About Real Estate

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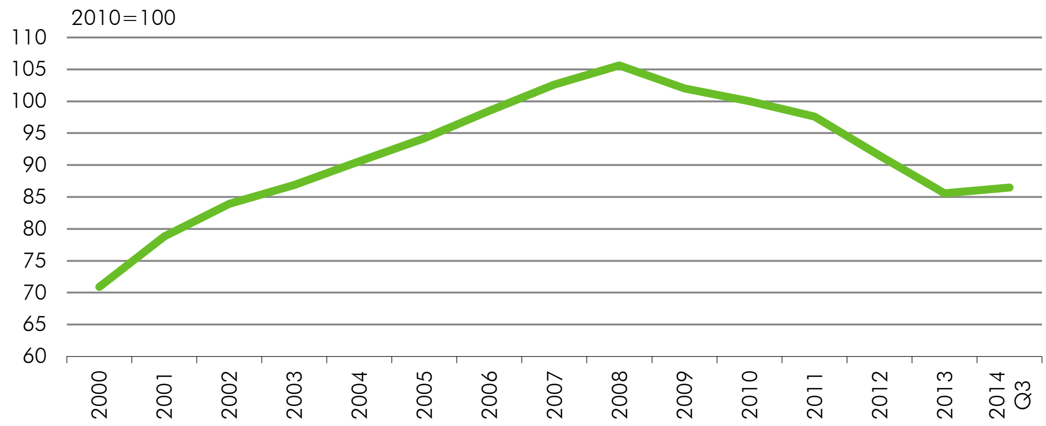
The Emergence of the Dutch Multifamily Market

Increasingly, multifamily residential in the Netherlands is appearing on the radar of international investors. This may not be a striking fact in itself, but one should bear in mind that until the end of last year, the Dutch housing market was essentially a closed, exclusive, and entirely domestic playing field. In fact, the commercial multifamily segment had become smaller and smaller over the years, squeezed between home ownership on the one hand and a strong social housing sector on the other, with both enjoying (indirect) government subsidies. It was a combination of government policies that had created this market structure many years ago. Now, triggered by austerity measures, new policies are rapidly opening up the market.

The "pincer" of private home ownership in the Netherlands was a result of fiscal stimulation; Dutch home owners are allowed to fully deduct the interest on their mortgage from their taxable income. This policy has prompted prospective buyers to borrow as much as possible, and has led to a situation in which the net monthly costs of a mortgage are generally lower than the monthly rent for a comparable dwelling.

After the financial crisis, tax losses and high personal indebtedness prompted the government to limit this stimulus. Since 2013, new mortgages have had to be amortized to allow for tax deductibility, and the maximum loan sum has been capped and will be gradually lowered. To international eyes these will not appear to be drastic measures, but the impact on the cost of borrowing, and subsequently on house prices, has been profound. From the summer 2008 peak through the trough at the end of 2013, house prices in the Netherlands dropped by nearly 20%. The drop was entirely caused by uncertainty and deleveraging, as demand pressure in the market—particularly in the densely populated western parts of the country—never abated. Most importantly, the higher cost of purchasing a home has provided a boost to the multifamily sector, with households turning to renting in increasing numbers.

Figure 1. Price Index of Existing Owner-Occupied Dwellings



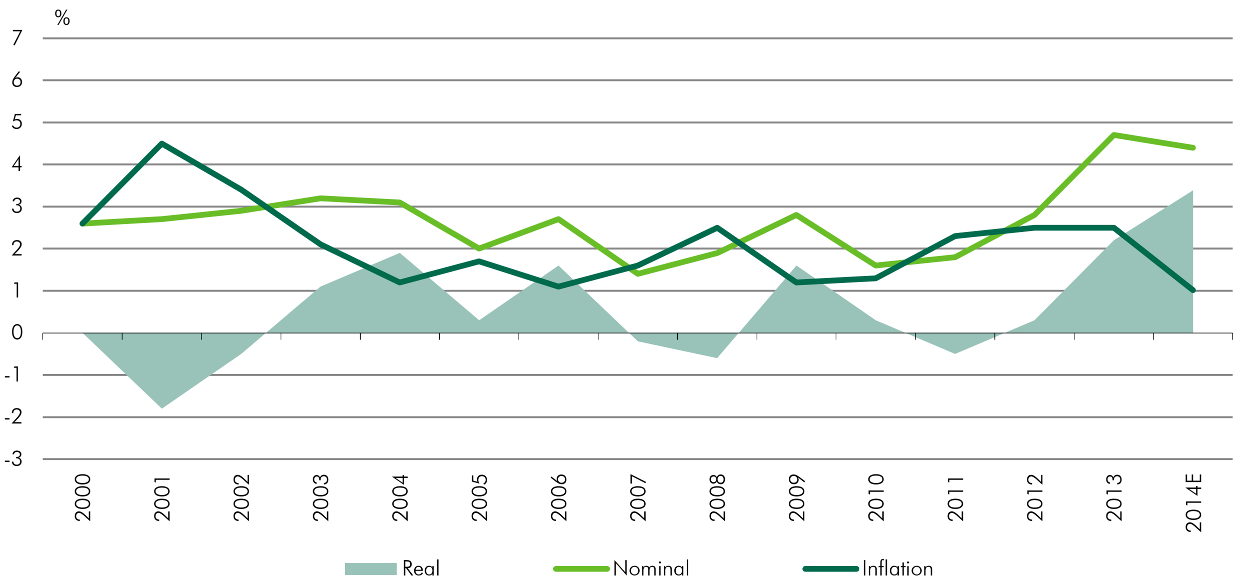
Sources: Statistics Netherlands; Netherlands Cadastre, Land Registry and Mapping Agency; Q3 2014.

