



> WHITE FUTURE FOR THE MORTGAGE INDUSTRY?

The Federation was delighted to welcome over 240 participants to its Annual Conference 2007, including 39 as speakers or panelists from 28 different countries, both from within and beyond the EU. In recognising the huge success of the EMF's 5th Annual Conference, which also marked the 40th Anniversary of the EMF, the

The President then introduced **Elemér Tertak**, Director at DG Internal Market and Services, who, having very kindly agreed to replace his Director General Jörgen Holmquist gave participants an overview of the Commission's work to integrate retail financial services in the context of its new European strategy to reinvigorate the single market.



Pasquale Giamboi,
President of the European Mortgage Federation

Mr. Tertak focused first on the creation of efficient and competitive markets and highlighted the need to remove the legal infrastructural obstacles that mortgage lenders face when seeking to offer their services cross-border. He did however stress that many obstacles encountered have been designed to protect consumers and/or preserve financial stability, such as rules on early repayment, and that as such the Commission is faced with the challenge of balancing lenders' and consumers' needs. Mr.

Tertak also highlighted the close link between primary and secondary markets and in this context made reference to the recent subprime crisis as clear evidence of this. He did however stress that it would be wrong to make hasty decisions or introduce regulatory measures in the wake of the turbulence. Instead, he referred to the 15 ECOFIN initiatives, which he felt recognises the need for a period of reflection.

Mr. Tertak then turned to the role of the consumer and stressed that financial education is high on the Commission's agenda, because efficient markets depend on confident and empowered consumers. In the same vein, Mr. Tertak considered the role of information and suggested that information currently provided

White future for the Mortgage Industry?.....1

Panel 12

Panel 24

Panel 35

Panel 46

Panel 57

Panel 68

Federation would like to extend special thanks to the speakers, moderators, panelists, its members as well as its lead sponsors, PMI Europe, Business Architects, AIG United Guaranty, Banca per la Casa, vdp, CML and EULIS and, finally, its media partners, Mortgage Finance Gazette, Mortgage Risk and Lending Strategy, for their contributions and support.

The first day of the Conference kicked off with a welcome speech by **Pasquale Giamboi** of Banca per la Casa - UniCredit Group in Italy and President of the European Mortgage Federation, who touched upon the key issues that the Conference would be addressing and briefly reviewed the economic development of mortgage markets in the past year.



Elemér Tertak,
Director at DG Internal Market and Services.

«...efficient markets depend on confident and empowered consumers...»



to European consumers is insufficient and that the Code of Conduct is outdated. He also stressed that price transparency is impeded by product tying and noted that the Commission would be investigating this and other similar practices in all financial services areas.

Turning to responsible lending – and responsible borrowing – Mr. Tertak acknowledged that while cases of misselling such as in the US are rare, they can and do occur and as such explained that the Commission is considering a range of measures to encourage responsible lending. Finally, Mr. Tertak touched upon credit intermediaries and the fact that they are increasingly viewed as a way to promote integration. Given the many questions surrounding the appropriate

« The White Paper will set out the Commission's strategy for improving the competitiveness and efficiency of EU mortgage markets by ensuring competition, and by going after any unfair or unsavoury practices, by increasing transparency and by empowering and informing the individual consumer.»

level of regulation for intermediaries, particularly in the wake of the US subprime crisis, the Commission will be launching a study on the EU credit intermediaries market, which will be ready by autumn 2008.

To conclude, Mr. Tertak noted that the forthcoming White Paper will set out the Commission's strategy for

improving the competitiveness and efficiency of EU mortgage markets by ensuring competition, and by going after any unfair or unsavoury practices, by increasing transparency and by empowering and informing the individual consumer. He added that everyone, consumers and business alike, stands to gain from this.



From left to right, Bernhard Scholz, Mike Bradford, Michael Coogan, Annik Lambert, Eric Ducoulombier & John Purvis.

