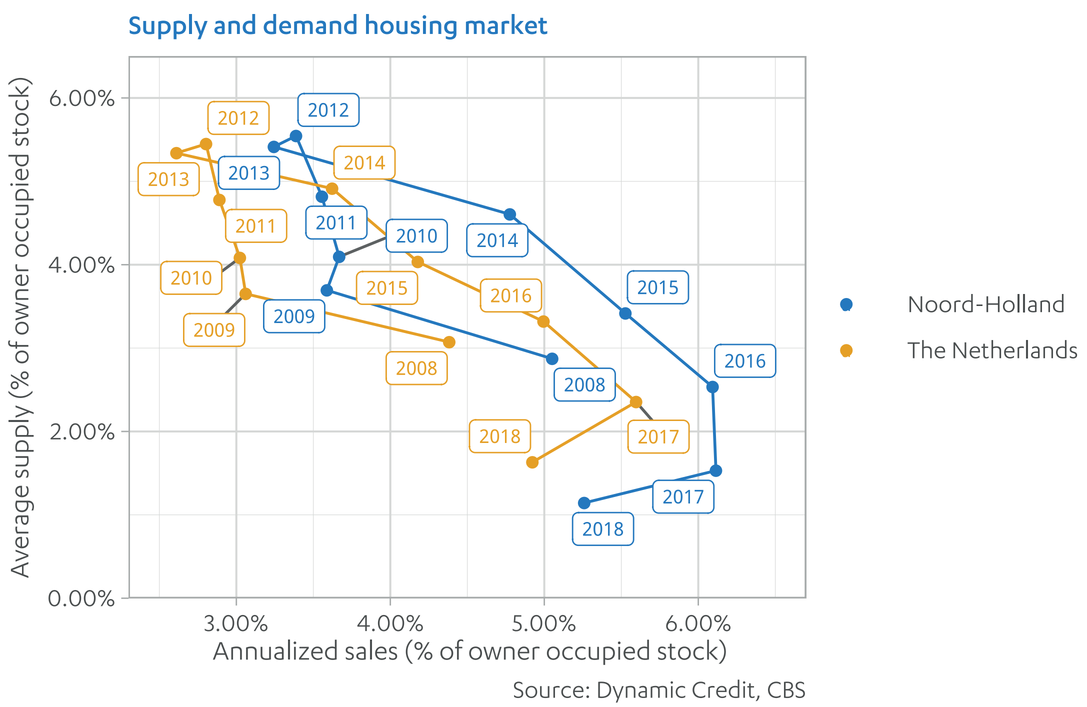


Figure 14: Supply and demand analysis. Supply data for 2018 is up to 2018-Q4 and sales data for the first three quarters has been annualized.

[1] Rabobank - Krapte op de huizenmarkt in beeld: Randstad losgeslagen van de rest van het land

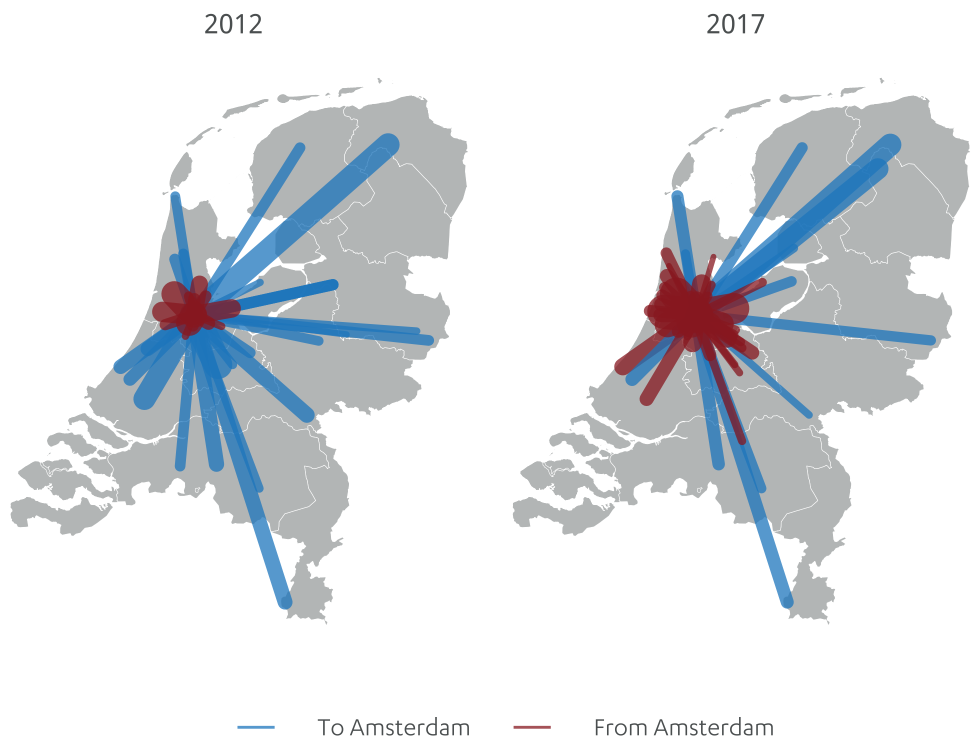
Migration within the Netherlands

We have taken a look at net migration data from Amsterdam and filtered for municipalities with absolute net flows of fewer than 50 people in 2017 and 2012 (Figure 15). It can be seen that people are moving to Amsterdam from many different parts of the country (largely student cities, but also from Noordenveld where an asylum seeker's center was closed). A lot of the people who end up leaving the 4 main municipalities end up moving to nearby municipalities within the Randstad. Cities such as Almere, Amstelveen, Haarlem, Lansingerland, Nieuwegein, Westland, and Zaanstad had an impressive net inflow of people from the main cities in 2017. Data from CBS shows that a lot of people leave the big cities after having their first child (Figure 16). This trend is most obvious in Amsterdam where 40% of the households who had their first child in 2012 left within 4 years. Figure 17 shows that the proportion of households with children is much higher outside of the main cities.