Meanwhile, housing associations have come to dominate the other side of the housing spectrum. In the Netherlands these have evolved into non-membership foundations, and are therefore referred to as housing corporations. Due to strict regulation that limits rents, and a deliberate policy of leaving residential development in the hands of the corporations, they have become the dominant and sometimes quasi-monopolistic provider of rental homes. As a result, prospective tenants in many cities have had little choice but to sign up for the corporations' waiting lists, regardless of their actual need for social housing. Overstretched, the corporation sector has increasingly ventured into commercial side activities.

Before the crisis, this went mostly unnoticed; however, due to losses on their property and derivative portfolios, a growing number of corporations have fallen into financial distress in recent years. As a result, the government has taken a more activist approach, limiting corporations' activity to the provision of affordable housing to the lowest income groups. Also, an active policy to move higher-income households out of social housing has been developed.

The first step has been to no longer allow households that exceed a certain income threshold to enter social housing, which means they have to resort to commercial renting (or buy a home) instead. Also, a levy has been imposed on owners of social housing. Although this is generally seen as a treasury funding measure, the government has allowed the affected owners to implement income-dependent rent increases to help in covering the costs. This way, they are also prompting higher income groups to move out of social housing. Nationwide, the average rent increase was 4.5% in 2013, and it is anticipated to be 4.4% in 2014—rates substantially higher than inflation.

Figure 2. Average Annual Rental Growth in the Netherlands



Source: Statistics Netherlands, 2014.

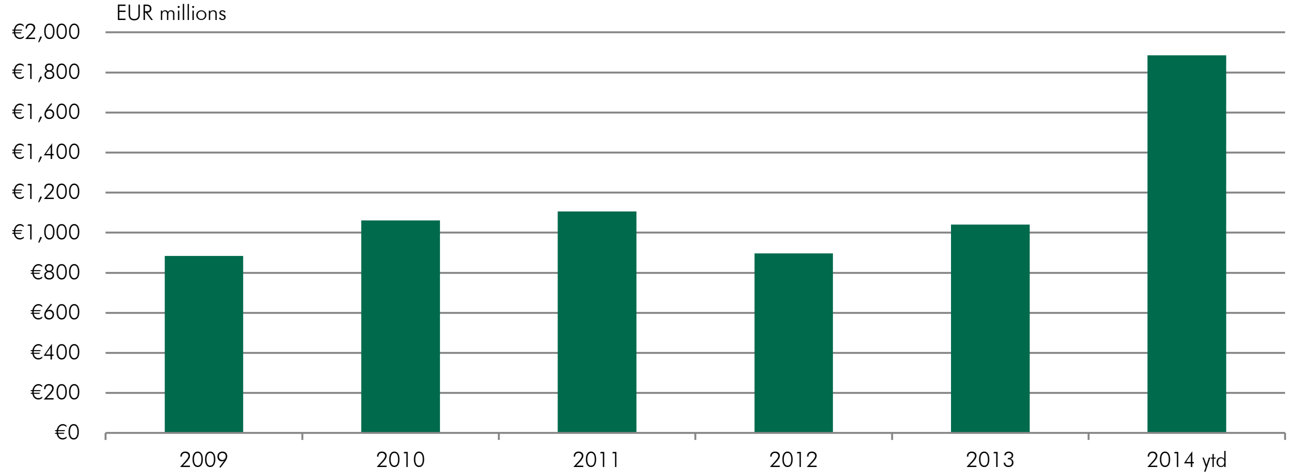
In summary, the restrictions on mortgage lending, which effectively make it more expensive to buy a home, and the active policy of giving higher-income groups incentive to move out of social housing, are accelerating demand for rental units in the multifamily segment. This demand is particularly manifest in cities and regions with strong demographic and economic pressure, such as the capital city of Amsterdam, and the central growth city of Utrecht. In Amsterdam, where the pressure is highest, developers have responded with a substantial number of new construction schemes.

The multifamily sector's growing scope and an increasing liquidity have not gone unnoticed by foreign investors. The past two years' strong rental growth is helping as well. Not surprisingly, the market has opened up, this year having seen, for the first time ever, the large-scale entry of foreign investors such as BNP Paribas and Round Hill Capital. The most eye-catching transaction was the purchase of a portfolio from distressed housing corporation

Vestia, comprising about 5,500 units. The German investor Patrizia seized the opportunity, investing more than half a billion euros.

Initially, Dutch institutional investors comprised the sell side of most of these portfolio trades, but this source is now drying up. Increasingly, housing corporation portfolios have to feed investor appetite. Also, eyes have turned toward the increasing number of multifamily construction schemes—particularly in Amsterdam, which has quickly become the prime market for single-block multifamily deals.

Figure 3. Annual Multifamily Investment Volumes in the Netherlands



Source: CBRE, 2014.

All in all, it is astonishing to see how quickly a number of selective government policy changes have opened up an entire market; although it was doubtlessly also fuelled by international capital market pressures. The process is by no means finished, and further growth in multifamily market activity can be expected.

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