PANEL I

Mr. Tertak's frank and insightful presentation was followed by the first panel session of the Conference, aptly entitled "What Future for the Mortgage Industry in Europe?". Moderated by **Annik Lambert**, Secretary General of the EMF, the panel focused on an expression of views from the European Commission, the European Parliament and the Industry on the

possible content of the upcoming White Paper on Mortgage Credit.

MEP **John Purvis** was the first of the panelists to express his views and in his opening words he focused on the recent US subprime crisis. Significantly, he emphasised that 'subprime' should not be considered a 'dirty' word and considered it important to pursue the socio-economic route in order to ensure access to housing – he noted that

unfortunately this was not the case in the US. **Eric Ducoulombier**, Deputy Head of Unit at DG Markt, was up next and confirmed that the White Paper will contain proposals for a policy mix and that there will be proposals for a regulatory element, which will of course be preceded by a targeted impact assessment. In his introductory statement, **Mike Bradford**, President of the Association of Consumer Credit Information Suppliers, stressed that in its White Paper the Commission should focus on the removal of structural barriers which hamper lenders from entering markets and doing business. **Michael Coogan**, Director General of the CML in London, provided an Industry view on the Integration discussions and made particular reference to the introduction of the concept of responsible lending in the White Paper. He wondered when this issue had come up in the Commission's assessment and hoped that it was not a 'knee-jerk' reaction to the events of recent weeks and months on the US subprime market. He also stressed that the UK model of information standardisation is not an appropriate one for the rest of the



EU. **Bernhard Scholz**, Member of the Board of Münchener Hypothekenbank in Germany, also provided an Industry view on the upcoming White Paper and focused specifically on the issue of early repayment. In particular, he questioned the significance of early repayment as an obstacle on the basis that if cross-border activity is largely supply driven, then this logically means that lenders have already overcome any potential barriers.

The discussion which ensued focused on the drivers of cross-border activity (supply vs. demand) and product diversity. Panelists also touched on the issue of responsible lending and Mr. Purvis pointed out that both Industry and Consumers suffer if lenders do not lend responsibly. The Industry was keen to stress that lenders in the EU do lend responsibly and that the US crisis largely resulted from unregulated credit intermediaries. The Industry therefore urged the Commission to await the results of its Study on this sector before taking any decisions about responsible lending.

The EMF was delighted to welcome MEP **Pervenche Berès** as the second Keynote speaker of the event. Ms. Berès gave participants an insight into the position of the European Parliament on the further integration of Europe's Mortgage Markets. Firstly, she emphasised that the EP strongly

believes that there is scope for further integration and that this can be best achieved with targeted, well-designed measures, which can bring about considerable benefits for consumers in terms of improved choice and quality of products and services; and, ultimately, bring about cheaper housing finance solutions. Ms. Berès explained that to this end, the first priority should be to achieve a single funding and lending market to boost market efficiency, economies of scale and scope, reduce borrowing costs and contribute to risk diversification. Secondly, she added that the EP believes that it is of paramount importance to preserve high levels of consumer protection, by ensuring high quality information, appropriate advice, greater transparency and comparability of prices and better education of homebuyers. Thirdly, she noted that the EP has highlighted the need to tackle different practices and standards that often discourage foreign lenders or consumers from entering a foreign market.

In the second part of her speech, Ms. Berès turned her attention to the recent subprime crisis. She informed participants that the EP is very concerned because the crisis continues to affect Europe by provoking a major liquidity squeeze and because of the potential negative impact on the real economy. Although she considered that securitisation



Ms. Pervenche Berès,
Chairwoman Economic and Monetary Affairs
Committee, European Parliament.

has several positive aspects, she stressed that something had gone wrong and highlighted what she considered to be the elements which contributed to the crisis i.e.: the looser underwriting practices and governance standards by originators, brokers and banks, the increased use of securitisation to fund mortgage credits, the dispersion of risk in capital markets and weakening of monitoring incentives, macroeconomic and monetary conditions and finally the opaque system which has resulted from financial innovation and the use of derivatives. She stressed that there are clearly lessons to be learned:

- There is a need to improve the quality and transparency of investor information;
- Transparency and understanding of underlying risks needs to be enhanced;
- Valuation processes and risk management practices need to be reviewed and adjustments in the Basel II and CRD might be needed;
- A better understanding and monitoring of the risks of off-balance sheet vehicles;
- Rules and requirements on liquidity risk and liquidity management need to be harmonised; and
- The system needs to be more transparent for investors and supervisors.

