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# Housing Market Monitor

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## Housing market still dodging the economic bullet

- House prices and purchases impervious to the weak economy so far
- Low mortgage rates are the main factor fuelling the housing market
- But the interest rate effect is waning and a worsening labour market will also take its toll
- The housing market is weakening less than previously foreseen: forecasts raised

We have substantially raised our forecasts for the housing market. Previously, we anticipated prices stabilising in 2021. We are now counting on a 5% increase. This major upward revision is, firstly, related to the carry-over effect. The strong appreciation in the second half of 2020 feeds through into the average increase for 2021. If prices stabilise at the current level, the average rise will already work out at 3.5%. In the year thereafter, the carry-over effect will drop out of the figures, causing a further weakening of the upward momentum. For now, we are counting on a 1% price increase in 2022.

The second reason for the increased forecast is that the future is starting to look more certain. Now that the vaccine roll-out is gathering pace in more and more countries, a recovery of economic activity is coming into sight. That is vital in order to limit the economic damage from bankruptcies and higher long-term unemployment. It is crucial for the housing market that the prospects for the labour market remain intact, as income levels directly determine the size of mortgages and, hence, property values.

Though the arrival of vaccines is reassuring, the number of unemployed will inevitably climb in 2021. Employees will be laid off when the government's support schemes are wound down. And the same will happen when companies start to implement their announced reorganisation plans. The expected increase in unemployment will temper the housing market. Initially via fewer transactions, later via lower price increases. After a 7.5% increase in transactions in 2020, our forecast sees house purchases falling by 10% in 2021 and 5% in 2022.

Mortgage rates constitute the most important pillar under the housing market. Major central bank interventions are keeping interest rates on government loans (a key yardstick for mortgage rates) low. Central banks are expected to continue their asset purchases to support the economy. The outlook for mortgage rates and, by extension, housing costs remains positive therefore. However, once mortgage rates stabilise, the amount that buyers can borrow will stop growing. This, in turn, will cause the favourable effect of low mortgage rates on the housing market to gradually diminish.

### Housing market shrugs off economic storm

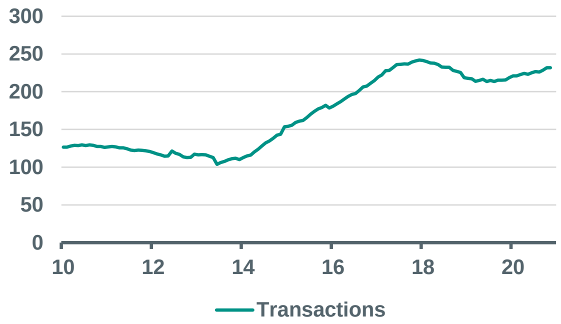
Though the renewed lockdown in the Netherlands is constraining economic activity and casting a cloud over the labour market, the housing market continues to power ahead. In the eleven months to the end of November, 209,000 pre-owned houses were purchased, 13,000 more than in the same period of 2019. Including December (traditionally a month with a high transaction volume), the total number will approach the record set in 2017, when 242,000 pre-owned houses changed hands.

The chance of this transaction record in 2017 being equalled is slim, however. The reason is that first-time buyers aged 18 to 35 will postpone their purchase until 1 January when the transfer tax will be reduced from 2% to zero for this group. From 1 April this zero rate will only apply to homes up to EUR 400,000, a price threshold which will be indexed in the years thereafter. In the run-up to 1 April there will probably be a short-lived boom in house purchases above EUR 400,000 by first-time buyers.

Whilst first-time buyers will have held back in December, investors will have brought forward their purchases - because this group will be confronted with an increase in transfer tax from 2% to 8% from 1 January. This change, however, will have a limited impact on the transaction statistics as only private purchases are recorded in the Dutch Land Registry. In this sense, the transaction series at best provides an indication of the total number of house purchases.

