Social Housing Finance in the Netherlands: the road to independence

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1. INTRODUCTION

The housing system of the Netherlands has acquired an international reputation, because of its special nature and the way in which it has evolved. Scholars from abroad are particularly intrigued by the strong position of Dutch social housing: in 2003, this sector still accounted for 35% of the total housing stock. In this respect the Netherlands clearly stands out; in most other West European countries this sector's share rarely reaches 20%. The strong position of Dutch social housing has its roots in the long period during which the national government influenced housing. Of course, for decades public intervention had been common practice throughout the region. However, the Netherlands eventually steered a course of its own. Whereas most other West European countries turned to privatization in the early 1970s, the Netherlands did not move in that direction until the 1990s (Boelhouwer & Van der Heijden, 1992).

Partly through this development, the social rented sector in the Netherlands can be said to have undergone a strong maturation. Thanks to some important policy adaptations in the 1990s, the social rented sector has also become much more independent. Housing associations are regulated by legislation much less than used to be the case. They do, however, remain retrospectively accountable to the government through the performances they deliver. In section 2, we consider the direction in which Dutch housing policy has developed and the role the social rented sector has played in general policy. We then consider in section 3 the unique manner in which the financial independence of the social rented sector has come about in European terms. Section 4 describes the opportunities for lenders outside the Netherlands. We end this contribution with some summary conclusions.

2. DEVELOPMENTS IN DUTCH SOCIAL HOUSING POLICY

The constant tension between government intervention and market influences becomes apparent when we study the development of the social rented sector in the Netherlands. Immediately after World War II the Netherlands had to deal with a serious housing shortage, in common with most Western European countries. The situation soon deteriorated, because of the rapid growth in the number of households and low production levels in residential construction in the early post-war period. The shortages that became apparent soon after 1945 made an exceptionally high level of government intervention in homebuilding programs broadly acceptable. Policymakers were faced with escalating costs, ranging from the cost of living to construction costs and interest rates. Thus, substantial object subsidies were needed to contend with the massive housing shortage. A high level of government intervention was called for; this was entirely fitting in a period when the welfare state was gaining ground.

In comparison with the rest of Europe, housing production in the Netherlands rose after the 1960s to an unprecedented level. This rapid rate of construction was necessary; during this period, as the number of households in the Netherlands increased much more rapidly than in the rest of Europe. The decline in the birth rate came to the Netherlands very late; there was also a postponed, but nevertheless intense decline in average household size. In contrast with the period before 1940, the need to build cheaply and quickly led to an emphasis on the social rented sector. These driving forces helped the sector to expand. The sector's share grew from 12% in 1945 to 41% in 1975 and to no less than 44% of the total stock by the early 1990s. No other Western European country attained such a high share.

The eventual turning point in Dutch housing policy was reached in 1989. The remainder of the new policy is strongly geared to the promotion of the market (Heerma, 1989). The Memorandum on Housing for the 1990s *[Nota Volkshuisvesting in de jaren negentig]* puts particular emphasis on deregulation, decentralization, and self-sufficiency. This new policy line includes the decentralization of authority. The transfer of responsibilities and risks from the State to the local authorities and provinces and the independence of housing associations and (organizations of) housing consumers are featured. For the housing associations, this shift meant that the existing regulations operating in advance were replaced by retrospective accountability (Heerma, 1989).

Financial freedom was also markedly increased in addition to freedom in terms of policy. The government decided to phase out the object subsidies for new construction as rapidly as possible. Rents in the period 1990-1994 were raised annually by 5.5%, a far greater margin than the general level of inflation, and this increase in revenue strengthened the financial position of the associations.

The Grossing and Balancing Operation constituted a second important episode marking the move towards financial independence. The State wanted at one and the same time to redeem the long-standing subsidy commitments (15.9 billion euro) and simultaneously call in early the loans that the associations still had outstanding (18,6 billion euro). In this way, the continuous pumping of money round the social housing circuit could be brought to an end. After intensive consultations with the sector, agreement was reached that the Grossing and Balancing Act would take effect in 1995. The advantages for the State were evident: savings were made on the object subsidies, the administrative bureaucracy could be substantially reduced, and the housing budget could be subjected to a stringent cleanout operation. Moreover, the State could take an independent position with respect to the housing association sector in the discussions concerning the annual rent increase. The Act also brought certain advantages for the associations. They traded in supposed savings at one and the same time, became capable through their greater independence of carrying out a more flexible and thus market oriented rental policy, and assumed new responsibilities in the management of their property. The increased rents and the Grossing and Balancing Operation have ensured that the associations have sufficient financial resources at their disposal to be able to carry out the housing task quite independently. In the Netherlands this is referred to by the term *revolving fund* (Ekkers, 2002).