«... Further integration ...can be best achieved with targeted, well-designed measures, which can bring about considerable benefits for consumers in terms of improved choice and quality of products and services; and, ultimately, bring about cheaper housing finance solutions».



PANEL II

Staying on the subject of the Commission's assessment of the Integration of EU Mortgage Markets, the second panel, entitled "Consumer Issues: Continuing the Dialogue" and again moderated by **Annik Lambert**, focused on the key consumer protection issues in Europe (consumer information, early repayment, APRC, duty to advise) and the Code of Conduct on Home Loans.

Rodrigo Gouveia, Secretary General of EuroCoop, gave participants the consumer perspective on the Integration discussions and stressed that a high level of consumer protection is a policy goal in itself and that it is vital for a high level of consumer confidence, which is in turn important for the creation of the Single European Market. He was of the opinion that regulation is the only way to achieve this, since as far as he is concerned, co- or self-regulation do not work. **András Botos**, Secretary General of the Association of Hungarian Mortgage Banks, was up next and in his introduction he focused on the promotion of awareness among consumers of the costs, risks and benefits of financial products. **Peter Engberg Jensen**, Group Managing Director at Nykredit, also spoke for the Industry and focussed on opening up the cross-border market for housing loans, for example, through mutual recognition and the launching of an EU mortgage concept, and on providing correct information to consumers through the use of market-to-market terms, by avoiding overregulation and information overload and through compliance with the Code of Conduct. In his opening statement, **Wolfgang Kälberer**, Head of the Brussels Office of the Association of German Pfandbrief Banks, underlined that the Industry supports consumer



From left to right:
Eric Ducoulombier, Wolfgang Kälberer, Peter Engberg Jensen, András Botos & Rodrigo Gouveia.

education and information, and product transparency but does not view early repayment as a key obstacle. **Eric Ducoulombier**, who had kindly agreed to step in to the second panel, once again provided the Commission stance, this time with regard to consumer protection and integration and stressed that in the absence of a consensus during the Mortgage Industry & Consumer Dialogue Group (MICDG) discussions, the Commission has to act in the general interest. He noted that whatever the final choice is with regard to the Code of Conduct, its achievements would be taken into account. The format of the Code will be more elaborate than at present and will be based on the MICDG breakthroughs. He stressed that the Commission shares the Industry view that products should not be harmonised but fears that it is unrealistic for lenders to export their products on the basis of mutual recognition. Finally, he underlined the importance of financial education of consumers and noted that the Commission would be publishing a Communication on the subject.

The discussion, which followed panellists' opening statements, focussed largely on the issue of early repayment. Further to a question

from the moderator regarding the possibility of 'accidents of life' as a potential compromise on early repayment, Mr. Ducoulombier acknowledged that this is a possibility and the Commission would be evaluating the pros and cons and the costs and benefits of this particular option. Mr. Gouveia stressed his position that early repayment should be a legal right and that the accidents of life compromise was completely unacceptable. The Industry stressed that early repayment should be agreed on a contractual basis between parties, as the introduction of a legal right would result in a mutualisation of risk and subsequently higher costs for consumers.



The Conference's third key-note speech was delivered by **Philippe Moutot**, Deputy Director General Economics and Director Monetary Policy of the European Central Bank, on the role of mortgage markets in achieving monetary and financial stability. Mr. Moutot spoke of the benefits of further integration to monetary policy in terms of the ability of households to make well-informed and forward-looking decisions on the basis of accurate and transparent information on the price and other aspects of the terms and conditions of a mortgage loan.