**Number of transactions, close to record of 2017**

Number of house purchases in the past 12 months (thousands)




Source: Statistics Netherlands (CBS)/Dutch Land Registry

**Housing supply shrinks further**

Number of properties for sale (thousands)


Source: huizenzoeker.nl

The continuing intensity of transaction activity is remarkable, not just because of the current economic uncertainty but also because of the limited supply. According to home search website *huizenzoeker.nl*, there are now only 45,000 properties for sale, 11,000 less than a year ago. Normally, constrained supply puts a brake on the number of transactions. However, with demand for dwellings remaining as strong as ever, the selling time is short and the transaction volume buoyant. According to the Dutch Association of Real Estate Brokers (NVM), houses sold in Q3 were on the market for an average of 30 days.

Regarding the selling time, there is no longer much difference between the various house types. Previously, apartments were popular. Now, terraced housing, semi-detached properties and apartments all sell practically just as quickly. Only detached homes take a little longer to find a buyer. That is understandable, as these tend to be specific properties with their own unique character. For this reason, it can take a bit longer for a prospective buyer to come forward and strike a deal with the seller.

The transaction price for detached housing sometimes also comes about in a different way. Some selling agents put this type of - typically more expensive - property on the market for a [high asking price] to test what interested parties may be willing to pay. The resulting information can be useful for negotiating the highest possible price. In the other segments, by contrast, homes are often offered for a low initial asking price in order to attract potential buyers. The greater the interest, the greater the chance of a keen candidate putting in a high offer to outbid the other contenders.

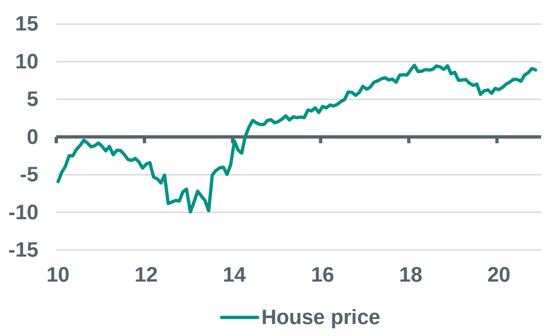
This difference in selling tactics partly explains why the gap between the asking price and actual transaction price is bigger with detached properties than with other house types. According to NVM data, overbidding is less frequent with detached housing, whereas offers at or over the asking price is now more or less standard practice in the market as a whole. More than half of the properties are sold above the asking price. On average, the selling price is now almost 2% above the asking price. Clearly, this is a seller's, and not a buyer's, market.

**Price increases continue**

The short selling time and regular overbidding are tell-tale signs of an heated market. The price momentum confirms that picture. In November the price index of pre-owned housing was almost 9% higher than a year earlier. Since November 2019 the average purchase sum has risen by EUR 32,000 to EUR 344.000. Current homeowners looking to move up the property ladder are benefiting from the rising prices. The larger amount of home equity gives them more financial clout to place a winning bid. In this sense, price increases can be self-reinforcing.

**Price appreciation accelerating since early 2020**

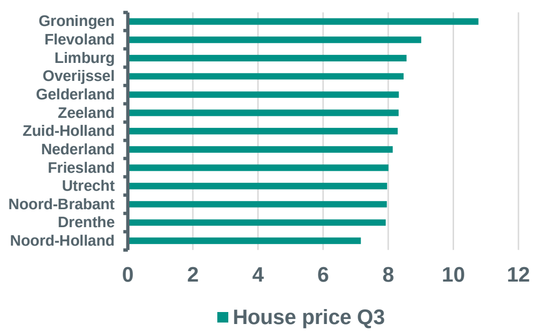
Year-on-year percentage change




Source: Statistics Netherlands (CBS)/Dutch Land Registry

**Randstad no longer the price driver**

Year-on-year percentage change




Source: Statistics Netherlands (CBS)/Dutch Land Registry

The higher prices of pre-owned housing have a knock-on effect on new-build prices. The average new-build price in Q2 was EUR 410,000, EUR 10,000 higher than in the same period of the previous year. House construction is continuing despite Covid, but is still lagging demand due to all sorts of problems, such as a lack of permits issued in the past. According to house construction website *WoningBouwersNL*, 28,500 dwellings were sold until end of October 2020, 3,500 more than in the first ten months of 2019.

