Dutch residential mortgage market

The Dutch residential mortgage debt stock is relatively sizeable, especially when compared to other European countries. Since the 1990s, the mortgage debt stock of Dutch households has grown considerably, mainly on the back of mortgage lending on the basis of two incomes in a household, the introduction of tax-efficient product structures such as mortgage loans with deferred principal repayment vehicles and interest-only mortgage loans, financial deregulation and increased competition among originators. Moreover, Loan-to-Value (LTV) ratios have been relatively high, as the Dutch tax system implicitly discouraged amortisation, due to the tax deductibility of mortgage interest payments. After a brief decline between 2012 and 2015, mortgage debt reached a new peak of EUR 870.7 billion in Q2 2024[1]. This represents a rise of EUR 25 billion compared to Q2 2023.

Tax system
The Dutch tax system plays an important role in the Dutch mortgage market, as it allows for partial deductibility of mortgage interest payments from taxable income. Historically, this has resulted in various deferred amortisation mortgage products, most importantly the use of interest-only loan parts.

Since 1 January 2013, all new mortgage loans have to be repaid in full in 30 years, at least on an annuity basis, in order to be eligible for tax relief (linear mortgage loans are also eligible). The tax benefits on mortgage loans, of which the underlying property was bought before 1 January 2013, have remained unchanged and are grandfathered, even in case of refinancing and relocation. As such, new mortgage originations still include older loan products, including interest-only. However, any additional loan on top of the borrower's grandfathered product structure, has to meet the mandatory full redemption standards to allow for tax deductibility.

A second reform imposed in 2013 was to reduce the tax deductibility by gradually lowering the maximum deduction percentage. As a result, the highest tax rate against which the mortgage interest may be deducted is 36.97% (equal to the lowest income tax bracket) in 2024. No further reductions are currently planned.

There are several housing-related taxes which are linked to the fiscal appraisal value ("WOZ") of the house, both imposed on the national and local level. Moreover, a transfer tax of 2% is due when a house is acquired for owner-occupation. From 2021, house buyers aged between 18 and 35 years will no longer pay any transfer tax. Currently, this exemption only applies to houses sold for 510,000 euros or less and can only be applied once. Since 2023, a transfer tax of 10.4% is due upon transfer of houses which are not owner-occupied (compared to 8% in 2022).

Although these taxes partially unwind the benefits of tax deductibility of interest payments, and several restrictions to this tax deductibility have been applied, tax relief on mortgage loans is still substantial.

Loan products
The Dutch residential mortgage market is characterised by a wide range of mortgage loan products. In general, three types of mortgage loans can be distinguished.

Firstly, the "classical" Dutch mortgage product is an annuity loan. Secondly, there is a relatively big presence of interest-only mortgage loans in the Dutch market. Full interest-only mortgage loans were popular in the late nineties and in the early years of this century. Mortgage loans including an interest-only loan part were the norm until 2013, and even today, grandfathering of older tax benefits still results in a considerable amount of interest-only loan originations.

[1] Statistics Netherlands, household data. The total amount of mortgages outstanding reported has also increased including historic data due to a benchmark revision.

Thirdly, there is still a big stock of mortgage products including deferred principal repayment vehicles. In such products, capital is accumulated over time (in a tax-friendly manner) in a linked account in order to take care of a bullet principal repayment at maturity of the loan. The principal repayment vehicle is either an insurance product or a bank savings account. The latter structure has been allowed from 2008 and was very popular until 2013. Mortgage loan products with insurance-linked principal repayment vehicles used to be the norm prior to 2008 and there is a wide range of products present in this segment of the market. Most structures combine a life-insurance product with capital accumulation and can be relatively complex. In general, however, the capital accumulation either occurs through a savings-like product (with guaranteed returns), or an investment-based product (with non-guaranteed returns).

A typical Dutch mortgage loan consists of multiple loan parts, e.g. a bank savings loan part that is combined with an interest-only loan part. Newer mortgage loans, in particular those for first-time buyers after 2013, are full annuity and often consists of only one loan part. Nonetheless, tax grandfathering of older mortgage loan product structures still results in the origination of mortgage loans including multiple loan parts.

Most interest rates on Dutch mortgage loans are not fixed for the full duration of the loan, but they are typically fixed for a period between five and 15 years. Rate term fixings differ by vintage, however. In recent years, there was a strong bias to longer term fixings (20-30 years) but since Q2 2022 10 year fixings have rapidly increased in popularity as the sharply increased mortgage rates drove borrowers to seek lower mortgage payments by going for shorter fixings. Most borrowers remain subject to interest rate risk, but compared to countries in which floating rates are the norm, Dutch mortgage borrowers are relatively well-insulated against interest rate fluctuations.

Underwriting criteria

Most of the Dutch underwriting standards follow from special underwriting legislation (“Tijdelijke regeling hypothecair krediet”). This law has been present since 2013 and strictly regulates maximum LTV and Loan-to-Income (LTI) ratios. The current maximum LTV is 100% or 106% when financing energy saving measures. The new government has indicated not to lower the maximum LTV further. LTI limits are set according to a fixed table including references to gross income of the borrower and mortgage interest rates. This table is updated annually by the consumer budget advisory organisation “NIBUD” and ensures that income after (gross) mortgage servicing costs is still sufficient to cover normal costs of living.

