International Union for Housing Finance

IUHF - A global organisation meeting your interests in housing finance

NEWSLETTER *June 2007*

Welcome to the June 2007 Edition of the IUHF Newsletter

By Adrian Coles, Secretary General,
International Union for Housing Finance

Welcome to the June 2007 IUHF Newsletter. Once again, our aim has been to bring you a range of interesting articles from around the world on current developments of relevance to all mortgage lenders. One area that has been receiving worldwide headlines in the financial media has been the state of the US sub prime market. We are delighted that Alex Pollock, a member of the IUHF Executive Committee, has been able to explain recent trends, put them in political context and propose his own legislative and regulatory solutions to the problem he identifies.

We then move on to an issue that affects all mortgage lenders – how do they get their products to their customers? Mercer Oliver Wyman has recently published a report on distribution channels in Europe; this review is by Andrew Gall, Business Economist of The Building Societies Association in the United Kingdom.

Our third item covers developments in Europe in 2006 with Annik Lambert, Secretary General of the European Mortgage Federation reporting on strong performance in most European housing markets over the past year. The next item looks at the formation of a new International Real Estate Advisory Network in the United Kingdom designed to help land, property and finance professionals develop contacts with their counterparts in transition and developing economies, with a view to helping those countries make progress and developing their own property markets.
The Association of German Mortgage Banks has recently published a study examining and explaining what appears to be the relatively low level of owner occupation in Germany. It is a fascinating study and has been reviewed for the IUHF *Newsletter* by Andrew Gall, who has been working overtime on this edition.

Finally, Niels Tørslev, Group Managing Director of Nykredit in Denmark offers his thoughts on how to improve the technical and credit efficiency of the mortgage lending process in order to help the poorest sections of society afford their own mortgage loans.

I very much hope that you enjoy reading this edition of the *Newsletter*. If you would like to contribute to the next edition please do not hesitate to send your articles to:
acoles@housingfinance.org or
kbaker@housingfinance.org
by the end of August.
We aim to publish a further Newsletter in September 2007.

U.S. Subprime Mortgages: Boom and Bust; Politics and Regulation

by Alex J. Pollock

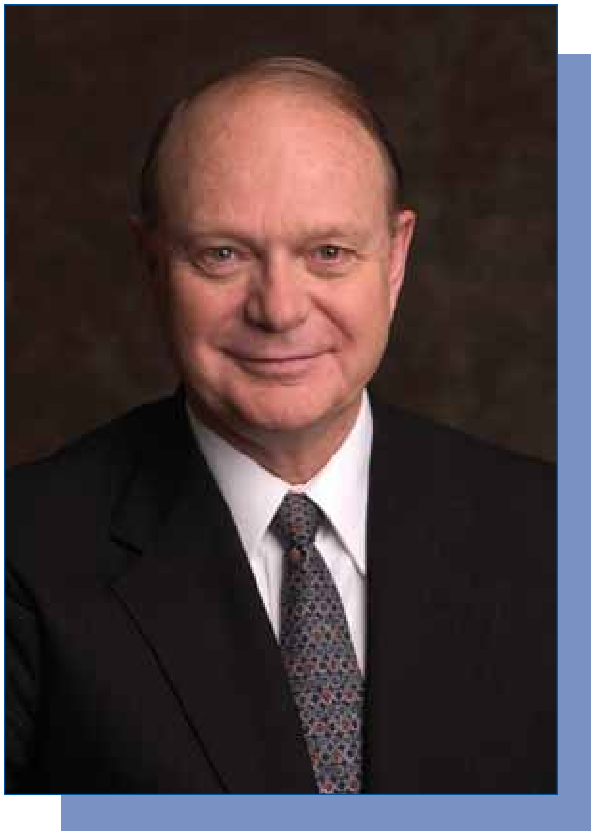
The great American house price inflation which opened the 21st century has topped out, and the unsustainable expansion of subprime mortgage credit which accompanied it has now shifted distinctly into reverse.

