DUTCH MORTGAGE PORTFOLIO MANAGEMENT

Q3 | 2024

QUARTERLY MARKET UPDATE

Index

Want to keep up to date with the latest market insights and data? Visit our data insights page: **https://dmmi.dmpm.nl**.

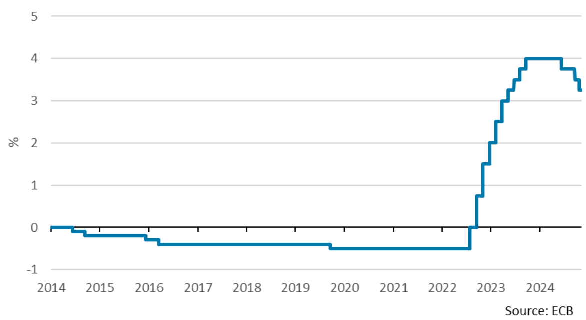
Do you have any questions about the information in this document, or are you interested in exploring Dutch residential mortgage investments? Send an email to **info@dmpm.nl**.

1. Dutch economy

Fragile eurozone economy induces ECB for further cuts

During the third quarter and most recently on October 17, the ECB reduced their policy rate, which is a continuation of the earlier cut in June of this year. In September the deposit rate was reduced from 3.75% to 3.50% followed by another cut of 25bp in October to 3.25%, see figure 1.1 below.

Figure 1.1: ECB Deposit rate

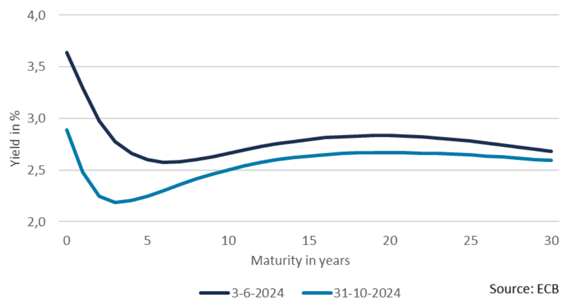


The rate cut in September had a more special character, as the main refinancing rate was reduced more than the deposit rate facility. In the end, the ultimate goal of this change in the ECB's monetary policy framework, it to normalize the size of the ECB balance sheet and therefore the normalization of monetary policy. It goes into too much detail to elaborate on the reasoning why the spread between these two rates has been reduced, but for the interested reader we would like to refer to the following ECB article: Changes to the operational framework for implementing monetary policy.

What is relevant for the Dutch mortgage market, is what the ECB is expected to do in the coming months and what the impact will be on the (swap) curve. Will the yield curve slowly normalize in the coming quarters and away from the current inverse?

To start with the latter. As figure 1.2 below shows, since the first rate cut in June the short-end of the curve rallied significantly. For example, the very short-end of the curve moved 70bp up to the end of October. As the 10+ year sector rallied only 20bp or less, it's clear that the curve is slowly but certainly starting to normalize. The 0-3 maturity bucket is still inverse, but either three or more cuts of 25bp or a significant change in ECB expectations could make the whole curve upward sloping again.

Figure 1.2: Euro AAA Governement Yield Curve



The October press conference of the ECB was surprisingly dovish. We mentioned in the previous quarterly update that the ECB was not in a hurry to cut rates, as the ECB mentioned that inflation risks are tilted to the upside. But last month the ECB made a twist, as they made clear that:

1. with regard to inflation, there is probably more downside risk than upside risk
2. there are downside surprises in indicators of economic activity
3. financing conditions remain restrictive

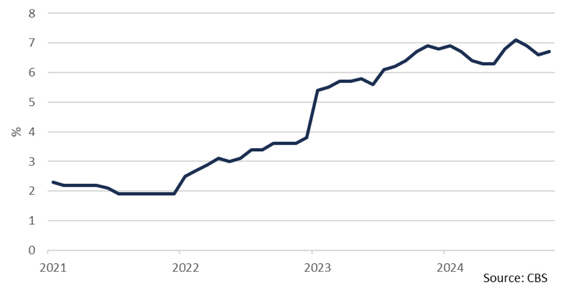
In addition, euro area inflation dropped to 1,7% in September from 2,2% in August, and that was a surprise for the ECB. So this basically means that there is plenty of room for further rate cuts. Markets now expect for the coming December meeting at least one cut of 25bp and possibly more than 25bp.

