



Brussels, 20 February 2009

Position paper of the European Federation of Building Societies on the consultation of the European Commission on non-credit institutions

On the occasion of the consultation on the study concerning the role and regulation of non-credit institutions in EU mortgage markets the European Federation of Building Societies would like to make the following comments.

General comments

The study on the role and regulation of non-credit institutions in the EU mortgage markets carried out by London Economics and published by the European Commission on 2 December 2008 takes stock of the European mortgage market at a moment of severe financial crisis. The financial crisis was caused inter alia by lending practices and refinancing mechanisms applied by non-credit institutions. Against this background we do not consider it an appropriate aim for a study to detect barriers to non-credit institutions' cross-border business. Past lending practices of non-credit institutions or subprime lenders are no basis for a sustainable business model but rather a source of macroeconomic risk. We doubt that non-credit institutions should serve as a model in the context of further EU mortgage market integration. Therefore we would like to take the opportunity and suggest focusing more on best practice examples like for instance the lending practice of credit institutions which though they are confronted with the subprime and financial crisis succeeded in continuing their housing finance business.

It is not comprehensible that this study was again awarded to London Economics. In 2005 a study on the integration of EU mortgage markets conducted by the same contractor was heavily criticized by the whole industry due to methodological shortcomings and a onesided UK-perspective. In the study of 2005 London Economics had advocated for an extension of the allocation of subprime-loans modeled on the UK subprime lending system and calculated a considerable long-term rise in GDP if this model was implemented across the EU. Currently, the "more developed markets such as the UK and the Netherlands"¹ are the ones who suffer most from the crisis.

According to the study non-credit institutions had the highest market share (12%) in the United Kingdom. The current nationalization of the UK banking sector shows that regulatory coverage for non-credit institutions was obviously insufficient and funding mechanisms too short-dated. Scepticism emerges especially as one aim of the study was the provision of supporting information for the (future) evaluation of a passporting scheme for cross-border mortgage provision by non-credit institutions. Considering current circumstances it is hard to understand the reasons of the European Commission for supporting via a European passport the export of a lending model that just demonstrated its susceptibility to risk. The overall aim of mortgage market integration will not

¹ London Economics (2005), *The costs and benefits of integration of EU mortgage markets*, p. 8.

benefit from the promotion of a business model that currently displays its weaknesses and hardly appears to be sustainable.

Specific comments on the content of the study

Apart from the questionable direction the study carries a number of methodological and other weaknesses:

- The conclusions are based on a survey of 10 non-credit institutions (page 20). Several questions are however not answered by all but only part of the 10 surveyed institutions. This response rate cannot be considered representative. Additionally, it would be interesting to clarify which of the answering institutions still provide mortgage credit to consumers.
- On page 12 it is stated, that the motivation to allow non-credit institutions to refinance using mortgage backed securities is that “the risk to the individual customer and to the market from the use of such mechanisms is low.” This is a global statement that is impressively rebutted by current market developments. The degree of risk of refinancing strategies depends on the concrete circumstances. The fact that the statement is not further discussed in the present crisis situation is regrettable and emphasizes the weaknesses as regards the content of the study.
- The financial crisis is mentioned superficially and without discussion despite the connection to lending practices applied by non-credit institutions.

Conclusion

Due to the above mentioned general and specific points raised the study on the role and regulation of non-credit institutions in the EU mortgage markets should not constitute the basis for further policy options in this area. We would instead invite the European Commission to explore, identify and assess the factors that led to this crisis and support prudent and efficient long-term measures to disable similar developments in the future. At the same time we would appreciate not only a discussion about the negative factors that caused the crisis but also about potentially stabilizing factors and best practices such as long-term funding mechanisms and solid own capital bases.