- People could, and did, move away from the main cities in 2017, especially those who had children -

Net migration flows

To/from Amsterdam



Source: Dynamic Credit, CBS

Figure 15: Net migration in 2012 and 2017 between Amsterdam and other municipalities in the Netherlands

Comparing 2017 to 2012, it is important to recall that a lot of mortgages were underwater in 2012, which made it hard for people to move. The situation was completely different in 2017 which enabled a lot of people to leave.

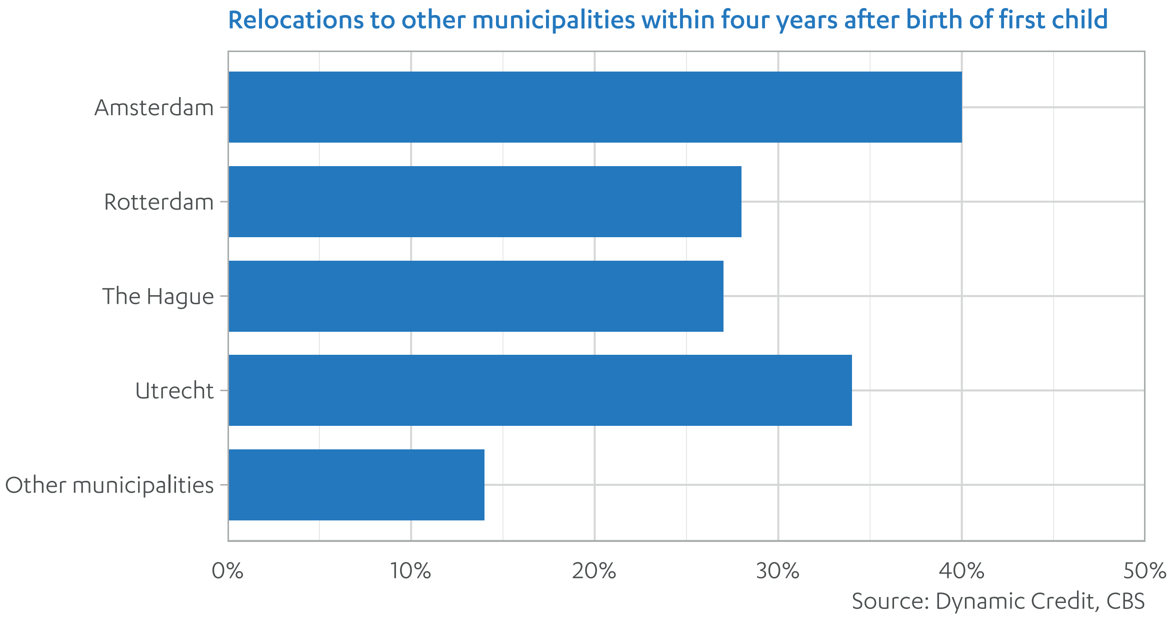


Figure 16: % of couples with first child born in 2012.

- Amsterdam grew in the period 2012-2016 due to an influx of foreigners. Net migration within the Netherlands was negative -

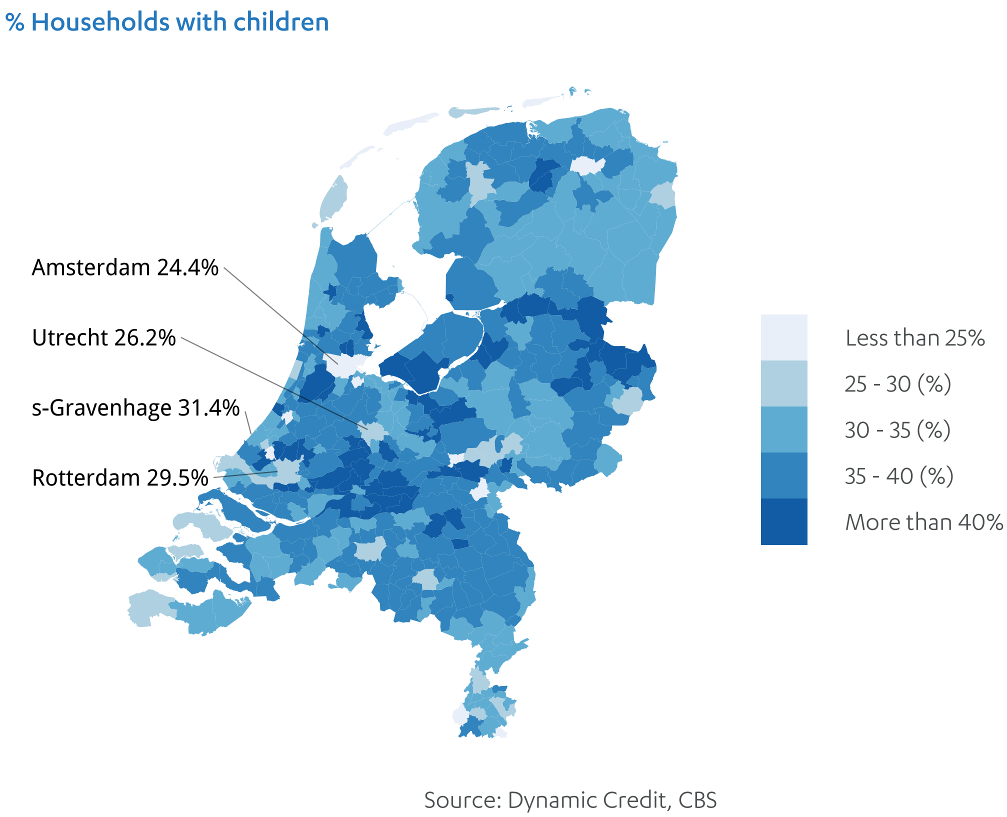


Figure 17: Private households in the Netherlands with one or more children. As of 1 January 2017.

