

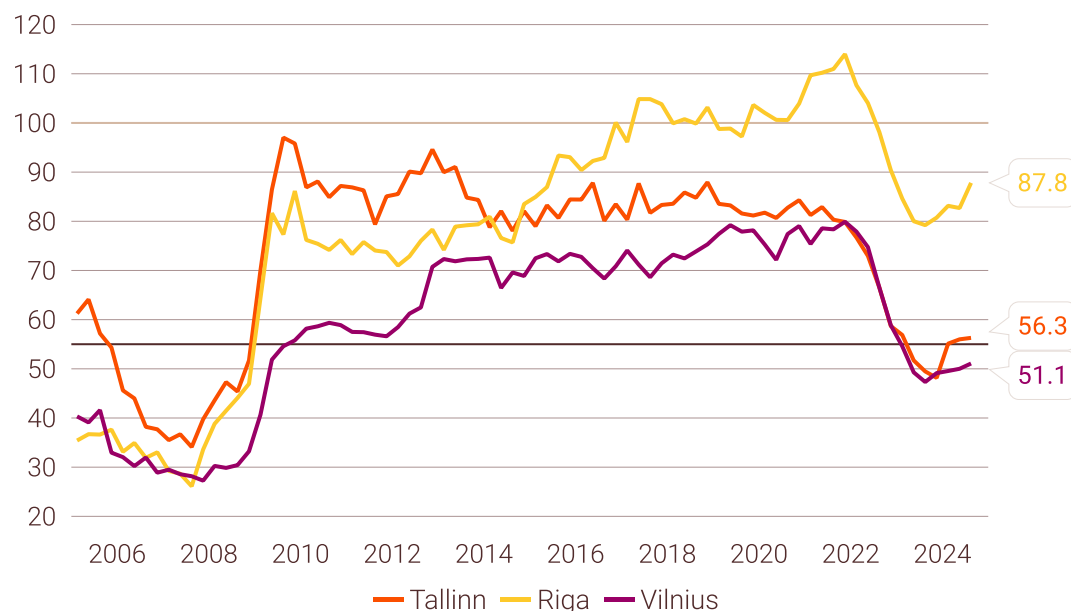
# Baltic Housing Affordability: 2024 Q3

## The road to recovery continues

- With interest rates falling faster than expected and wage growth remaining strong, housing affordability gradually improves.
- Both factors will continue boosting affordability and demand in Latvia and Lithuania next year, while Estonia will rely solely on lower rates.

### Baltic Housing Affordability\*

Size of an apartment that an average household can afford to purchase with a mortgage, m<sup>2</sup>



\* Last quarter's value is preliminary and subject to change.

The line at 55m<sup>2</sup> indicates the average size of apartment typically bought in the Baltic capitals.

Sources: Swedbank Research & Macrobond

Example: 56.3 m<sup>2</sup> represents the apartment size that an average household in Tallinn can afford, given 1.5 times the average net monthly wage, the quarterly average apartment price, and the interest rate for new loans.

Favourable inflation readings and a weak economy have already led to three rate cuts by the ECB. Paired with strong wage growth, this has improved housing affordability in the third quarter in the capitals of the Baltic states. Affordability in Riga was supported also by a slight decline in average market price. An average-sized apartment in the primary market, however, remains out of reach for the average household across the Baltics.

Market activity is picking up, while the number of transactions per capita is nearly identical across the cities. Consumer confidence in Lithuania and Latvia continued to improve, yet it waned in Estonia after a promising start to the summer.

We expect another 25-basis-point rate cut by the ECB in December. The deposit rate, which is closely followed by the EURIBOR, will gradually decline to 1.75% by next September – the expected low point in this cutting cycle. Therefore, lower rates are likely to continue to boost activity and housing affordability in the Baltic countries. Tax changes in 2025, however, will differentiate the pace of recovery. Higher taxes will result in comparatively negligible net wage growth in Estonia. Conversely, in Latvia, the shift from a differentiated to a fixed non-taxable minimum will push net wage growth up. In both Latvia and Lithuania, net wage growth is expected to exceed 8% – lower than before, yet still a rapid tempo.