An underlying regional shift is also visible. Whereas the initial price surge mainly occurred in the large cities, now the peripheral municipalities and cities outside the Randstad are catching up. Several economic causes can be cited for this. Covid may be taking a heavier toll on a city like Amsterdam with its many expats, tourists and symbiotic relationship with Schiphol. Another possible reason is that house prices in the large cities may have been stretched to the limit, with buyers unwilling to pay even more.

Interestingly, housing preferences may also be changing. With home working on the rise, commuter distance is becoming less important, and people feel a greater need for extra indoor and outdoor space. The latter is evident from the searches on the Funda property site. Analysis of these data shows, however, that prospective buyers adjust their wishes if these are difficult to fulfil. Improving an existing home can also be an attractive alternative to moving - particularly as many people are attached to their social network. Taking this into account, and the fact that vaccines now promise an end to the pandemic, we see a mass exodus from the Randstad as an improbable scenario.

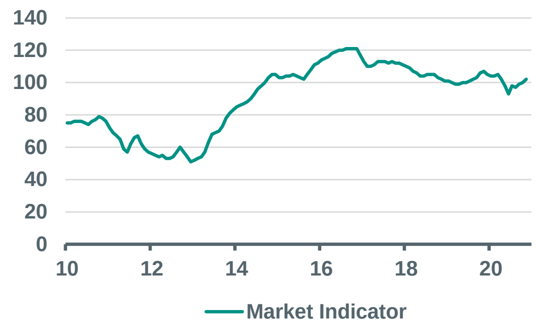
**Low mortgage rates keep housing affordable**

The sustained price rise is feeding confidence among potential buyers. After a brief dip, the Market Indicator of the Homeowners' Association (VEH) has been going up steadily since July. In November it broke through the neutral value of 100 to reach 102. A majority of the respondents are optimistic and foresee continuing upward momentum. Moreover, the respondents have lowered their mortgage rate outlook, with only a quarter now counting on an increase in the near future.

Low mortgage rates are a key pillar underpinning the housing market. These keep mortgage costs in check and contribute towards affordability. According to Calcasa, net housing costs amounted in Q3 to 14% of net income for homeowners with interest-only mortgages; that's only fractionally above the lowest level ever. The falling interest rates are less beneficial for people with annuity mortgages, who have seen their net housing costs rise to 33%. That is higher than the low point of 29% in 2016, but also clearly below the peak of 42% in 2008.

**Confidence rebounds after brief dip**

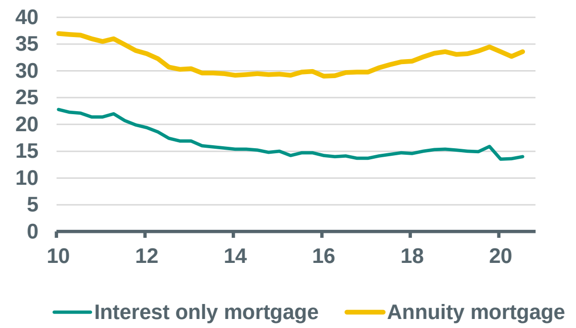
Index (100=neutral)




Source: Homeowners' Association (VEH)

**Housing costs low in terms of income**

Net housing costs as a percentage of net income




Source: Calcasa

Back in April we foresaw rising mortgage rates due to the higher risk premiums in the financial markets. However, thanks to massive government interventions, companies stayed afloat and unemployment growth was marginal, so that risk premiums declined again. Governments can easily finance the increased budget deficits resulting from the support measures. Central banks are creating the right conditions for this by buying up debt paper on a massive scale. This is keeping down interest rates on government loans, which is an important yardstick for mortgage rates.

International house prices are also converging, largely because central banks are pursuing similar policies. This reflects the fact that economic cycles of countries are increasingly synchronised. Economies are becoming more intertwined due to more intensive trade and the integration of the financial sector. Banks extend cross-border loans and raise funding abroad. The US, in particular, is a popular source of funding. This is why the inflow and outflow of US dollars to and from the US is increasingly putting an ever-stronger stamp on global house prices.