3. Relevant news items

DNB Economic Outlook

On 13 December 2018, the Dutch National Bank published its semi-annual Economic Developments and Outlook report. The most interesting trends are discussed below:

More permanent contracts. 141,000 more people were on permanent contracts at the end of 2018-Q3 than at the beginning of the year. This compares to an increase of 22,000 for employees on flexible contracts. The development meant that the proportion of people on a permanent contract increased from 72% in 2017 to 73% in 2018. It should be noted that the number is still significantly lower than pre-crisis levels of 80% in 2008. The DNB argue that the increase in 2018 is attributable to increasingly tight labor market conditions.

- The proportion of people with permanent contracts has increased for the first time in 10 years -

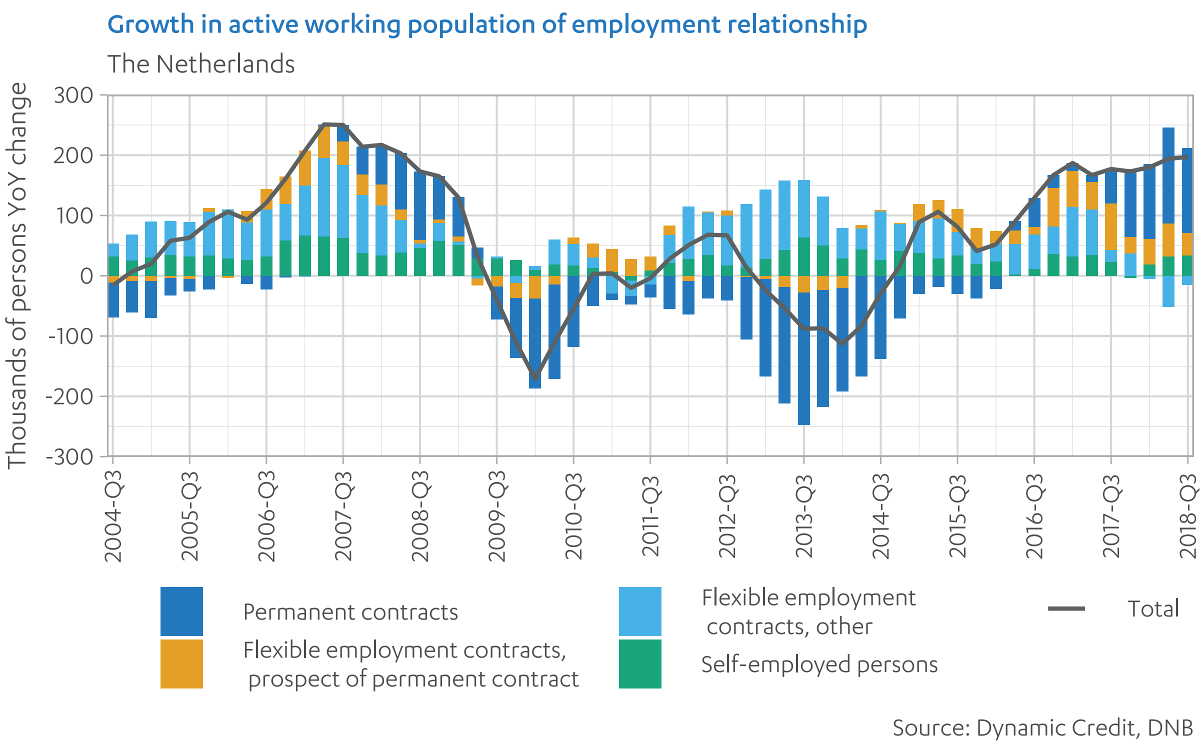


Figure 18: Contract type developments.

Accelerating wage growth in the private sector. Overall compensation per employee can be decomposed into employers' social contributions, wage drift, and negotiated wages. The 2018 data for growth in contract wages is not available as of the moment of writing this report, but it is expected to come in at 2.1%. DNB expects contract wage growth to accelerate in the coming years and reach 2.6% and 3.0% in 2019 and 2020 respectively. Furthermore, wage drift (overtime, bonuses, promotion, etc.) is expected to turn positive again in 2019 for the first time in 5 years. DNB argue that the tight labor market will cause the employers' to look more towards experienced and thus more experienced labor. Overall, the increase in total compensation per employee is expected to accelerate from 2.3% in 2018 to 3.8% in 2020.