#### Analysts:

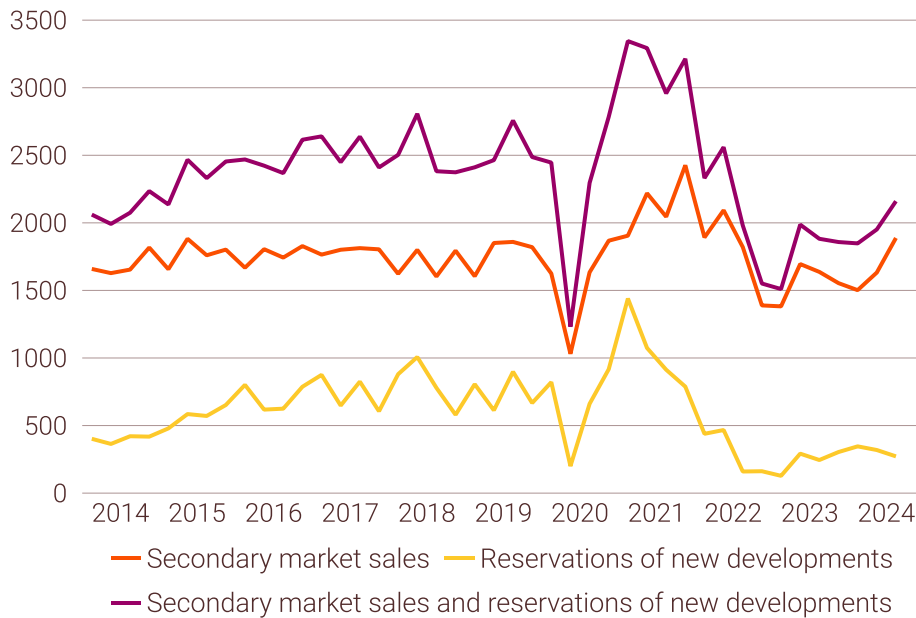
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# Tallinn – falling interest rates will be the main tailwind for demand in 2025

## Tax increases will dampen the growth of net wages next year

### Tallinn market activity

Number of apartments per quarter

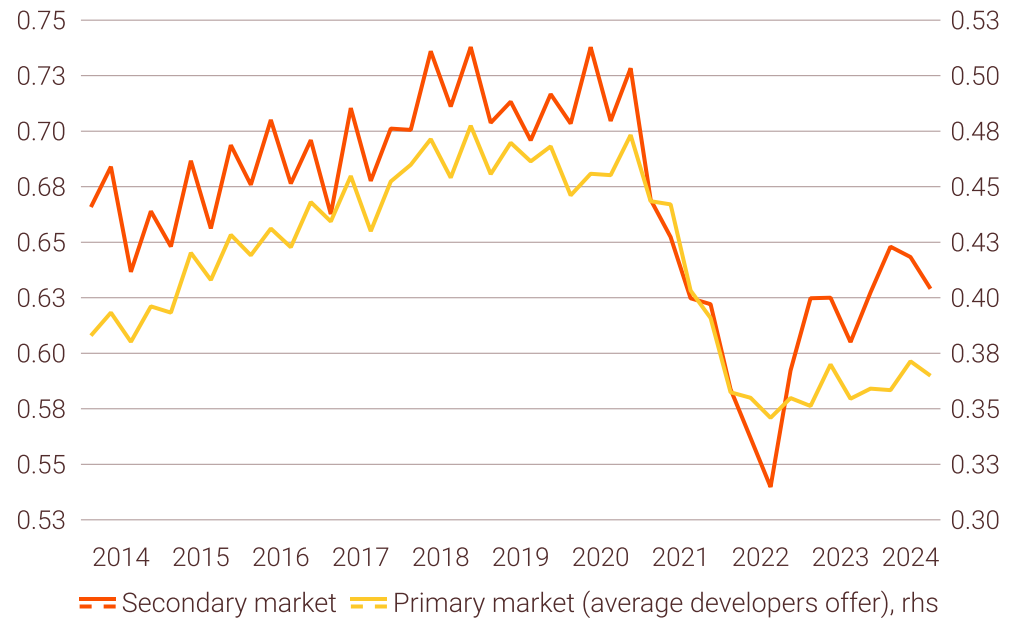


Sources: Swedbank Research & Macrobond

- Market activity showed some signs of improvement in the third quarter, as housing affordability was supported by falling interest rates. Sales in the secondary market increased over the year and were stronger than in the first two quarters of this year. Meanwhile, reservations in the primary market were still muted, although higher than last year.
- Sales of relatively new and more expensive apartments in the secondary market were larger than in previous years, as households were looking for alternatives to the out-of-reach primary market. The share of new developments in total transactions remains at the lowest level in 10 years.