LOWER RATES AND HIGH WAGE GROWTH POSITIVE FOR HOUSE PRICES AND ARREARS

For the Dutch mortgage market this means that mortgage rates will decline further across the curve, with a more pronounced decline in rates at the short end of the curve. In addition, the probability that consumers will aim for longer fixed rate periods may increase. But we have not seen that yet, as 80% of the new mortgage loan applications have a fixed interest rate period of 10 years or shorter. And that percentage has remained stable in 2024, despite lower mortgage rates. We will discuss this further in chapter 3 below.

The gradual reduction in mortgage rates is good news for consumers, as it improves affordability for new home buyers. Also, wage growth has remained relatively high in 2024 and also the latest reading from October of 6,7% growth year on year is still solid, see figure 1.3. All in all, this is positive in terms of house prices and credit risks in mortgage portfolios.

Figure 1.3: Dutch wage growth YoY



REPAYMENT CORONA SUPPORT DRIVES CORPORATE BANKRUPTCIES HIGHER

Despite positive economic growth in the second and third quarter of 2024, the number of corporate bankruptcies continued to increase. This is a trend that started in the fourth quarter of 2021, see figure 1.4 below. Over the past two years, the incidence of bankruptcies has doubled. But as figure 1.4 also shows, a year on year comparison can sometimes be tricky as the level of bankruptcies in 2023 was close the lowest level in 25 years. Although the number of bankruptcies is indeed increasing, it's also moving back to longer term averages. Secondly, this rise is not currently alarming given the scale of the Dutch business environment, which comprises over 2.3 million companies compared to the 1,087 bankruptcies recorded in Q3 2024. These figures indicate that 0.05% of all companies went bankrupt in Q3 2024.

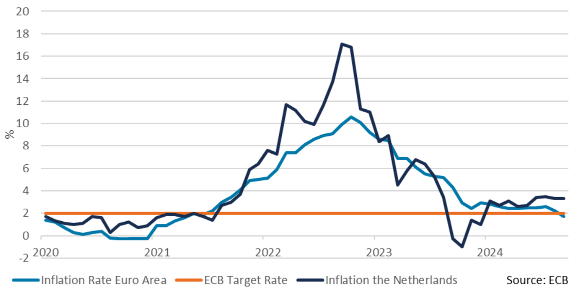
Figure 1.4: Number of bankruptcies per quarter

One significant factor contributing to the rise in bankruptcies is the obligation of many companies to repay financial assistance that was granted by the government during the COVID-19 pandemic, see the following article Verwachte faillissementsgolf geen reden tot paniek. Hence the current increase in also contains the postponed bankruptcies of unviable companies, which survived as a result of COVID-19 pandemic government measures.

DUTCH INFLATION REMAINS ELEVATED VS REST OF EUROZONE

Meanwhile, the labor market remains tight, characterized by a persistent imbalance between job vacancies and available workers. The unemployment rate in the Netherlands remains low, reflecting a tight labor market that has both positive and negative implications for the economy. The persistent labor shortage continues to put upward pressure on wages as mentioned above. This contributes to an inflation rate (HICP) that currently stands at 3.3%. In contrast, the annual inflation rate for the Eurozone has decreased to 1.7% in September compared to 2.8% at the beginning of this year, see figure 1.5 below.