The government considers the social rented sector in its entirety as a revolving fund that should be capable of functioning without government subsidies. The idea of a revolving fund implies that current and future reserves generated in the social rented sector are put to use within that sector; in this manner, the housing associations subsidize themselves. The revolving fund applies both to the sector as a whole and to the individual associations. Each of them has to use the yields of their operations in the current stock to pay for (non cost-effective) new instruments in the quality of the stock, new construction, and improvements in liveability. For the sector as a whole, the yields of the prosperous and the poor associations can be balanced. Prosperous associations could, for instance, support their poor relations by lending them the funds they need at below-market interest rates. There may also be a role for the Central Housing Fund *[Centraal Fonds Volkshuisvesting]* (CFV) (see below). The annual contributions of the associations to this fund have created a situation that enables the CFV to manage a substantial part of the sector's assets. These could be used to set up a revolving fund in the sector. This principle is already being applied whenever the CFV provides financial support to an association in financial straits. If the sector succeeds in operating as a revolving fund, it will create the unique situation of a social housing system that is no longer dependent on extensive public subsidies (Gruis, 1997, p.12).

3. FINANCING OF THE SOCIAL RENTAL SECTOR

Until the beginning of the 1980s, the financing needs of the Dutch housing associations were covered via loans granted by the State. These loans exerted a direct pressure on the national budget. In the 1980s, the government came into serious financial problems, saw the national debt rising rapidly, and so decided in 1984 to abolish the provision of loans to associations and also the counter-guarantees provided by the State for loans borrowed on the capital market. In 1983, the Social House-building Guarantee Fund (WSW) *[Waarborgfonds Sociale Woningbouw]* (WSW) was set up as a private law institute to enable the financing needs of associations to be covered. At first, only guarantees for housing improvement were concerned. Five years later, it also became possible to obtain guarantees for the financing of the construction of new dwellings. The WSW endeavours to provide the participating associations with access to the capital market at the lowest costs. Since that time, the WSW has granted guarantees to moneylenders for loans for new construction, housing improvement, the acquisition of dwellings and nursing and retirement homes. The WSW is not, however, the only institute that makes guarantees available. Local authorities also grant guarantees for housing associations' loans, albeit on a limited scale.

If housing associations borrow with loan guarantees provided by the WSW, there is a triple guarantee. The primary security is formed by the financial resilience of the association itself and of the entire sector through the participation of the Central Fund (see below). The secondary security consists of the capital assets of the WSW, which are created by a single capital contribution from the State and the fees the associations pay to obtain guarantees. The tertiary security is formed by the ultimate responsibility of the State and the local authorities that share this task equally (Van der Schaar, 1991, p.404). The attractive interest rates on loans secured by the WSW demonstrate the great confidence that lenders have in the fund. Their confidence is largely due to the ultimate security provided by the State (Priemus, 1995).

In the last few years there has been some discussion concerning the legal force in a European perspective of this safety net function of the State and suggestions have been put forward to impose a levy on the interest advantage acquired. According to the WSW, whenever the EU perceives the safety net function as a form of State support, it considers it in any case to be permissible (WSW, 2002, p.1).

A housing association wishing to use the facilities of the WSW must first register with the fund. Before the WSW approves an application, it tests the creditworthiness of the applicant. As of 1995, the evaluation of the financial position of an association is based on its assets. Its solvency position must be positive if it is to be admitted. This implies that the securities provided by the WSW to any association have to stay below a set ceiling. This amount is determined annually by subtracting the loans an association has borrowed from its total assets (Gruis, 1997, p.18).

It is of great importance for foreign financiers that, for loans provided under WSW-guarantee, the 0% solvency requirement applies and that mortgage banks may use these loans as security for the issue of, for example, mortgage bonds. Since the end of 2002, the 0% solvency requirement has also applied to loans borrowed in Germany, France, and Luxemburg. The WSW has submitted a similar request in the other EMU countries.