### Purchasing power of a monthly wage in the housing market

m2 of apartment affordable with an average monthly wage



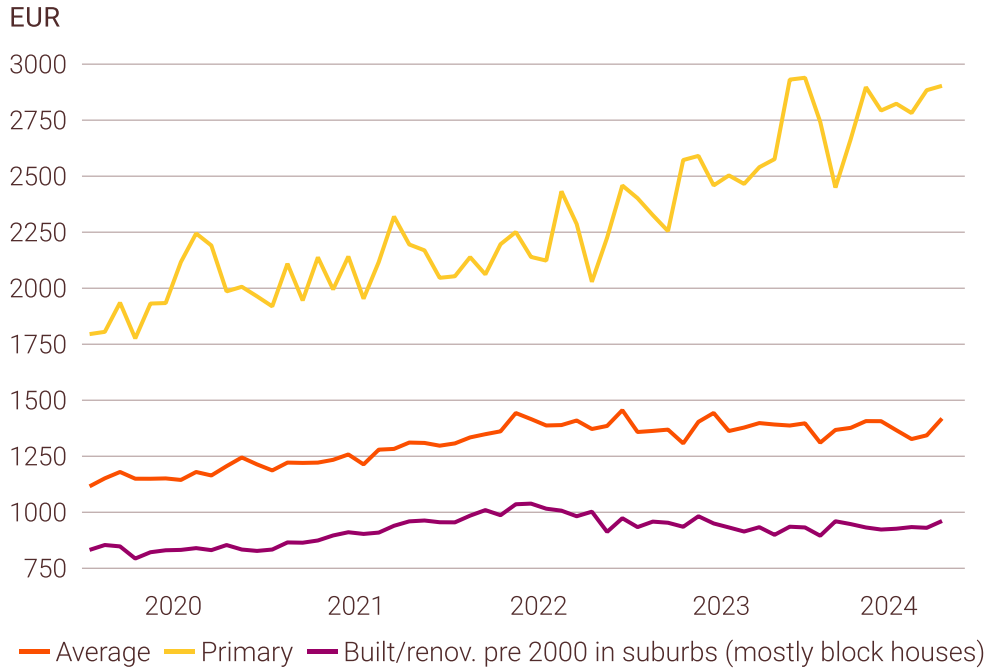
Sources: Swedbank Research & Macrobond

- Annual price growth in the secondary market slowed to 2.6%. Online listings of developers showed a deceleration of annual price growth to 3.7% in the primary market. However, official registry data reflected some negotiated price discounts, as prices of new developments were down by 1.6% over the year.
- In 2025, we expect interest rates to continue to decline and support housing affordability and demand. However, the improvement of demand is likely to be gradual, as tax changes have hurt households' confidence and will slow the growth of net wages next year. While overall supply in the housing market has risen in the last couple of years and peaked recently, improving demand means that homebuyers' negotiating power over the price will gradually start to diminish.

## Riga – interest rates lower, activity slightly higher

With interest rate burden easing and wage growth outpacing that of prices, affordability increases

### Prices of residential apartments in Riga

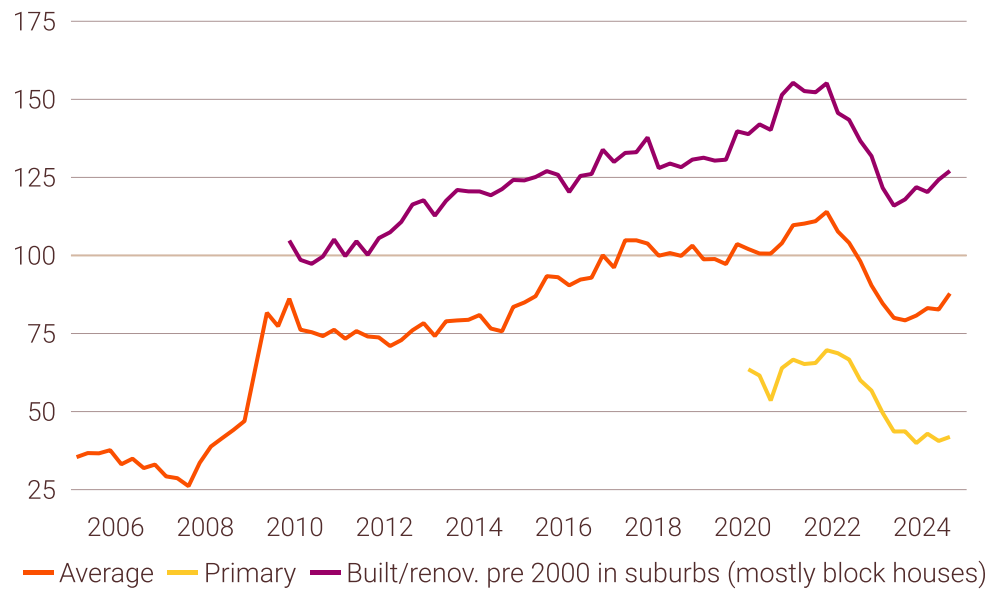


Sources: Swedbank Research & Macrobond

- The stars are seemingly starting to align in favour of new homebuyers. In the third quarter, the average apartment price fell both in respect to the previous quarter and the third quarter of last year. Wage growth, although decelerating, remained strong. Lastly, interest rates finally fell more pronouncedly, although the interest rate Latvian households pay is still higher than in Estonia and Lithuania.
- The housing market is warming up, although the primary market is still in dire straits. Reservations for new apartments are down and the stock of unsold apartments increased even further. Some new projects, however, have managed to balance the price-quality ratio and attract notable interest (for example, via soft reservations). This implies that interest in the primary market has not disappeared.