- Wage growth expected to increase in 2019 and 2020 -

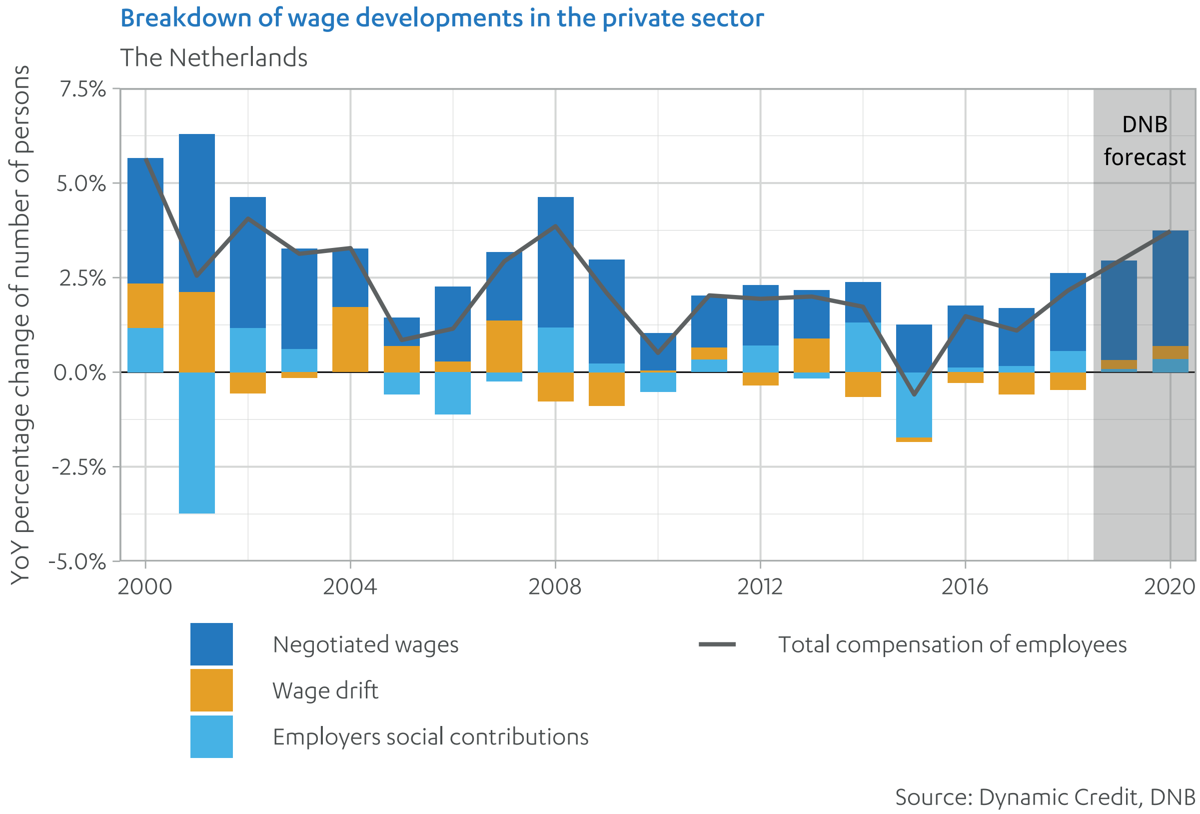


Figure 19: Breakdown of private sector wage developments in the Netherlands. Data for 2019 and 2020 is based on a forecast by the DNB.

House price increases to slow down. The DNB expects that house prices will increase by 5.5% in 2019 and 2.8% in 2020. They argue that the decline in mortgage interest rates has stalled. In their analysis, they also mention that recent price increases are partly due to increasing obstacles for newbuilding due to a shortage of labor and materials. Housing investment is expected to grow at a sligtly slower pace in the coming years.

- House prices expected to increase by 5.5% in 2019 -

Monetary policy

On 13 December 2018, the Governing Council of the European Central Bank met. Main takeaways:

- The Governing Council decided to keep the interest rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility unchanged at 0.00%, 0.25% and -0.40% respectively;
- The rates are expected to remain at the current level at least through the summer of 2019;
- Draghi mentioned that "the balance of risk is moving to the downside" as the growth estimate for 2019 was downward adjusted to 1.7% from 1.8% "owing to the persistence of uncertainties related to geopolitical factors, the threat of protectionism, vulnerabilities in emerging markets and financial market volatility";
- The inflation estimate for 2019 was lowered from 1.7% to 1.6%;
- Despite growing concerns, the ECB confirmeded that QE would stop at the end of 2018;
- The ECB extended its window for reinvesting bonds held under its QE programme, giving itself 1 year instead of 3 months to make purchases. The move was taken to give more flexibility as maturing volume can fluctuate. Redemptions will be reinvested in the jurisdiction in which principal repayments are made, and "any adjustment to the portfolio allocation across jurisdictions will be gradual and will be calibrated to safeguard orderly market conditions."

New Year's article by Maarten Camps calls for increased stability in the Dutch housing market

Maarten Camps, the highest official at the Ministry of Economic Affairs in the Netherlands published a New Year's article in the economic magazine ESB.

In the article, he argued that procyclicality in the Dutch housing market is bad for the economy in the long run. Measures are needed to reduce the difference between the peak and through levels.

- Large fluctuations in the housing market reduce Dutch prosperity -

He gives concrete proposals aimed at increasing stability in the housing market:

- The current accelerated **phasing out of the mortgage interest deduction** (see our last quarterly report with details about steps taken since the Lehmann Brothers collapse) is a step in the right direction, but a further reduction is a good idea.
- A **building fund** should be put in place for housing associations such that they can continue to build houses, also in bad economic times. This would partly compensate for the reduction in construction by private developers during a downturn. He argues that the fund could be financed via the landlord levy.
- Set aside **land profits.** Municipalities have an incentive to postpone land sales during an economic downturn. This is problematic as land sales can limit decline in construction during a market downturn. In order to prevent land from being sold only at the peak of the market, setting aside part of the land profit may be a solution. These profits can then be used to compensate for the losses in a low economic climate.
- More **steering at a national level** is needed as there are municipalities in which the interests of current homeowners prevail those of prospective homeowners.