The subprime market is contracting sharply and rapidly, if belatedly. The subprime boom is over; the bust is here. Former enthusiasm has been replaced by large financial losses, the bankruptcy of subprime lenders, layoffs, accelerating defaults and foreclosures, fear, a liquidity squeeze—and of course political recriminations, some deserved, as well as proposals for increased regulation. Committees in both the US Senate and House of Representatives are holding hearings on the issue.

A single page of the April 23, 2007 issue of the trade publication, *National Mortgage News,* contained the following items:

- "Four of the top 25 subprime lenders have gone bust in the past four months"
- "Several others are trying to sell themselves to avoid liquidity crunches"
- Subprime lending volume in 2007 is anticipated to fall to half of its 2005 peak
- A top subprime lender, WMC Mortgage, "last week laid off 50% of its workforce"
- Washington Mutual, by far the largest savings and loan, announced a $113 million loss in its home loan business for the first quarter of 2007 due to subprime problems
- Fremont General, another large subprime lender, announced a $100 million loss on the sale of subprime loans
- Fraud in the mortgage industry is "skyrocketing"
- The Senate Banking Committee leadership "ruled out any government bailout for delinquent subprime borrowers".

Subprime adjustable rate mortgages (ARMs) have serious delinquencies of 9% and rising. This is six times the comparable 1.45% for prime ARMs. The current subprime foreclosure rate is 4% and rising rapidly. This is below its recent peak of 9% in 2000,



Alex J Pollock

but the subprime market is much larger than it was then, having grown from about $150 billion in outstanding loans to $1.3 trillion or over 8 times during the boom years. So its political impact is now much greater.

Sources of Risk

As usual, this credit cycle displayed the human sources of financial risk. These include short institutional memories and the inclination to convince ourselves that we are experiencing "innovation" and "creativity" when all that is happening is a lowering of credit standards by new names.

For example, in the latest cycle, "stated income" loans became common—in other words, loans without confirmation of the borrower's income. The disastrous previous experiences with this bad idea, then called "no doc" or "low doc" loans, seem to have been forgotten. Such loans are an obvious temptation, or even invitation, to exaggeration of household income in order to get a bigger loan than one can legitimately qualify for. They are now being called "liars' loans"— a surprise only to those with no memory.

Human elements of risk also included, as always, optimism, gullibility, short-term focus, belief in momentum or the extrapolation of so-far successful speculation, group psychology or the lemming effect, and inevitably in some cases, fraud.

In addition, this cycle became enamored with statistical treatments of risk. Household International was a large subprime lender bought by HSBC, which is now greatly embarrassed by its subprime losses. Household's former CEO is said to have bragged that his operation had 150 PhDs to model credit risk. What happened?

The huge subprime securitization market is based on the mathematical models of the bond rating agencies. Moody's has recently announced that losses on securitized pools of subprime mortgages may be as much as one-third higher than they expected. This should put us in mind of Moore's Law of Finance: "The model works until it doesn't."

Pressure on Regulators

Given the bust, it is not surprising that there is political pressure on regulatory agencies to do something. But what should be done at this point? Late in the credit cycle, when losses are rising, liquidity is shrinking and asset prices are already falling, regulators face a dilemma. The former mistakes and scandals are now clear in retrospect, and they feel like they must respond somehow, but how to take action that is not pro-cyclical and will make the current problems worse?

For example, the combined US financial institution regulators have issued a joint "Proposed Statement on Subprime Mortgage Lending." Many subprime borrowers now cannot afford the reset to a higher interest rate their mortgages call for. So a key requirement of this combined regulatory "guidance" is that ARM borrowers must be qualified using mortgage expense ratios with the fully-indexed interest rate, not only the low introductory or "teaser" rate.