Figure 1.5: Inflation rate in the Netherlands vs Euro area



The housing market remains under pressure, facing challenges similar to those in prior quarters. A continual imbalance between housing supply and demand is pushing prices higher. Consequently, first-time buyers and others trying to enter the market arefinding it challenging due to rising costs and fierce competition for available homes.

The Dutch economy continues to navigate a complex landscape of tight labor markets, inflationary pressures, and housing market challenges as it progresses through the third quarter of 2024.

PLANS OF THE DUTCH GOVERNMENT TO TACKLE THE HOUSING SHORTAGE

In the previous report we referred to the 'Hoofdlijnenakkoord' that was published by the new Schoof cabinet. During Budget Day (in Dutch: Prinsjesdag) more details were provided on the policy goals of the new cabinet. We have highlighted a few items that are relevant:

1. **Increase in purchase power:** Purchasing power is set to improve for many individuals next year. On average, people are expected to see an increase in their purchasing power. The government is particularly focused on supporting vulnerable groups and middle-income earners through several key initiatives. The government is implementing a comprehensive package of measures, including increased child benefits, tax reductions for lower incomes, enhanced childcare subsidies, and improved housing benefits. These measures collectively aim to bolster the purchasing power of low- and middle-income households, helping them navigate rising living costs more effectively.
2. **Housing:** The top priority of the government is to reduce the housing shortage. The plan to build 100,000 new per year remains. Two-thirds of this will be affordable to low and middle-income households. To support this plan, the government

decided to allocate €5 billion until 2030. The government plans to increase land availability for housing and reduce construction barriers through the 'Versterking regie volkshuisvesting' law. This includes making building land more affordable and exploring a tax on undeveloped housing land to encourage sales. The government aims to accelerate housing construction by streamlining planning and permits, promoting standardised industrial methods, and targeting 50% of new homes to be built this way by 2030. For a more in depth analysis on the housing plans of the government, see: New Dutch government: Tackling the housing shortage is top priority and New Dutch housing plans: clear acknowledge of the problem but more budget and creativity is required.

3. **Focus on Energy Transition and Climate Adaption:** The Dutch government aims to enhance housing sustainability and energy efficiency primarily to reduce energy costs for residents, focusing on improving insulation in existing homes and buildings. In parallel, it has allocated €1.8 billion to strengthen the Netherlands' flood protection infrastructure, reinforcing dikes and dunes to prevent sea and river water intrusion. This integrated approach not only addresses immediate environmental challenges but also promotes long-term resilience and efficiency in the housing sector, ensuring that homes are both energy-efficient and safeguarded against climate-related risks.

DUTCH
MORTGAGE
PORTFOLIO
MANAGEMENT

2. Housing market

Uncertainty in housing market prevails Owner-occupied houses

Despite the Cabinet measures announced on Budget Day (Prinsjesdag), uncertainty in the housing market remains high. A recurring problem is the supply shortage on the owner-occupied housing market, which is pushing up prices. In the DMPM publication, about the new plans of the government for the housing market, New Dutch housing plans: clear acknowledgement of the problem but more budget and creativity is required, we took a closer look at the structural housing shortage in the Netherlands in relation to the government's plans.

What is clear is that, for now, the uncertainty in the housing market remains. Whereby the supply shortage, the high demand for housing, the further declining mortgage interest rates, stabilizing inflation and the trend of rising wages will certainly have a price-raising effect in the time to come.

SUPPLY SHORTAGE REMAINS

Due to the high population density and competing demands for limited space that is available, there will be a significant housing shortage in the foreseeable future. There is currently a shortage of more than 400,000 homes. And in 2050 the housing shortage will still be an issue, given the estimated shortage of 150,000 homes in the latest optimistic forecasts. To tackle this issue, the Dutch government is aiming to build/create 100,000 per year. But two issues need to be taken into account. First of all, adding 100,000 houses annually to the housing stock is ambitious. Secondly, one of the inputs that is used to calculate the annual shortage is the expected population growth rate. But the fact is that the population growth has been grossly underestimated over the last decade, and as a result the home shortage risk will further increase.