The WSW has been awarded two ratings. Both ratings are stable, dating from 1997 and 1998 respectively: Standard & Poor's AAA rating, and Moody's Investors Service Ltd Aaa-rating. Both are the highest possible ratings and have a 'stable prospect' (WSW, 2003).

At the end of 2001, of all the 620 social landlords 591 were registered with the WSW. This number represents about 90% of all the housing associations in the Netherlands. The total secured capital of the WSW had risen by the end of 2002 to almost 54 billion euro. This means that the WSW secured more than 90% of the financing for a period of two years or more within the social housing sector. In 2001, loans amounting in total to about 4 billion euro were borrowed with direct security. For almost 95% of them this borrowing took place directly on the private market. As far as is known, the services of mortgage brokers are used for almost 13% of the transaction entered into. At about 78%, fixed interest loans have the greatest market share (WSW, 2003).

In addition to the WSW, the Netherlands has a second important institute: the Central Housing Fund *[Centraal Fonds voor de Volkshuisvesting]* (CFV). This fund is responsible for two important tasks: financial supervision (since 1998), and financial reconstruction (since 1988). Associations in a poor financial position can appeal to the CFV for assistance.

The CFV is a mutual fund established by and for the associations. Its purpose is to support financially weak associations and, where necessary, help them restructure their operations. To this end, each association contributes annually to the fund. The size of the contribution required from an association is calculated on the basis of its financial situation and, since 2001, whether it has given financial assistance to another association that does not have enough capital to finance some specific project. An association that fails to qualify for (further) participation or guarantees from the WSW can appeal to the CFV for help. The CFV will provide an interest-free loan to an impoverished association on condition that it becomes self-supporting within three years. Sometimes, this condition requires the restructuring of an association. In many cases, its management is taken over by a member of the CFV. In principle, the CFV contributes half the cost of such an operation. The other half is usually borne by the local authority that is also ultimately responsible for housing. The conditions imposed by the CFV for support closely reflect those operated by the WSW in assessing an association's creditworthiness (Gruis, 1997, p.18). In the ten years or so of its existence, financial support amounting to over 480 million euro has been granted to seventeen housing associations.

In addition to its financial reconstruction task, since 1998 the CFV has also undertaken a supervisory task that features early-warning monitoring. Through the fund's timely signalling of an association's financial weakness to the national government, it can intervene as a formal supervisor. As a result, as far as possible any financial problem affecting an association can be avoided. In this context, the CFV has been given a number of specific new tasks. In the first place comes the signalling task related to the assessment of the likelihood of future cases needing financial reconstruction. For this purpose, the CFV compiles reports on the financial position of individual associations. These reports are based on the associations' annual reports and supplementary information they may provide. Furthermore, the CFV advises the State over the financial aspects of new admissions, mergers, and any changes in the statutes. The CFV also reports each year on the financial situation of all the associations taken as a whole. It was announced that the financial position of the sector in the 2001 financial year could be considered to be healthy. Taking the financial assets into account, the associations' housing property is financed to the extent of 74% with long term-borrowed capital. According to the CFV, the own capital of the 620 associations, who together own more than 2.4 million rental dwellings, has risen by almost 0.7 billion euro to 8.8 billion euro. On the basis of their business plans, the associations expect their own capital to grow further to 12.3 billion in 2005. Partly on the basis of this development, the number of associations that can be considered financially weak has further declined. The number of the associations applying to the CFV with a request for support in financial reconstruction confirms this picture (CFV, 2002, 2003).

In addition to the two national sector institutes WSW and CFV, certain individual associations also undertake activities to provide for their financing requirements. An example is ColonnadeDuhaf, created in February 2002 as a joint venture of Colonnade N.V. and DuHaf Holding B.V. Twenty-five associations came forward as joint shareholders. In fact, non-shareholders may also take part in an issue. In this manner the associations have available an issue canal of their own and direct access to the capital market without the intervention of brokers or banks. As a result, the number of market providers of capital is extended, thereby creating more competition and keeping the rates under pressure.