### Housing affordability in Riga

Size of an apartment that an average household can afford to purchase with a mortgage, m<sup>2</sup>



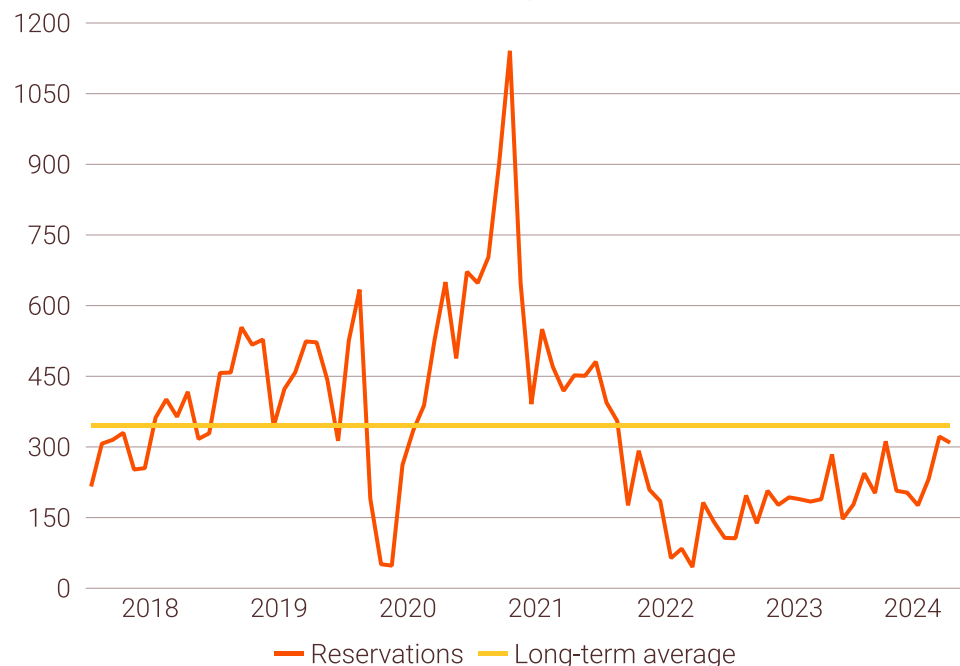
Sources: Swedbank Research & Macrobond

- Nevertheless, affordability has not improved much yet, and new apartments are still too pricey for the average household.
- Those who are not satisfied with the quality of comparatively three times cheaper block house apartments have to wait and shop around as the stock of well-priced, good-quality secondary market apartments is still low.
- Consumer confidence reached a three-year high. Wages are expected to grow even more, with the labour tax reform lifting average net wages. Rates are declining faster than expected. The future does look brighter for the housing market.

# Vilnius – market activity strengthens, yet affordability creeps up slowly

## A boost of optimism driven by lower interest rates and strong wage growth

Apartment reservations, Primary market, Vilnius



Sources: Inreal, Swedbank Research & Macrobond

- According to the official registry, secondary market sales edged higher, while new apartment sales also recorded a modest increase. The share of new apartments in total sales rose slightly to 31.5%, yet remained at its lowest level since 2021. Meanwhile, reservations in the primary market have increased and are now approaching the long-term average.
- Official registry data also indicate a gradual increase in prices. Apartment prices rose by nearly 8%, though this figure is somewhat inflated by delayed registrations of new apartments. Alternative data suggest that prices are remaining at roughly the same level as last year.