The target of building 100,000 new homes consistently per year is ambitious because of this population growth. Also other factors such as labor shortages in the construction sector, the lack of availability of land and environmental restrictions play an important role. Moreover, the €5bn allocated by the government to stimulate the increase of available homes may not be sufficient and needs to be adjusted for inflation and unforeseen costs . All in all achieving the targeted 100,000 houses per year on short notice, seems to be very challenging if not impossible.

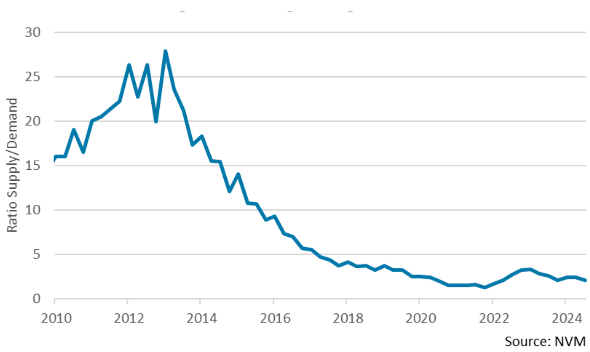
HOUSING MARKET STILL CROWDED DESPITE TIGHTNESS

The housing market continued to be under pressure in the third quarter, due to a shortage of available homes, posing major challenges especially for first-time buyers. The scarcity creates a fighting market, with overbidding remaining the rule. Adjustments in lending standards and increased incomes have made homes for sale more accessible to buyers, which has increased demand.

SUPPLY-DEMAND RATIO CLOSE TO 15 YEAR LOWS

The tightness indicator dropped from 2.6 to 2.1 in one year, figure 2.1. The indicator says something about the ratio of supply to transactions, the lower the indicator the tighter the market.

Figure 2.1: Housing shortage indicator



NVM REPORTS HIGHEST NUMBER OF TRANSACTIONS IN ALMOST FOUR YEARS

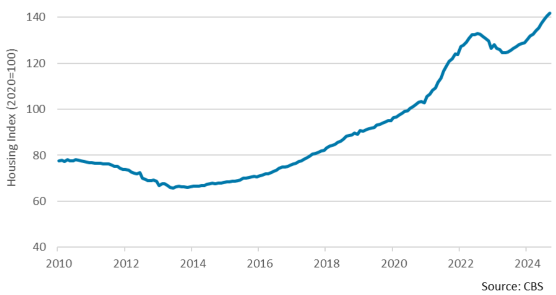
Over the last quarter the Dutch Association of Realtors (NVM) also reported the highest number of homes sold, by NVM brokers, in almost four years. This is notable because normally in the quarter that includes the holiday season, far fewer homes are sold. NVM attributes the upward trend to slightly more homes being offered for sale in a tight market with increasing confidence and improved financing options.

HOUSE PRICES HAVE FURTHER ROOM TO RISE

In one year, the average price of homes sold in the Netherlands increased by €50,000. However, the price development in the third quarter showed just a small plus of 0.4% and an average transaction price of €473,000. Only €2,000 more than in the previous quarter. The increase is thus much smaller than the 7.7% increase achieved last quarter, figure 2.2. As already mentioned, in the third quarter, which includes the holiday season, prices usually rise less sharply, but the minimal increase this quarter seems to be a correction to the very sharp rise last quarter. But, given lower mortgage rates, strong wage growth and a continuing housing shortage, there is every reason to expect for house prices to go higher.

In addition, higher home prices are leading most homeowners to have surplus value, which more and more often is used to remodel the home or make it more sustainable.