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CONTINUE TO THE APPENDIX ⟶

Appendix

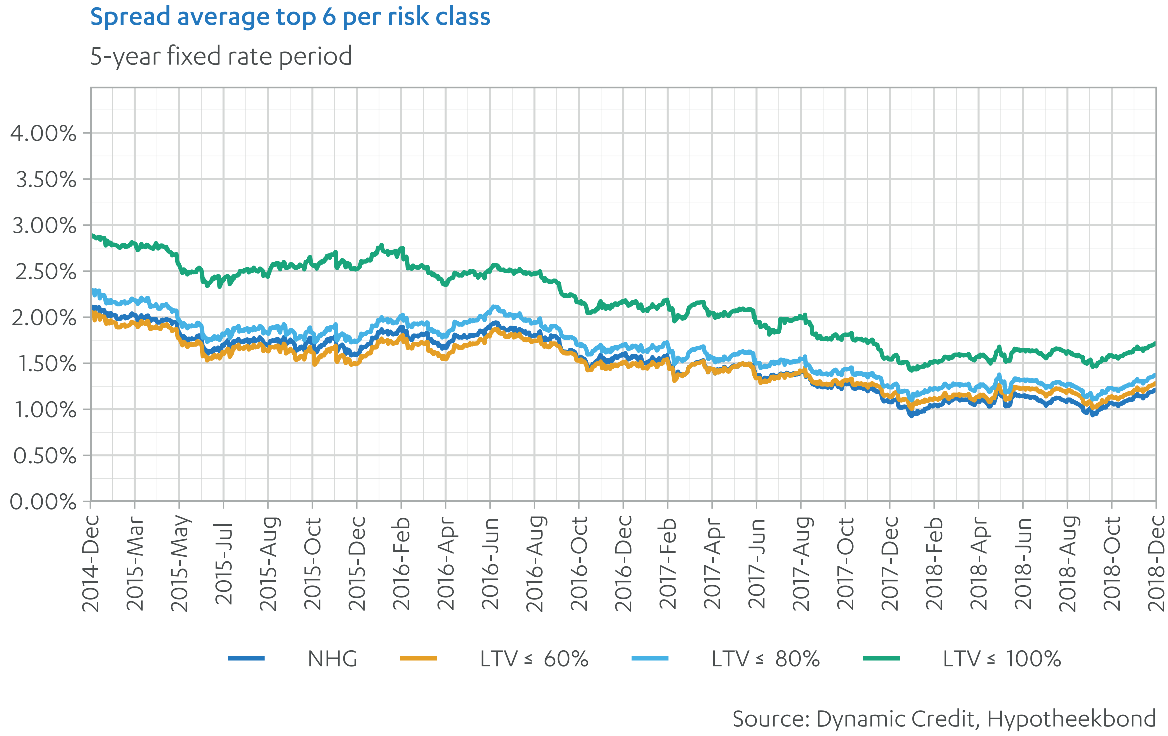


Figure A1: Spread of the average top-6 price leader mortgage rates (excluding action rates) for mortgage loans with a 5-year fixed rate period for four risk classes.