Mr. Moutot then spoke about the legal possibility of refinancing outstanding fixed rate mortgages without facing significant transaction costs as another factor which could have a significant monetary policy impact. He advised that a separate and competitive pricing of the repayment option could contribute to more transparency and thereby help consumers to make rational choices.

Mr. Moutot then spoke about mortgage equity withdrawal (MEW), and he explained that there are two main possible consequences of such products becoming more widely available: First, household indebtedness could increase, which would entail a higher sensitivity of household spending decisions to

changes in interest rates, and second, MEW would make it considerably easier for households to transform increases in their wealth as a result of higher property valuations into consumption spending. He then explained that this could point to a larger marginal propensity to consume out of wealth, leading to increased effectiveness of the wealth channel of monetary policy transmission.

Though welcoming from a monetary policy perspective the fact that increased MEW tends to increase the speed at which monetary policy impulses are transmitted to the economy, Mr. Moutot explained that it can prove challenging if agents in the economy set expectations in a backward-looking manner. In such a case, he continued, agents would tend to extrapolate past house price increases into the future and thus engage in unsustainable borrowing behaviour. Mr. Moutot then added that such behaviour would magnify cyclical volatility and lead to undesirable pronounced boom-bust phenomena, and would require special attention by bank regulators.

On mortgage funding, Mr. Moutot explained that the recent problems in the securitisation market in Europe have highlighted the deficiency of data on the performance of mortgage loans in Europe. He pointed out that



Philippe Moutot, Deputy Director General Economics and Director Monetary Policy of the European Central Bank.

such data is important not only for investors in residential mortgage-backed securities, but also for issuers themselves and for central banks for monetary policy and financial stability purposes. Explaining that the information currently available in Europe is fragmented across many different data providers, that it lacks consistency and comparability and that it is not available in sufficient detail, Mr. Moutot then highlighted that compared with the situation in the US, data transparency can be vastly improved. He added that while the industry is well aware of these concerns and that it is already addressing them, much of the hard work still needs to be done.

PANEL 3

Panel 3 focussing on the outlook for the EU mortgage and housing markets was moderated by **Adrian Coles**, Director General of the Building Societies Association, who set the scene by highlighting a number of key developments, namely the significant growth in mortgage lending activity in the last ten years in the EU as well as the intensification of competition as attested to by the falls in mortgage margins. He also honed in on the issue of demographics, pointing out the growing proportion of the population

over 65 years compared to those of working age, and on what implications this will have for mortgage lenders going forward. **Simon Low**, Director at Oliver Wyman, contributed to the debate by posing the question of whether European mortgage margins may have reached a turning point, using recent market events as triggers of a change in the risk appetite of lenders and the consequent slowing down of market growth and volumes. **David Miles**, Chief UK Economist at Morgan Stanley highlighted some interesting distinctions between the US and various EU house markets.

He noted that house prices in the last ten years had risen more sharply in most parts of Europe than in the US and that expectations had a big part to play in house price developments. David Miles went on to conclude however that the prospect of some future corrections in house prices was perhaps not as dramatic as all that, especially given the phenomenal growth in recent times across much of Europe. **Tony Moroney**, Executive Director at EBS Building Society and Tomas Riestra, Senior Economist at BBVA, both spoke in turn about the prospects for the Irish and Spanish



markets respectively. Anticipating perhaps the less sanguine outlook given by **Jean-Michel Six**, Chief European Economist of Standard & Poors, Mr. Moroney and Mr. Riestra gave a number of reasons for the particular speedy growth observed in the last few years in their markets and provided some basis for expectations of a soft, rather than hard landing, going forward. Mr. Moroney pointed to the relatively high proportion of young adults in Ireland driving demand for housing as well as huge increases in the Irish labour force in the last twenty years and spoke of current and future developments in terms of a transition from a period of rapid growth. He highlighted a generally downward trend in house price growth going back some ten years. Mr. Riestra highlighted that Spain had only relatively recently attained a proportion of housing investment to GDP comparable to other developed



From left to right,
Tomas Riestra, Jean Michel Six, David Miles, Tony Moroney, Simon Low & Adrian Coles

countries and spoke of the relatively low levels of household indebtedness in Spain. Jean-Michel Six highlighted expectations of further falls in house price growth, pointing to substantial increases in the ratio of household

debt to annual income combined with recent increase in interest rates, along with an expected slowdown in lending growth and the possibilities of a downturn in the construction sector.