Figure 2.2: House prices at record high



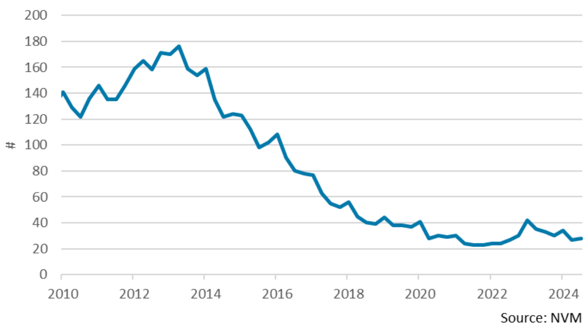
OVERBIDDING STILL COMMON PRACTICE

On average, people pay 4.6% more than the asking price. For the average home, this amounts to €22,000. More than two in three home sales in the Netherlands involve paying more than the asking price, about the same as in the previous quarter.

HOMES ARE STILL BEING SOLD VERY QUICKLY

It currently takes an average of four weeks (28 days) to sell a home, see figure 2.3. Compared to a year ago, this is four days faster, and compared to last quarter one day longer. Close to 90% of all homes are sold within two months. Another 6% are sold within six months. Only 1% of homes, took longer than a year to sell. Often these are homes that deviate from the norm. For example, homes that require substantial renovation or modernization or these are homes that are poorly located.

Figure 2.3: Average number of days needed to sell



NEW HOUSING CONSTRUCTION

ALREADY MORE SALES IN 2024 THAN IN ALL OF 2022 AND 2023

The number of new construction is increasing. This was necessary, as a low point was reached at the end of 2023. Nearly 23,200 new construction homes went on sale in 2024. This is more than in the first three quarters of 2021, 2022 and 2023.

Sales tend to decline in the third quarter, including 2024. With over 6,300 homes sold, there is a significant drop from the 7,800 in the previous quarter. However, this decline is normal. Less new supply comes on the market during the summer and many home seekers pause their search. Despite the decline, sales momentum remains good. The good sales momentum is also evident from a comparison with last summer's numbers, this year 27% more homes were sold.

Sustainability, especially the associated lower energy costs, remains the main reason why home seekers choose new construction. This reports NVM following a survey of new-build estate agents it conducted.

RENTAL MARKET

NUMBER OF HOMES IN RENTAL MARKET DROPS SHARPLY

It is not only the purchase market that is in trouble; finding a rental property is also almost impossible. On July 1, 2024 the Affordable Rent Act went into effect, with which former Minister De Jonge (Wonen) intended to make rents affordable again. The law results in a large number of medium-priced rental properties falling under regulated rent, with corresponding maximum rents. This would eventually reduce the rent of as many as 300,000 homes by an average of €190. There is also a ban on temporary rental contracts and grumbling about the tax burden.

Because of these new government measures many landlords decided to sell their property. The number of available homes in the non-subsidized rental housing has dropped by more than a third, causing the rent per square meter price to rise sharply.

The Pararius Rent Monitor shows that tenants again have less choice and have to pay more. Across the Netherlands in the third quarter of this year, only 12,368 non-regulated rental properties became available for new tenants, a decrease of 37.6% compared to a year earlier.

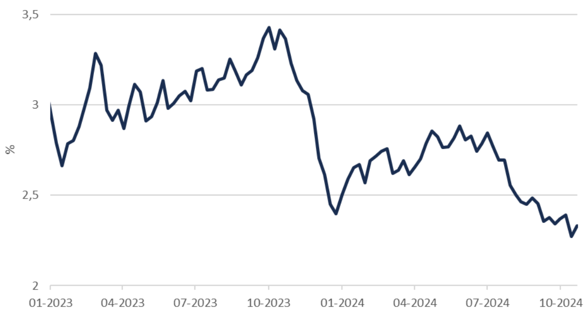
The average square meter price of non-subsidized rental property rose by 7.4% in the third quarter of 2024 compared to a year ago. That average rent is €1751.61 per month. Government measures designed to better protect tenants therefore seem to be counterproductive.