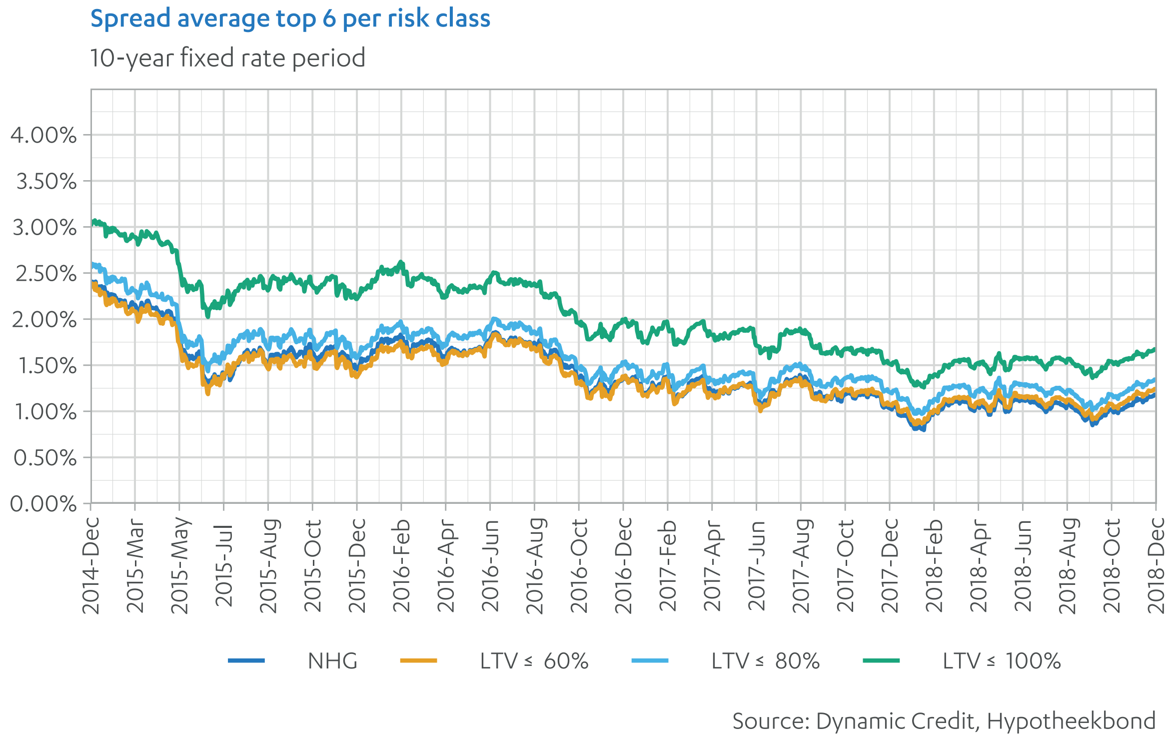
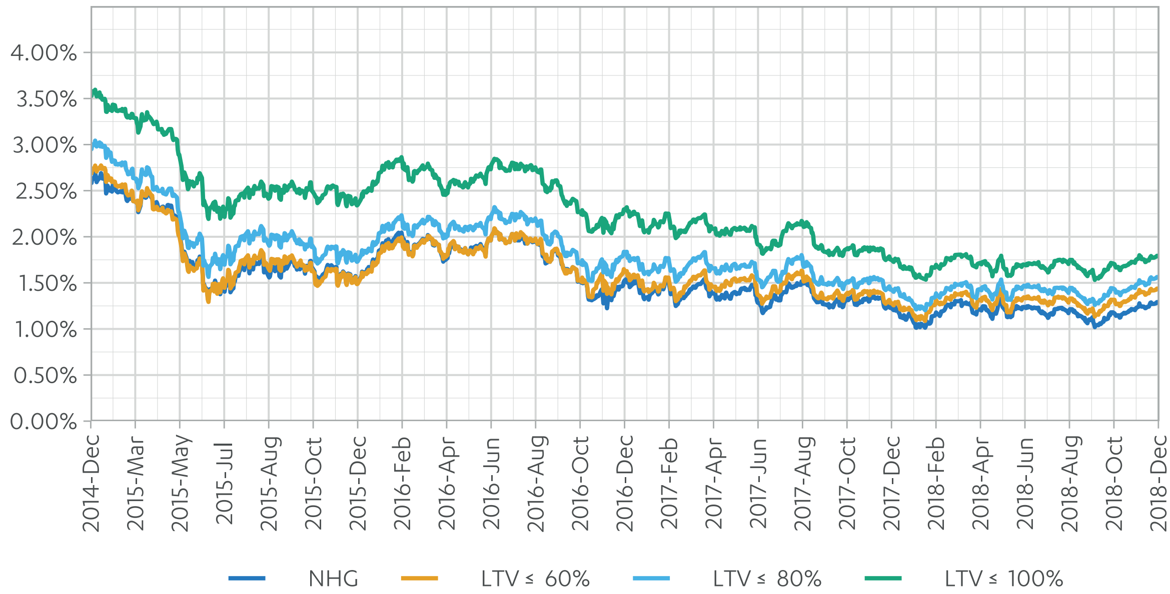


Figure A2: Spread of the average top-6 price leader mortgage rates (excluding action rates) for mortgage loans with a 10-year fixed rate period for four risk classes.

Spread average top 6 per risk class

20-year fixed rate period

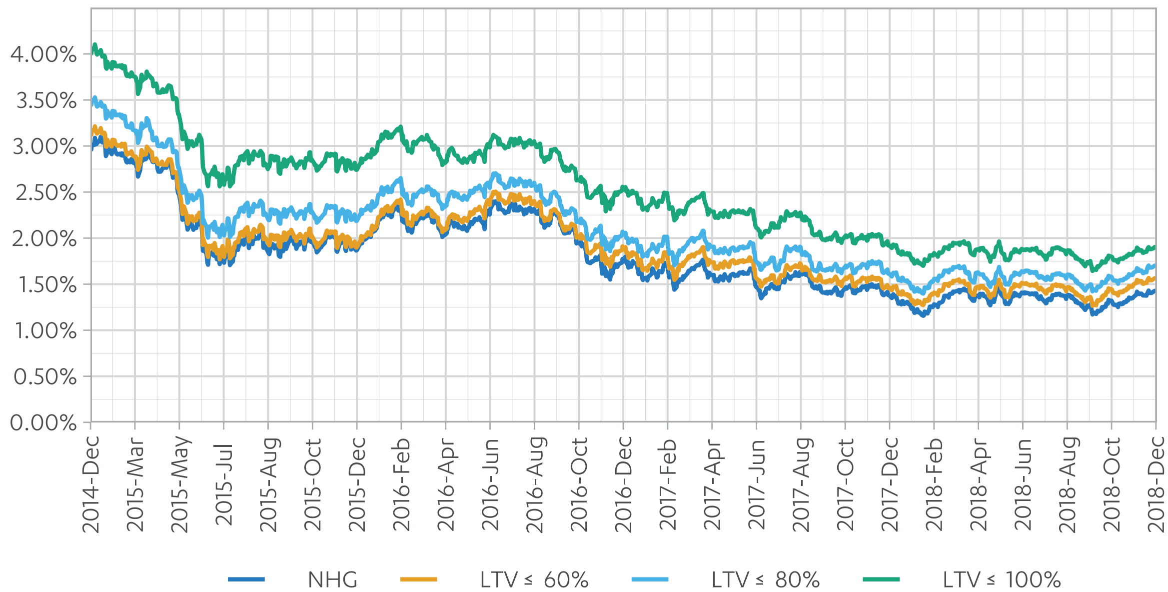


Source: Dynamic Credit, Hypotheekbond

Figure A3: Spread of the average top-6 price leader mortgage rates (excluding action rates) for mortgage loans with a 20-year fixed rate period for four risk classes.