Repeat sales house price index and wage growth, Vilnius



Sources: Swedbank Research & Macrobond

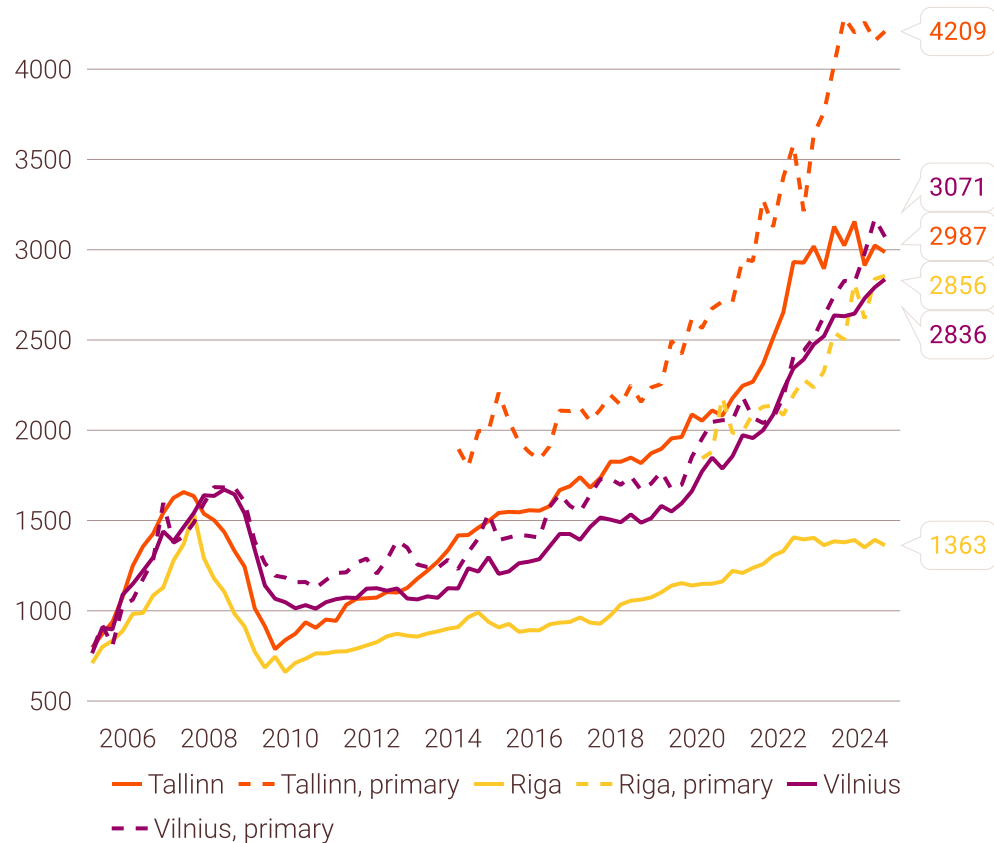
- Affordability has improved only modestly so far. Buyers on average could afford to buy a 51.1 m<sup>2</sup>-sized apartment in Vilnius, 1.1 m<sup>2</sup> larger than in the previous quarter. Wage growth continued to outpace price increases, while interest rates maintained their gradual decline. Affordability should improve going forward.
- The stock of unsold apartments has dropped somewhat but still remains at the highest level in five years. Although the number of construction permits issued fell, for now the number of completed apartments is still relatively high – supply should remain quite abundant. This improves the odds that a reduction of interest rates would bring back housing demand without excess price growth.