3. Mortgage market

Mortgage spreads move back to highest level of 2024

Swaps rallied in the third quarter, together with Dutch and German government bonds, see for example the 7-year swap rate time series in figure 3.1. But the rally in swaps e.g. in the 7 year sector, was more pronounced and as a result swap spreads tightened vs government bonds. At the start of October, there was a sell-off in governments bonds, this let to a further tightening in swaps spreads.

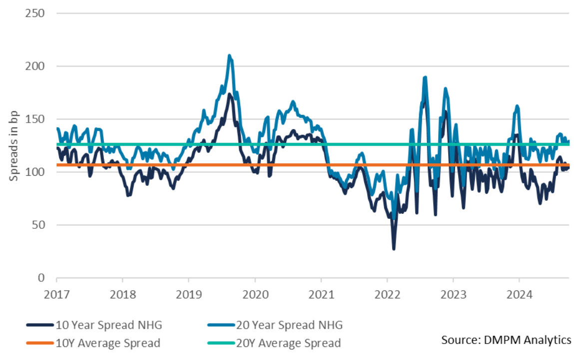
Figure 3.1: Seven years swaps



Source: DMPM Analystics

Mortgage rates also declined, but given the delayed response in mortgage rates, mortgage spreads increased versus swaps in the third quarter. To visualize, we have included 10 and 20 year NHG spreads, and non-NHG spreads for the same maturities in figure 3.2 and 3.3. With respect to NHG spreads, as swaps rallied, the 10 year mortgage spread is back above 100bp from around 80 during the summer months. The same holds for the 20 year sector, which is currently above 125bp. To make comparison over time easier, we have added average spreads for both maturities in the figures 3.2 and 3.3. Judging from figure 3.2, it looks like that there is a minimum spreads level of 75bp for 10-year NHG, with a brief exception in 2022, due to the rapid rise of swaps. For 10-year non-NHG that minimum spread level is around 125bp, see figure 3.3.

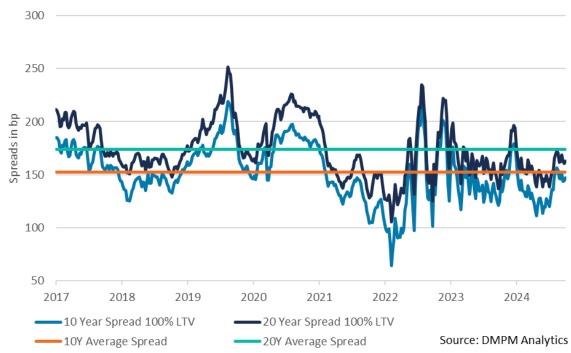
Figure 3.2: NHG spreads



Source: DMPM Analytics

The 10-year Non-NHG spread widened 25bp since July to currently 150bp and the 20 year non-NHG spread is currently above 160bp.

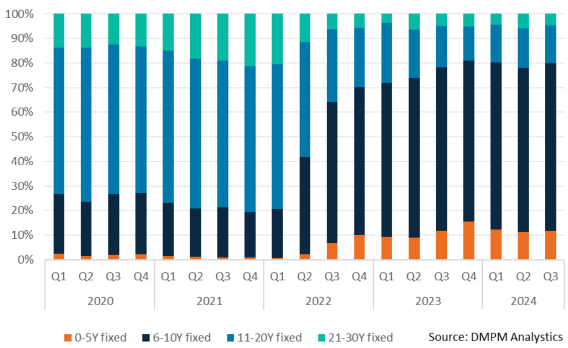
Figure 3.3: Non-NHG spreads



AVERAGE FIXED RATE PERIOD REMAINS AT A LOW LEVEL, DESPITE LOWER MORTGAGE RATES

As interest rates have risen since 2022, the preferences of consumers and brokers with respect to the fixed interest rate period has shifted significantly too. Figure 3.4 below shows the market share of each maturity bucket on a quarterly basis. In response to the rapid increase in mortgage rates at the beginning of 2022, consumers opted for a much shorter fixed rate period. That explains the complete turnaround in market share of the maturity buckets.