ColonnadeDuhaf combines the associations' demand for capital into units of half a million euro and issues the total amount as debenture on the European capital market. ColonnadeDuhaf do that exclusively for loans secured by WSW, so that the debenture acquires the highest rating and consequently a low interest rate. The loan is placed on the capital market by one or more international banks. The organization passes on the loans acquired on the open market, without any form of risk in terms of interest rates, currency exchange rates, or time, to the commissioning housing associations. In that way, the organization fulfils a bridge function between the housing associations and the European capital market. In the period between June 1988 and March 2003, ColonnadeDuhaf made in total more than 1.6 billion euro available for the housing association sector. There have been 16 issues, in which the organization has bundled 122 transactions for the housing associations. The last issue took place on 4 March 2003. This brought in 134 million euro for 11 housing associations. The associations pay 4.15% for a 10-year loan. This rate is just 6 basic points above the SWAP rate (ColonnadeDuhaf, 2003).

4. OPPORTUNITIES FOR LENDERS OUTSIDE THE NETHERLANDS

As described above, the Dutch housing associations are still quite active on the building market and also in the process of restructuring urban areas. An OTB-survey in 1996 estimated that the capital needed by the social-rented sector for investments will remain substantial during the next few years, amounting to 2 to 3 billion euro per year (Gruis, 1997, p.19). So, there are clearly opportunities in the Netherlands for activities by foreign lenders. The market for loans to housing associations in the Netherlands is also wide open for foreign investors. Thanks to the guarantees available through the WSW and the role of the CFV, loans to housing associations are a safe investment. Nevertheless, this overall positive image should be seen in a certain perspective. In the first place, sufficient financing is available for all providers of social rented housing in the Netherlands, which implies that the market for foreign lenders is limited and the competition will be tough. Mainly due to the Dutch housing system, there are institutional investors in need of investment opportunities. Yet in view of the scope of their investment portfolio, Dutch investors are not always willing to lend to housing associations. In the second place, the very limited risks lead to a yield that is only fractionally higher than the rate paid on Dutch government bonds (Gruis, 1997, p.19).

At the moment, housing associations are mainly getting their loans from two banks: the Bank for Dutch municipalities (BNG) and the Waterschapsbank (a semi-public body). ColonnadeDuhaf was initiated to get more competition on this market. One of there main goals is to be sure that the conditions of the BNG and the Waterschapsbank stay at a competitive level and to keep the rates under pressure. To underpin there efforts, more competition from outside will surely be welcome.

5. CONCLUSIONS

This contribution has shown the uniqueness of the maturation of the Netherlands social rented sector in an international perspective. Not only does the Netherlands have, with 35% of the total housing stock, far and away the largest social rented sector (followed at a respectable distance by the United Kingdom with 21%), but also independence and substantial accumulated capital in the existing stock. Thanks to the opportunities of rent pooling, the input of the accumulated capital, and the freedom to dispose of real estate so that capital invested in bricks and mortar can be put towards other objectives, the housing associations are able to rent out newly constructed social rented dwellings at well below cost price. The usual unprofitable top of 50,000 euro for the construction of a social rented dwelling is currently substantially higher than the object subsidies that the State government granted at the beginning of the 1990s.

Financing needs can also be met entirely via the WSW so that, in addition to being able to obtain sufficient capital, borrowing on the international capital market is against keen rate competition. This unique situation has been brought about through mutual cooperation and solidarity, and not least through the safety net function of the State. Impoverished associations are also restructured via the CVF through the sector itself.

For the future, however, the strong financial position of the associations may also constitute a danger. Now that the national government is being threatened by financial heavy going because of the flagging economy, politicians in particular are looking covetously at the associations' accumulated capital. Following up on the thought that this capital was to some extent built up through earlier subsidies, the associations' task package has gradually been extended. The broad concept of *liveability* has now been added to the original four strongly housing-related task areas. Furthermore, proposals are being put forward to enforce a creaming off of a share of the capital of the more prosperous associations to invest it in tasks in urban areas on behalf of less prosperous associations, or even to use the surplus capital for activities other than housing (including infrastructure). The tenants in the social rented sector who enjoy a somewhat higher income are also being regarded with a critical eye. Serious consideration was given in cabinet negotiations in the spring of 2003 to the imposition of a rental tax, or a hefty rental increase on these groups, so that more public resources could be made available.

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