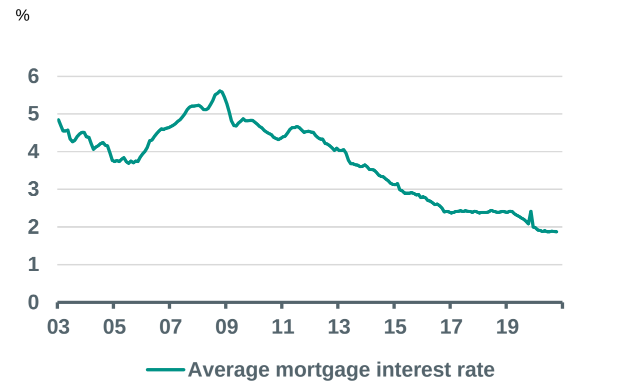
The central banks are likely to continue their asset buying programmes in their joint effort with governments to pull the economy out of the trough. As a result, the mortgage outlook is favourable. The fact that house prices have not only risen in the Netherlands since the Covid outbreak, but also in many other countries, suggests that a common factor (such as low mortgage rates) is responsible for the recent house price revival rather than local factors (such as the persistent housing shortage in the Netherlands).

**Setbacks for investors**

Investors are also benefiting from the low mortgage rates. Though hard data are absent, various signals suggest that the rental market continues to tempt investors. Apart from the attractive financing costs due to the low mortgage rates, the meagre interest rates on savings are also prompting them to seek better performing, safe investment alternatives. In contrast with retail and commercial buildings, the income from rented housing has remained fairly stable and rented properties have retained their value.

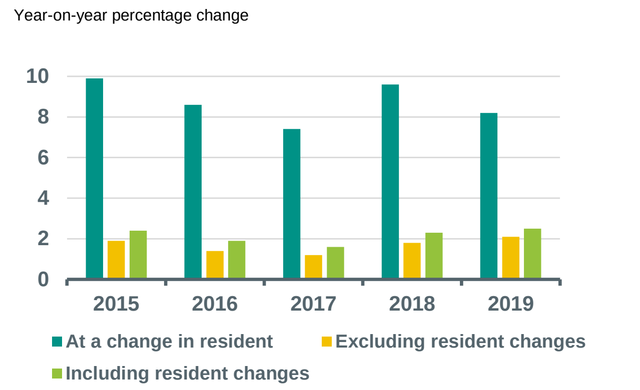
Against this, the measures being taken to protect tenants are discouraging investors. Investors are protesting against the rental increase cap of inflation plus 1% (was inflation plus 2.4%). In their view this measure, which applies to the private as well as the social segment, is at odds with arrangements made in rental contracts. They also oppose the plan to limit the share of the property's rateable (WOZ) value in the total number of home valuation points to 33%. This could push lots of liberalised dwellings back into the social segment, where rents are lower and landlords with a substantial number of dwellings are subject to the Landlord Levy.

**Central bank support dampens mortgage rates**




Source: DNB

**Cabinet wants to clamp down on rental increases**




Source: Statistics Netherlands (CBS)

Further setbacks for investors include the higher transfer tax rate effective from 1 January 2021. This affects the marketability and value of rented housing. In addition, municipalities are being given more scope to prevent investors buying up properties and to issue restrictive rental permits, thereby limiting the opportunities for buy-to-let investors. The government also wants to clamp down on temporary rental contracts. This will make it less easy for investors to raise rents or sell properties.

According to investors, these measures will at most put private parties off investing in rented properties in the future. As a result, less rented housing will be added to the existing stock, making it even more difficult for home seekers to find a suitable home in the tight mid-market segment. In addition, they expect less funding to be made available for energy-efficiency measures, which will adversely affect the quality of existing housing for current tenants. If these predictions prove correct, the upward pressure on house prices from investor demand will decrease in the coming years.