Figure 3.4: Market share per maturity bucket



For example, in 2020 the market share of the 11-20 year maturity bucket was 60% and less than 25% for the 6-10 year maturity bucket. In addition, sub 5 year sector was hardly existent. Starting in 2022 and beyond, this completely reversed. In the third quarter of 2024 the market share of the sub 10 year maturity bucket was 80% versus 15% for the 11-20 year sector and around 5% for 21-30 year sector.

This shift in fixed rate preference can also be visualized in terms of the average fixed interest period of new mortgage loan applications. Figure 3.5 below illustrates the significant shift from 20 years in 2022 to 11 years in 2024. The current average fixed rate period of around 11 years, hasn't been this low since 2016.

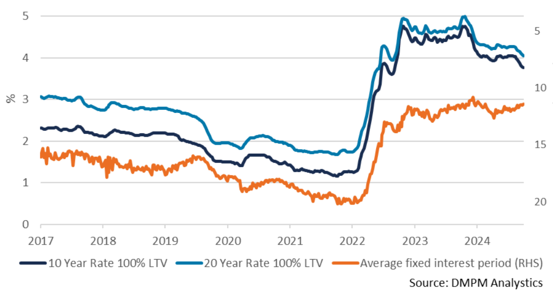
Figure 3.5: Average fixed interest period new mortgage applications

WHAT WILL CONSUMERS DO IN THE NEXT FEW YEARS?

Since the top in mortgage rates in at the end of 2023, see the dark and light blue timeseries in figure 3.6, rates have moved 100bp lower. Despite this significant move, consumers haven't opted for longer maturities. For example, as is clear from figure 3.4, the market shares of all maturity buckets remained more or less unchanged in 2024. To visualize the relation between mortgage rates and the average fixed interest period of new mortgage loan applications, we combined the two variables in figure 3.6 below.

Do take note of the reverse order of the average fixed interest period of new mortgage loan applications on axis on the right hand side.

Figure 3.6: Mortgage rates vs average fixed interest period new mortgage applications



The inverse relation and good fit is clear in figure 3.6. But, as mentioned early, despite the drop in mortgage rates, the average fixed rate period has not moved up yet in recent months. Given the ECB trajectory to lower policy rates, further curve normalization and lower rates across the curve are expected. But what will consumers do and also when? Although it's hard to predict when consumers will respond, it's a near certainty, provided continuation of the downward trajectory of interest rates, that consumers will opt for longer maturities. The only remaining question is when. For bank investors this is something to take into consideration.

WE EXPECT A DECREASE IN THE MARKET SHARE OF NHG MORTGAGES IN 2025

NHG recently announced that two important changes are planned for 2025. First, the NHG limit, that is the maximum value of a home that can be financed with the backing of NHG, will increase to €450,000 from €435,000. The maximum home value including new measures to make the home more energy efficient, will be increased to €477,000 from €461,100.

Secondly, the levy that is charged to homebuyers to use the NHG protection will be decreased by 20bp, to 0.40%. To learn more about this levy, we would like to refer to the following article that we wrote earlier: Dutch National Mortgage Guarantee Scheme - A Primer for Investors. Although the difference in purchasing costs of a house at the maximum NHG limit is only €900, it can make a big difference for the average home buyer in the NHG segment.

Different from last year, is that the current average home price of €473,000 (Q3 2024) is higher than the NHG limit that will be valid from the first of January 2025. In comparison, the average house price in the third quarter of 2023 was €422,000 vs a NHG limit of €435,000 starting from the first of January of 2024. This means that, right from the start of 2025, the pool of eligible houses for the NHG market is a lot smaller than at the start of 2024. For that reason we expect an overall decline of NHG market share in 2025 compared to 2024. As housing prices will very likely continue to increase in 2025, the pool of eligible houses will shrink even more. In figure 3.7 below, we have included the NHG market share over time and currently its above 30%. To be complete, the market share of the NHG market also depends how the relative size of the non-NHG market evolves.