Prior to the underwriting legislation, the underwriting criteria followed from the Code of Conduct for Mortgage Lending. Although the Code of Conduct is currently largely overruled by the underwriting legislation, it is still in force. The major restriction it currently regulates, in addition to the criteria in the underwriting legislation, is the cap of interest-only loan parts to 50% of the market value of the residence. This cap was introduced in 2011 and is in principle applicable to all new mortgage contracts. A mortgage lender may however diverge from the cap limitation if certain conditions have been met.

Recent developments in the Dutch housing market

Existing homes for sale have become more expensive at a rapid pace in recent months. In July, we saw a double-digit growth rate for the first time since the summer of 2022. Homes for sale were as much as 10.6% more expensive than a year earlier. On average, buyers paid about EUR 44,000 more for the average home sold. Compared to the price peak in 2022, houses are now about 4.6% more expensive again.

The rapid price recovery can be explained by the rapidly increasing demand: many house hunters, thanks to increased incomes, again have more financial opportunities to buy a house. In the second quarter of this year, Collective labor agreement (CLA) wage growth was 6.4%. Since 1982, wages have not risen as fast as they are now. Due to the robust wage increases, the gross modal annual income is expected to be as much as EUR 5,500 higher this year than in 2022. Due to increased wages, a household with two modal incomes can borrow about EUR 14,000 more in 2024 at an interest rate of 4% than in 2022 at an interest rate of 1.5%. The borrowing capacity has thus increased by about 3.5% in two years. Single people with an income of EUR 28,000 and above can borrow an additional EUR 16,000 from 2024. The borrowing capacity – which is mainly determined by the development of interest rates and incomes – is an important determinant of house prices. The ratio of borrowing capacity to house prices this year is again about the same as in early 2022. Back then, the housing market was overheated and house price appreciation broke all records. Therefore, it comes as little surprise that house prices are again soaring.

In the face of increasing demand, there is still very little supply. In fact, due to rising interest rates, new construction has received a severe blow, so that the housing shortage has only increased in recent years, despite the policy ambition. The number of homes for sale has also been falling for more than a year. The stiff competition for scarce houses for sale has also led to massive overbidding.

While incomes have risen sharply, we have seen mortgage rates drop a bit recently. Mortgage rates fell to the lowest level we've seen so far this year, Lower mortgage interest rates not only lower monthly costs for the same mortgage amount, but also allow people to borrow a little more and thus offer more on a house.

Thus, the house price acceleration at present can probably also be explained by sentiment in the housing market. Meanwhile, just over half of housing consumers expect moderate to strong price increases, according to the Market Indicator of home owners association Vereniging Eigen Huis. The fact that consumers expect house prices to rise further may have a reinforcing effect on the demand for owner-occupied homes. International research shows time and again that consumer price expectations (often based on recent price developments) are a very important predictor of how house prices will actually develop.

Since this year, the number of sales of existing homes for sale is picking up slightly. In the period August 2023 to July 2024, about 193,500 houses changed hands. That is 4.5% more than in the same period one year earlier. Looking only at 2024, the sales counter stands at nearly 111,000 homes sold, an 11% year-on-year plus.

In recent months, not only were a few more houses sold, houses were also sold faster. On average, houses were sold within a month (27 days); a year ago this took an average of 34 days (NVM 2024).

The fact that more homeowners have put their homes up for sale is probably not a structural trend but a temporary (catch-up) effect. When mortgage rates rose sharply, potential homebuyers dropped out and prices began to fall, a portion of homeowners probably temporarily put their selling plans on hold for a while. Now that the market is picking up, it has become easier to sell a home. Sales confidence has increased, and people who waited for market conditions to improve are putting their homes up for sale. The fact that more homes are being put up for sale is also associated with the wave of buy-to-let properties sold off by investors, which has been going on for a while now. Increasingly, rental houses are not re-rented after the tenant leaves, but the house is sold to people who are going to live in it themselves (owner-occupiers), the Dutch Land Registry (Kadaster) recently reported.

Forced sales

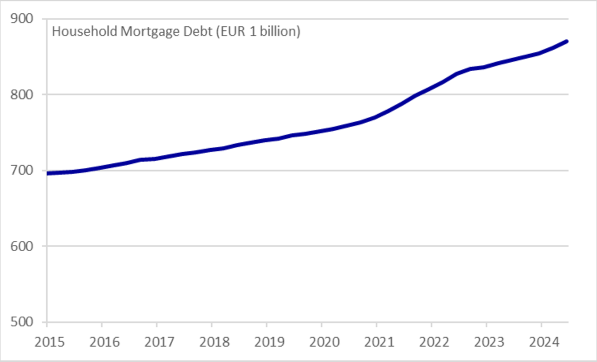
Compared to other jurisdictions, performance statistics of Dutch mortgage loans show relatively low arrears and loss rates[2]. The most important reason for default is relationship termination, although the

[2] Comparison of Moody's RMBS index delinquency data.

increase in unemployment following the economic downturn post financial crisis was increasingly also a reason for payment problems. The ultimate attempt to loss recovery to a defaulted mortgage borrower is the forced sale of the underlying property.