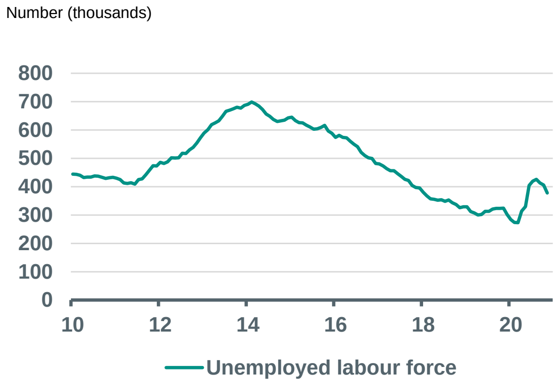
**Factors driving house inflation are subsiding**

Apart from the reduced investor interest, several other reasons can be mentioned for assuming that the upward price momentum will abate. As noted, central banks will continue to support governments in their efforts to pull the economy afloat. Their massive debt buying programmes are keeping interest rates low. This has also pushed down mortgage rates, enabling borrowers to take out a higher mortgage which, in turn, contributes to higher prices. However, if the decline in mortgage rates stalls, this favourable effect will gradually ebb away.

Another reason concerns the income trend. So far, the labour market has held up reasonably well thanks to the wage cost subsidies from the government. But these will be gradually wound down, raising the threat of unemployment rising from the current low level. Various large companies have already announced reorganisations. This means that even people on permanent contracts - who are more likely to be homeowners than flexible workers - are now also at risk of being laid off. The collective labour agreements currently being negotiated (or rather the absence of such agreements) also point to a moderate trend in contract wages. Finally, there is great uncertainty surrounding the pensions. All in all, stagnating income growth could make mortgages less affordable, which would also dampen house price increases.

Yet another factor is the national election in March. Given the many problems surrounding the provision of housing, the organisation of the housing market will be an important campaign theme. During the past two terms of government, measures were already taken to significantly reduce the mortgage interest relief for homeowners. This tempered the upward price momentum. And if it's up to the Dutch central bank (DNB) and a large number of international policy organisations, there is more of the same to come. These institutions are finding a ready ear among several political parties (D66, GroenLinks, PvdA and SP) whose election manifestos include proposals for further adjustments to the mortgage interest relief.

**Unemployment growth limited so far**




Source: Statistics Netherlands (CBS)

**Less consumption translates into high savings**


Source: Statistics Netherlands (CBS)

Against this, there are also several factors that may fuel house valuations to even higher levels. The crisis effectively forced people to rein in their spending, for instance because they were unable to go on holiday. Due to this fall in consumption, the amount of surplus savings has grown. The bulk of these savings have been placed in deposits for a rainy day. However, when the economy opens up again and people see a brighter future ahead, these savings will be freed up and possibly used to buy a new home.

House prices are also receiving support from the lower transfer tax for first-time buyers. This will give valuations in the price segment up to EUR 400,000 an extra impulse. Furthermore, the increase in the cost threshold for the National Mortgage Guarantee (NHG) by EUR 15,000 to EUR 325,000 will give buyers extra breathing space, as will the increase in the maximum available mortgage for buyers with student debt and double-income households. Regarding the group of double-income households, a US study confirms that a second income helps to limit the risk of income loss and mortgage arrears.

A final pillar underpinning price levels is the current shortage of housing. Despite the Government taking more active control, providing more funding and helping provinces to expand their planning capacity, the volume of house construction remains too low. Thanks to the shift to online, more office and commercial buildings are becoming available for conversion to residential use, but this is a drop in the ocean. Due to the many problematic issues confronting the construction industry and the mismatches between supply and demand, the expansion of the housing stock continues to lag behind the growing population.

On balance, the factors driving house inflation are losing force. Once the adverse consequences of the Covid crisis start to feed through in the labour market and the favourable impact of low interest rates fades away, the increase in prices will gradually decelerate. We are counting on a price increase of 5% in 2021 and 1% in 2022. The weakening of the upward price momentum will be preceded by a decline in the number of transactions. Following an increase of 7.5% in 2020, the transaction volume is expected to fall by 10% in 2021 and 5% in 2022.

This implies a strong upward adjustment. Our previous Housing Market Monitor assumed that prices would stabilise in 2020. Two reasons can be mentioned for this. First of all, the carry-over effect. The strong price rise in the second half of 2020 will feed through into the average price increase for 2021. If prices stabilise at the current level, this will already result in a rise of 3.5%. Furthermore, the arrival of the vaccine opens up prospects of a revival of activity, which will limit the economic damage inflicted by the pandemic.