## Appendix

### Wages still noticeably outpacing yearly housing price growth

Average apartment price

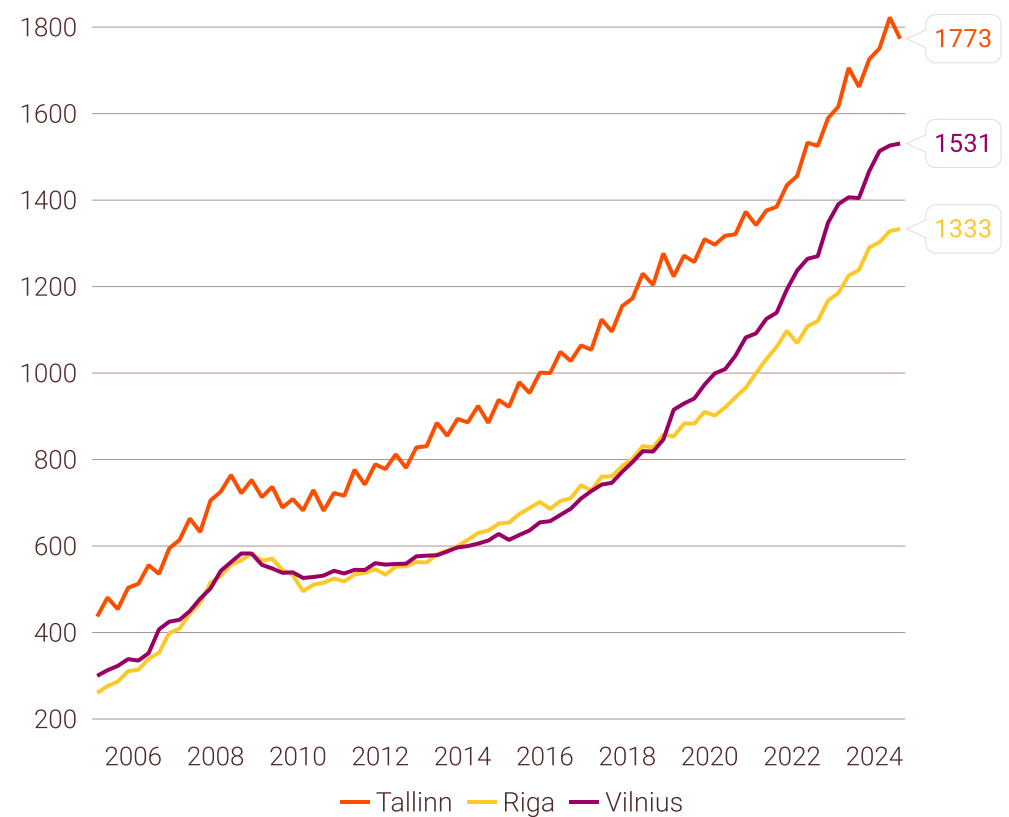
EUR/m2



Sources: Swedbank Research & Macrobond

Average monthly net wage\*

EUR