Spread average top 6 per risk class

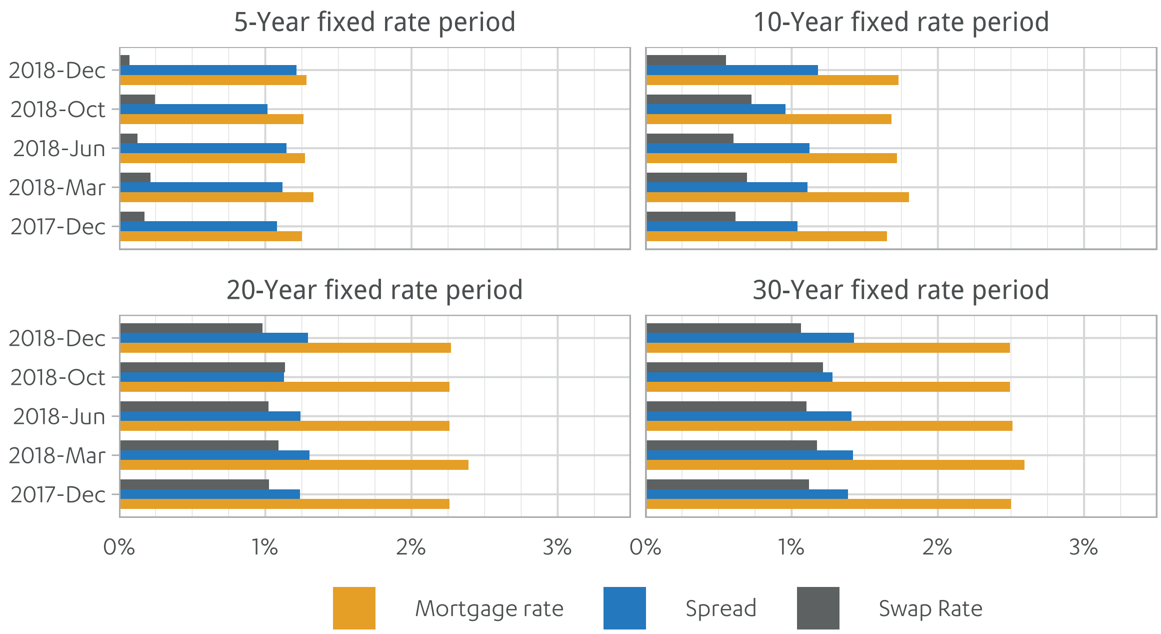
30-year fixed rate period



Source: Dynamic Credit, Hypotheekbond

Figure A4: Spread of the average top-6 price leader mortgage rates (excluding action rates) for mortgage loans with a 30-year fixed rate period for four risk classes.

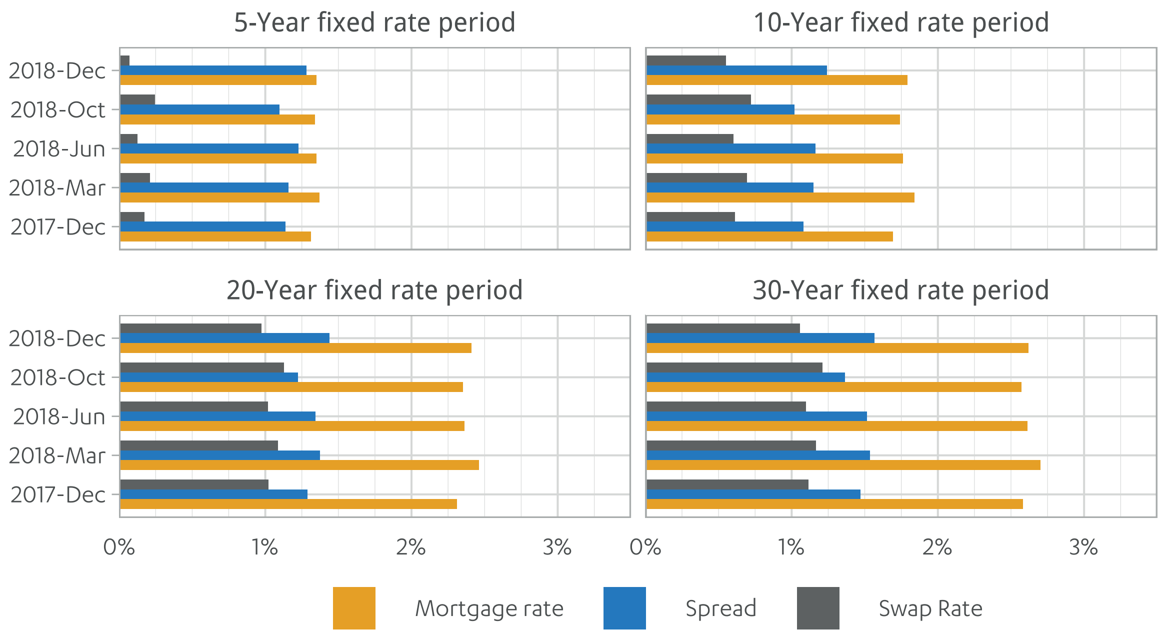
Mortgage rate decomposition for NHG mortgage loans



Source: Dynamic Credit, Hypotheekbond

Figure A5: Mortgage rate decomposition of the average top-6 price leaders (excluding action rates) for NHG mortgage loans with different fixed rate periods. End of month data has been used.