Figure 3.7: NHG market share of total mortgage applications

The graphs shows also that with every turn of the year there is local maximum visible which can be attributed to the increase of the NHG limit right at the start of the new year. With the exception of 2022, the market share gradually levels of during the year. The latter is related, as mentioned above, that the pool of eligible houses decreases as result of the increase in housing prices.

ARREARS HAVE INCREASED MARGINALLY

In some European country arrears can be a tricky subject, but not in the Netherlands given the extremely low percentage of arrears in the residential housing market. So we do have to put things in perspective. But, during 2024 we do see a small uptick in arrears. For example for the arrears at the end of the month in figure 3.8 below, at the start of 2023 the percentage of arrears was around 0,25%, currently that's around 0,35%. Still extremely small, but it's worth noting. From the inflow of arrears there is nothing we conclude yet, despite the increase in 2024. In 2017, 2018 and 2019 similar spikes were visible, but the statistic moved back to the average in the months that followed. It's normal to see in increase in arrears after the summer, so we need more data to draw further conclusions. If we look at daily mortgage arrears as a percentage of the portfolio in figure 3.9, we can see an improvement in the month of October. The peak value in the middle of the month is lower, and the arrears percentage at the end of the month is also improving. Therefore, the data for the month of October looks promising, but more data is required to see if arrears move back to longer term averages.

Figure 3.8: Percentage of mortgages in arrears

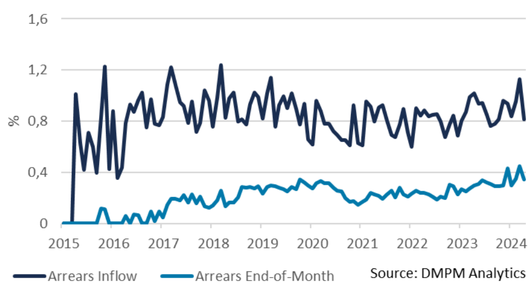
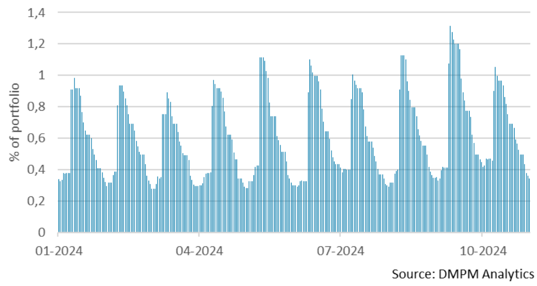


Figure 3.9: Number of Daily Arrears as % of Portfolios



AUTHORS

Marck Bulter

Portfolio Manager

marck.bulter@dmpm.nl

Eric Rood

Portfolio Manager

eric.rood@dmpm.nl

Walter van Maurik

Portfolio Manager

walter.vanmaurik@dmpm.nl

Arno Dries

Manager Investor Relations

arno.dries@dmpm.nl

Roy van den Hatert

Portfolio Manager

roy.vandenhatert@dmpm.nl

FOR MORE INFORMATION

For more insights and information about our services, visit our website: **www.dmpm.nl**.

To stay up to date with our publications, **follow DMPM on LinkedIn**.

GET IN TOUCH

For questions about this publication or about our services, feel free to reach out to the authors of this article or to **info@dmpm.nl** or **+31(0)10 242 2400**.

SOURCES

- DMPM Analytics
- Prinsjesdag: Miljoenennota en Rijksbegroting | Rijksoverheid.nl
- New Dutch government: Tackling the housing shortage is the top priority | DMPM
- New Dutch housing plans: clear acknowledgement of the problem but more budget and creativity is required | DMPM
- Meer faillissementen in september | CBS
- Monetary policy decisions