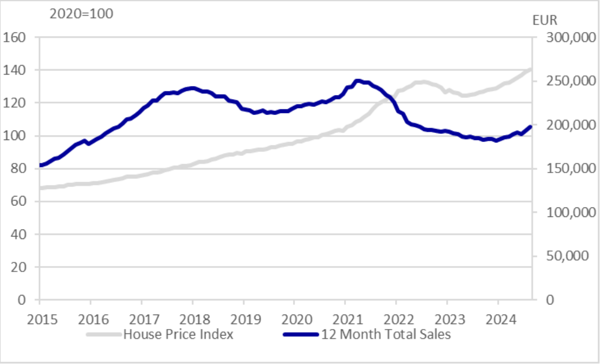
For a long time, mortgage servicers opted to perform this forced sale by an auction process. The advantage of this auction process is the high speed of execution, but the drawback is a discount on the selling price. The Land Registry recorded 60 forced sales by auction in Q2 2024 (0.12% of total number of sales over a 12 month period).

Chart 1: Total mortgage debt



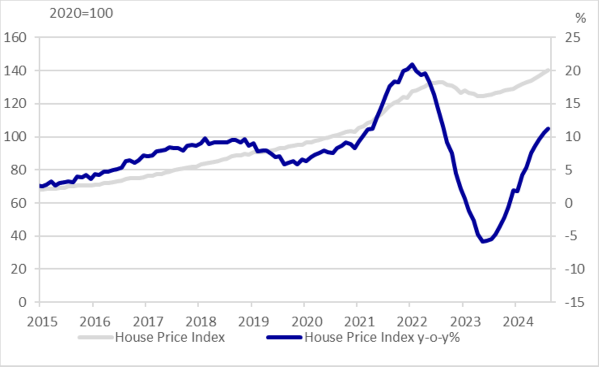
Sources: Statistics Netherlands, Rabobank

Chart 2: Sales



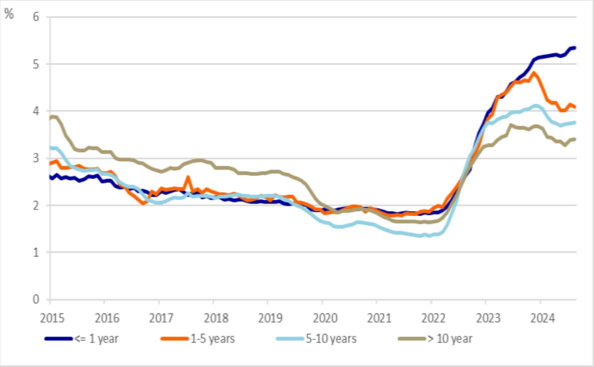
Sources: Dutch Land Registry (Kadaster), Statistics Netherlands (CBS)

Chart 3: Price index development



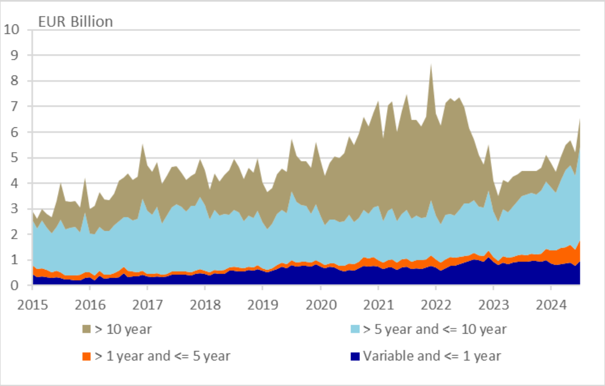
Sources: Statistics Netherlands, Rabobank

Chart 4: Interest rate on new mortgage loans



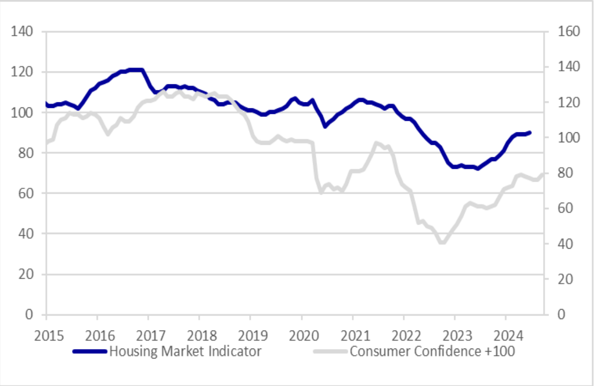
Source: Dutch Central Bank

Chart 5: New mortgages by interest type



Source: Dutch Central Bank

Chart 6: Confidence



Sources: Statistics Netherlands, OTB TU Delft and VEH