PANEL 4

The fourth panel session, focussing on home-ownership and affordability, was moderated by **Andrew Heywood**, Deputy Head of Policy at the Council of Mortgage Lenders. Andrew opened the panel by asking a series of questions including whether borrowers or lenders should determine affordability and whether present difficulties with sub-prime lending in the US pose a challenge for those arguing for a more liberal market integration agenda for Europe.

Keith Hale, Technical Specialist at the Financial Services Authority (FSA), gave an insight into the FSA's approach to regulation of the UK mortgage market. Speaking in favour of better regulation, Keith highlighted an approach guided by an interest in stimulating competition and smoothing the way for innovation, rather than an attempt to control product design. He added that the case for action has to be based on



From left to right,
Bernard Vorms, Ruud Vermeulen, Hugh Harper, Keith Hale & Andrew Heywood

clear evidence of market failure, supported by robust cost-benefit analysis and in-depth consultation with stake-holders.

Hugh Harper, Partner at McKinsey & Company, pointed out that he feels that the issue of sub-prime lending is not one of home ownership affordability, but instead one of refinancing, and that it should

not be viewed by the Industry as a problem, but as an opportunity. Speaking about the 1990's boom in sub-prime lending in the US, he explained that it was fostered by product innovation to allow greater leverage, growth of the private label MBS market, low interest rates and growth in independent monoline primary originators.



Ruud Vermeulen, Economist at the European Central Bank, focussed on the results of an assessment of the key vulnerabilities and risks in EU mortgage markets, published in the November 2007 issue of the ECB Banking Sector Stability Report. He highlighted that while pockets of vulnerability have grown in the EU mortgage markets, particularly with respect to rising household mortgage indebtedness, the risks to

both households and banks' balance sheets are rather limited.

Bernard Vorms, Director of the French National Housing Information Board (ANIL), spoke of how even though the French market for housing loans offers some of the lowest rates in Europe, and has very low rates of default, customers are denied access if they are either unable to provide evidence of regular income or to have access to death and disability

insurance. He then went on to explain how widening access to home loans should not mean radical changes in the regulation in place or indeed the establishment of sub-prime lending markets.

PANEL 5

Panel 5, which was intended to look at developments and innovation in residential mortgage lending, was moderated by **Tammo Van Leeuwen**, Head of Product Management at Business Architects International. Tammo introduced the subject by speaking of the importance of innovation for the mortgage industry and outlining the multiple reasons for new product failures and the difficulties of success of new products. He then highlighted the importance and benefits of centralised mortgage processing supporting all the channels, and its necessity due to channel diversification. He explained that the most important element in innovation is in terms of selling and servicing the product in an integrated way over multiple channels. Four of the five panellists then went on to speak specifically about product development in their respective markets.

Laszlo Harmati, Deputy CEO of FHB Land Credit and Mortgage Bank in Hungary spoke of the difficulties of foreign entrants who assume that they can introduce the same products in foreign markets as in their own domestic markets. Going through the speedy developments of mortgage products in Hungary in the recent years, Laszlo spoke about some of the latest product innovation trends in his market, mentioning for instance the growing importance in