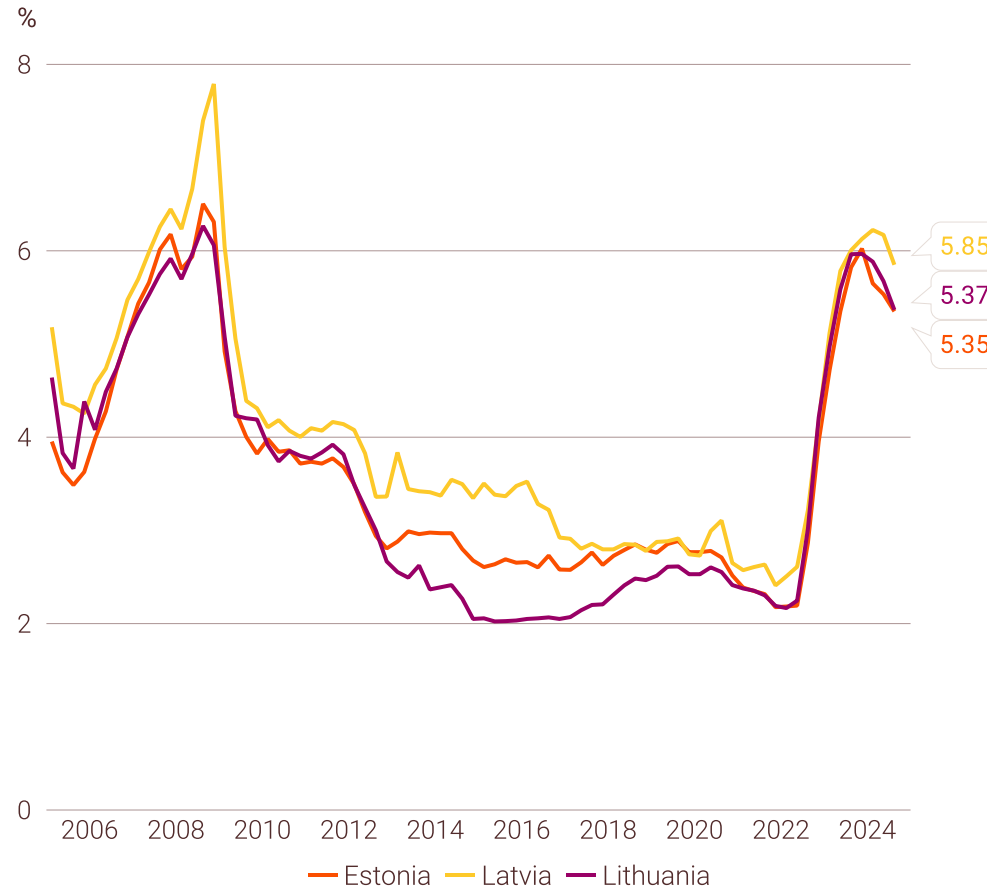
\* An estimate for the last quarter

Sources: Swedbank Research & Macrobond

## Appendix (continued)

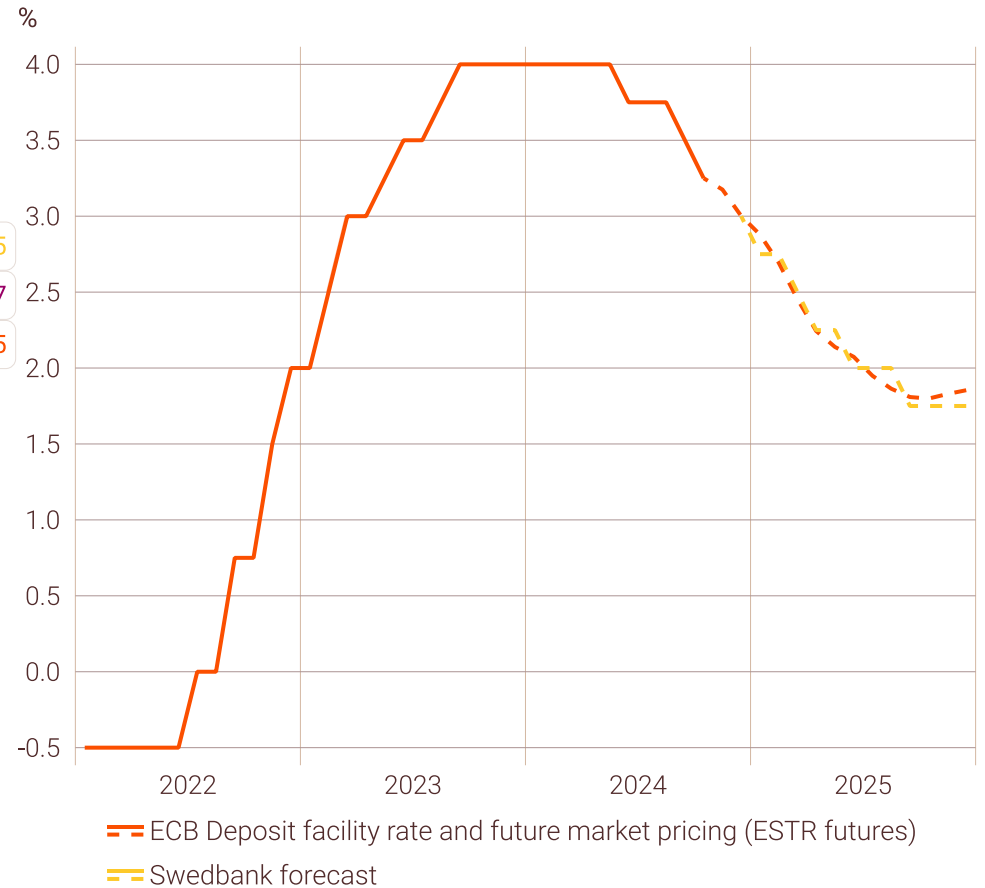
Rates are falling; the rate in Latvia still higher than in Estonia and Lithuania