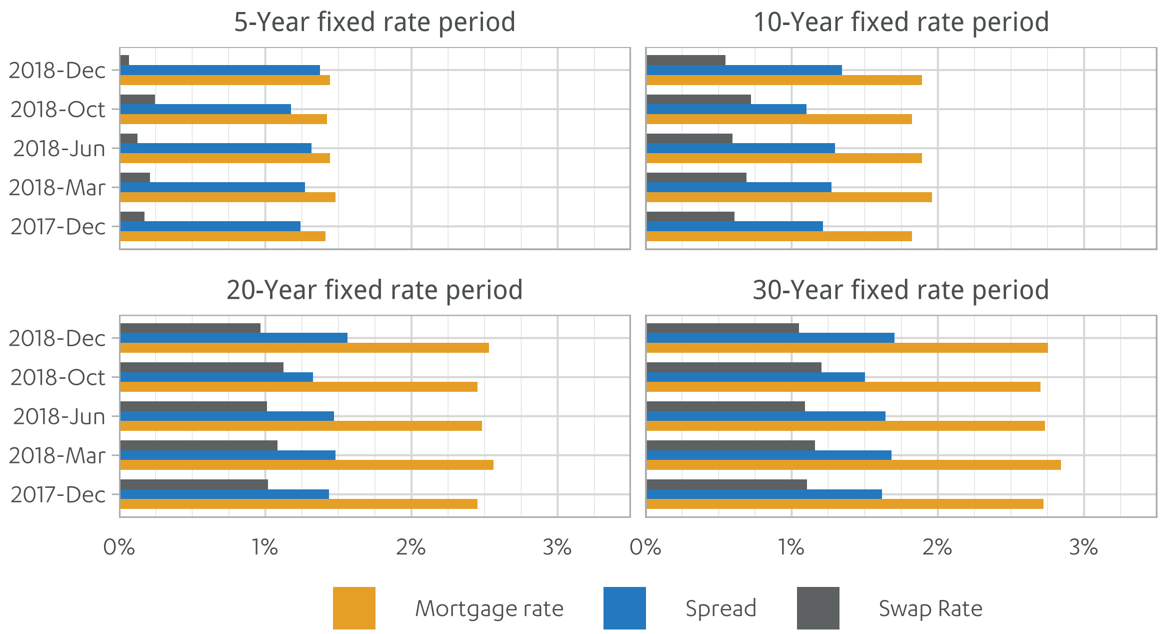
Mortgage rate decomposition for 60% LTV mortgage loans



Source: Dynamic Credit, Hypotheekbond

Figure A6: Mortgage rate decomposition of the average top-6 price leaders (excluding action rates) for 60% LTV mortgage loans with different fixed rate periods. End of month data has been used.

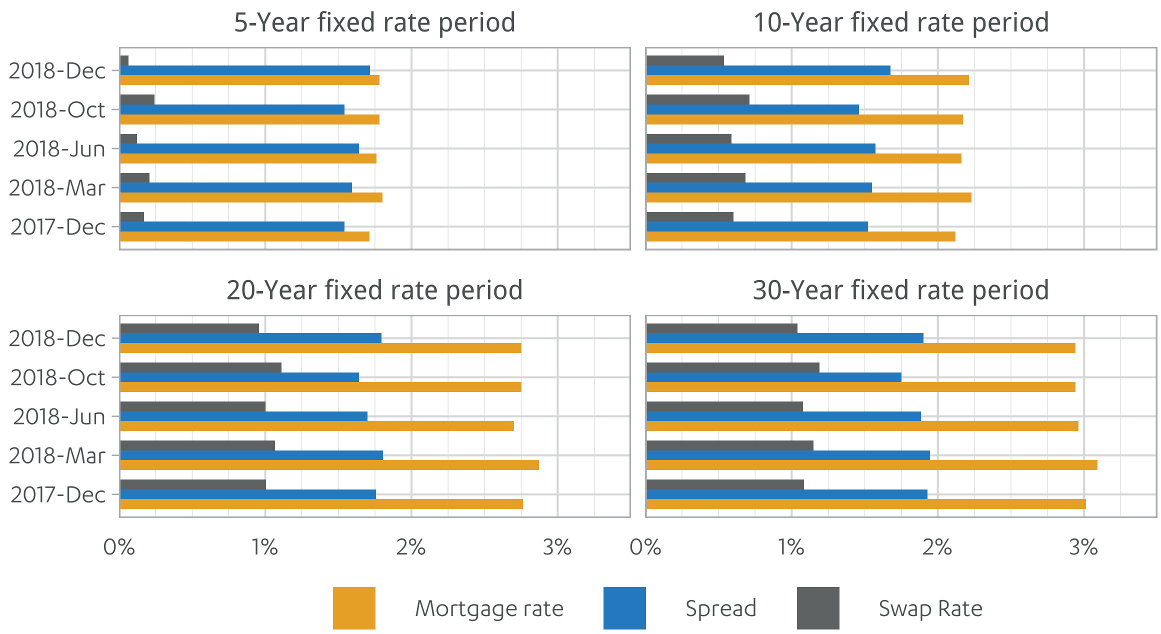
Mortgage rate decomposition for 80% LTV mortgage loans



Source: Dynamic Credit, Hypotheekbond

Figure A7: Mortgage rate decomposition of the average top-6 price leaders (excluding action rates) for 80% LTV mortgage loans with different fixed rate periods. End of month data has been used.

Mortgage rate decomposition for 100% LTV mortgage loans



Source: Dynamic Credit, Hypotheekbond

Figure A8: Mortgage rate decomposition of the average top-6 price leaders (excluding action rates) for 100% LTV mortgage loans with different fixed rate periods. End of month data has been used.

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