From left to right,
Claude Taffin, Mike Schneider, José Ramon Ormazábal, Tony Moroney,
Laszlo Harmati & Tammo Van Leeuwen

the development of flexible products such as revolving mortgages and remortgaging facilities and the development of market niches. **Tony Moroney**, Director of EBS Building Society in Ireland, spoke, among other things, about the significant growth in the diversity of mortgage products in Ireland as well as product regulation and credit assessment developments of mortgages there. From Spain, **José Ramón Ormazábal** focused on the detrimental effects of regulation on product development, using the disappearance of fixed rate products and the lack of reverse mortgages there as case studies. He did however speak positively about new legislation developments. **Claude Taffin**, Director of Economic and Financial Studies

at l'Union Sociale pour l'Habitat in France highlighted the introduction of a number of new products on the French mortgage market targeting non-standard or niche customers, and explained how these would contribute to improved accessibility without circumventing the very strict consumer protection rules in France. The future of reverse mortgages was the focus of the discussion which followed the presentations, aided by the presentation of **Mike Schneider**, Academic Assistant at the European Center for Financial Services, on the introduction of reverse mortgages in Europe, which revealed the wide existence of such schemes in spite of the relatively low activity to date in most countries.



PANEL 6

The sixth and final panel session, focussing on the latest developments in mortgage funding in Europe was moderated by **Paul O'Connor**, Deputy Head of Wholesale Banking and Risk at the Irish Banking Federation. Mr. O'Connor opened the panel by outlining the current market situation and by asking participants to provide their forecasts in both the near term and long term with regard to the securitisation and covered bonds markets.

The exchange of views between panellists, **Patrick Amat**, Chief Financial Officer at Crédit Immobilier the France (CIF) and new Chairman of the ECBC, **Ralf Grossmann**, Head of Covered Bond Origination at Société Générale & Investment Bank, **Louis Hagen**, Executive Director at Association of German Pfandbrief Banks and **Rick Watson**, Managing Director of the European Securitisation Forum highlighted the need among market participants to return to normal market conditions as soon as possible.

The panelists agreed that the subprime crisis has given rise to a major credit crisis: from an issuer point of view, short-term funding has become expensive. The concerns over securitisation structures has resulted in a reluctance of the banks to lend to each other.

The market is clearly very nervous in this context. Securitisation products have suffered in the market with very little activity in recent months. Various policy initiatives are envisaged with the ESF involved in the exercise by the EU Commission. This will include measures to improve transparency, assess the role of Credit Ratings Agencies and analysis of the various accounting approaches such as 'Fair-Value'. There was also an initiative to explore the possibility of improving and standardising product definitions



From left to right, Rick Watson, Patrick Amat, Ralf Grossmann, Louis Hagen & Paul O'Connor

across the many jurisdictions, so that investors could rely on a system of common terminology. It was also noted that the CDO and RMBS sectors are likely to be smaller than has previously been the case.

Covered Bonds issuance is down, however some products such as Pfandbrief have managed to withstand much of the market volatility. The issues surrounding Northern Rock had created some uncertainty in the structured covered bond marketplace. Covered bonds issued under legal frameworks were performing much better than structured covered bonds. It was agreed that the markets were behaving irrationally as Covered Bonds are extremely low risk, and should not really be subject to rapid movements in spreads. The participants felt that Covered Bonds would be restored to normal trading conditions ahead of other products carrying higher risk. While some issuance was possible before year end, it was clear that banks were less likely to pursue issuance programs until next year. The market conditions would remain difficult for quite some time, especially through Q1/2008 as the major banks file their end of year reports.

With respect to the role of rating agencies and the meaning of a triple A rating, the panellists felt that the rating agencies provide a highly effective service and that regulation in this field further to the crisis does not represent a solution. On the contrary, it is important to facilitate an analysis of the structures on the markets. Maximizing transparency will also help the market to get back to normal.

All participants felt that market conditions would eventually improve but with a number of changes, particularly effecting securitisation. Investors still required low risk products which carry inherent protection such as Covered Bonds, and banks would still have a requirement to securitise debt. The longer term opportunities for both markets should be viewed positively.



Hypostat 2006 is now available for FREE!

Download the latest Quarterly Review and Hypostat 2006
from our website NOW!



Merry Christmas & Happy New Year