Annual % rate of charge for new mortgages to households



Sources: Swedbank Research & Macrobond

ECB rate market expectations and forecasts



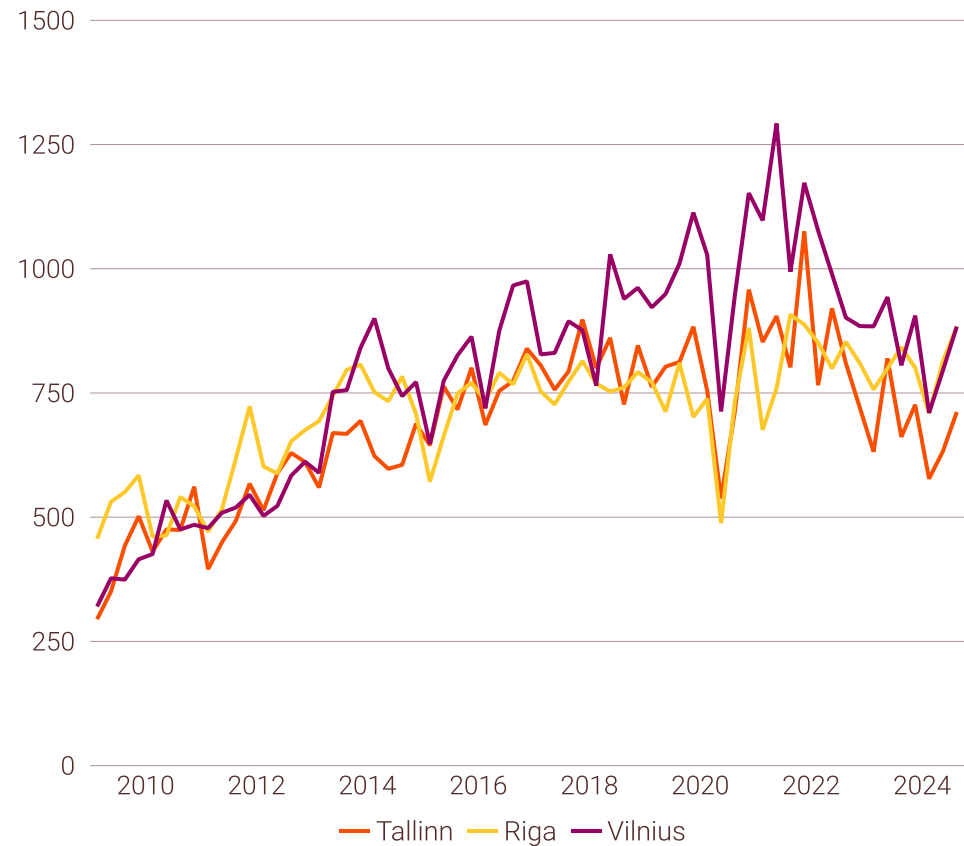
Sources: Swedbank Research & Macrobond

## Appendix (continued)

### Activity slightly higher; consumer confidence in Estonia deteriorating

#### Apartment transactions

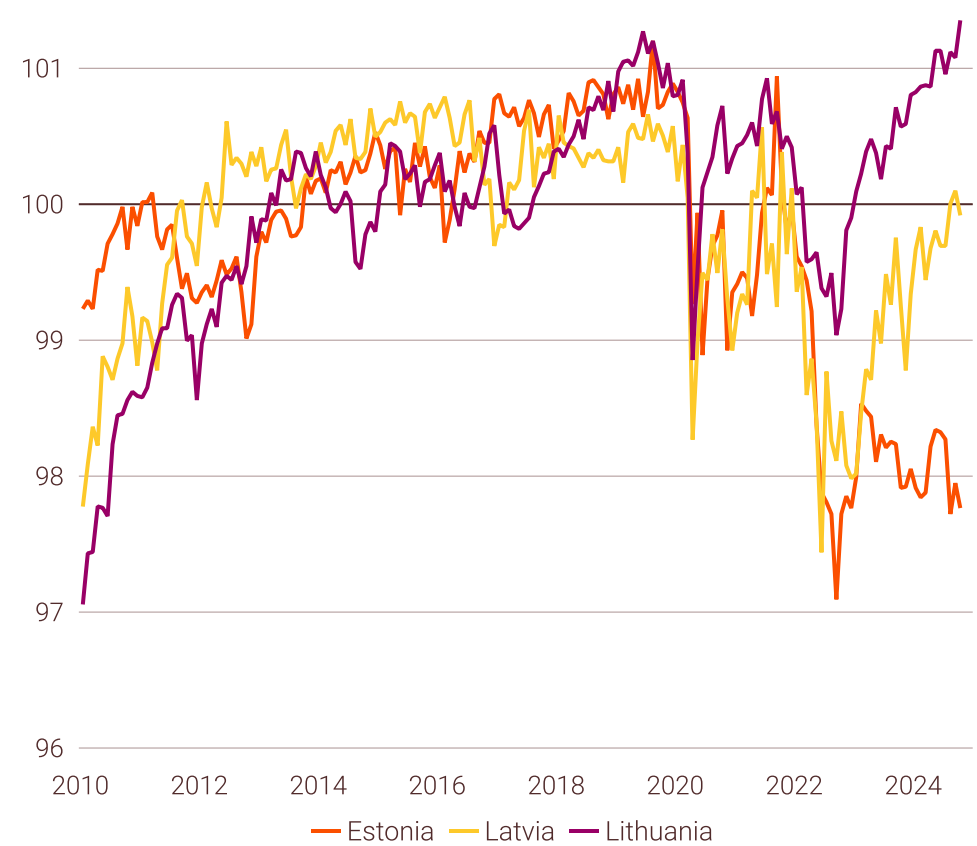
Number per month, quarterly average



Sources: Swedbank Research & Macrobond

#### Consumer confidence

Standardized, 100 = long term average



Sources: Swedbank Research & Macrobond

## Baltic Housing Affordability: Methodology

### Objective

The Baltic housing affordability (henceforth, HA) measures the size of an apartment that an average household can afford to buy with a mortgage in the Baltic capitals.

### Norm (the main assumption)

Household monthly mortgage payments do not exceed 30% of household income.

### Variables

- Average apartment price per m<sup>2</sup>: three-month average apartment transaction price per m<sup>2</sup> in Baltic capitals.
- Household income: 1.5 of average monthly net wages in Baltic capitals.
- Mortgage interest rate: three-month average annual percentage rate of charge (including interest rate and other related charges) for new housing loans to households, issued in euros, in the Baltics.

### Other assumptions

- Average apartment size: 55 m<sup>2</sup> (our benchmark).
- Down payment: 15% of total apartment price.
- Term: 30 years.
- Saving rate for down payment: 30% of household income.

### Calculation of HA

The HA shows how many square meters of an apartment a household can afford, given it uses 30% of its income to service mortgage payments.

$$HA = \frac{\text{AverageINC}}{\text{NINC}}, \text{ where } \text{NINC} = \frac{\text{PMT}}{30\%}$$

where  
 AverageINC – household income,  
 NINC – household income that satisfies the norm,  
 PMT – monthly mortgage payment.

### Limitations

The HA provides an indication of the average household situation, not that of a particular household. Household income and mortgage interest rates faced by a particular household may differ from those presented in the report. The HA accounts for mortgage costs but excludes taxes and subsidies, including property tax and interest deductions. It also does not consider other household expenses that could affect the household's ability to service mortgage payments, such as rent, lifestyle, or existing liabilities. The HA does not provide any direct guidance for business decisions, including lending and interest rate decisions.

The average apartment price per m<sup>2</sup> reflects past transactions and does not necessarily indicate the potential affordability or price of apartments in the future. Differences in apartment segment structure and the physical condition of newly built apartments at the time of purchase might affect the comparability of the average apartment price per m<sup>2</sup> across the Baltic capitals.

The HA is of an informative nature and reflects macroeconomic developments, rather than banks' decisions and lending policies or the potential behaviour of individual households.

### Change of methodology

Starting in 2024, instead of expressing HA as an index, the report was changed to highlight the size of apartments afforded. Otherwise, the methodology is unchanged; the switch is purely for ease of interpretation purposes.

### Frequency

Quarterly.



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