This is a sound and fundamental credit principle. It would have been excellent if implemented at the beginning of the subprime boom. But to put it in place now will mean that subprime borrowers facing large increases in their interest rate and mortgage payments will be cut off from refinancing possibilities, locking many of them into default. So it is probably not a good idea now, at least as it applies to existing subprime borrowers facing "payment shock" from increasing ARM rates.

Another idea discussed in Congress and elsewhere is the possibility of some kind of government fund to refinance defaulted subprime mortgages. The Federal Housing Agency (FHA) is often suggested in this context, although it is a credit insurer, not a mortgage investor. Moreover, the FHA's own delinquency rate is at the same level as the subprime sector, which suggests that loosening its credit standards further is probably not a good idea. Naturally, no one wants to bail out subprime lenders and investors, who should be on their own for whatever losses are in store.

There is one interesting historical precedent for government refinancing of defaulted mortgages: the Home Owners' Loan Corporation (HOLC), created by the Home Owners' Loan Act of 1933. Of course, the subprime problems of today do not begin to approach the financial collapse of 1933, but HOLC makes a useful study for anyone intrigued by such a possibility.

As noted above, recent statements by the leadership of the Senate Banking Committee suggest that the "bailout fund" idea is not being pursued, at least for now.

The One-Page Disclosure

The legislative and regulatory action I propose is to require a one page form for every mortgage loan, with short, simple and clear disclosures of the essential loan terms and their relation to the borrower's household income. The borrowers should be able in effect to "underwrite themselves" and understand their basic risks.

A good mortgage lender wants a borrower who understands how the loan will work and what the financial commitments of the loan agreement are. Current American mortgage loan documents certainly do not achieve this. Most borrowers are overwhelmed and befuddled by the huge stack of documents full of confusing language in small print presented to them for signature.

To achieve an informed and understanding borrower, the key information must be simply stated and clear: 90% of the relevant information which is understandable is far better than 100% which is complex and confusing - the latter results in effectively zero information transfer to the borrower.

The following one-page "Basic Facts About Your Mortgage Loan" form demonstrates the idea. There is some Congressional interest—I hope it will grow.

THE BASIC FACTS ABOUT YOUR MORTGAGE LOAN

Borrower: ____________________ Property address: ____________________

____________________ ____________________

____

Lender: ____________________

Amount of loan: $ ____________, which is ______% of the property's appraised value.
Your loan is for ________ years. Its final maturity date is ________________.
The type of loan you have: ____________________

Your beginning interest rate is ________%. This rate is good for ________ months/years. The rate and your payment can go higher on ________________ and each ______ months after that.

Today's estimate of how high the rate will go, called the fully indexed rate, is ________%.
The maximum possible rate on your loan is ______%.

THIS LOAN IS BASED ON YOUR MONTHLY INCOME OF $____________________.

Your beginning rate = a monthly loan payment of $____________ = ______% of your income.
-including taxes and insurance this is about $____________ = ______% of your income.

The fully-indexed rate = a loan payment of $____________ = ______% of your income.
-including taxes and insurance this is about $____________ = ______% of your income.*

*This is called your fully indexed housing expense ratio.

Special factors you must be aware of:

-A prepayment fee of $__________ must be paid if ____________________.
-A "balloon payment" of $__________ to pay off your loan will be due on __________.
-You do/do not have a "payment option" loan. If you do, make sure you really understand what this means. Start with the definition on p. 3.

Total "points" plus estimated other costs and fees due at closing are $____________________.

FOR QUESTIONS CONTACT: Name: ____________________

Phone: ______________ e-mail: ______________

See definitions of underlined terms and guidelines on pages 2–3.
DO NOT SIGN THIS IF YOU DON'T UNDERSTAND IT!

____
Borrower Date

____________________ ____________________
Authorized Signer of Lender Date Borrower Date

POLLOCK/AMERICAN ENTERPRISE INSTITUTE/2007

Changing Channels

by Andrew Gall, Business Economist, The Building Societies Association (UK)

A new report by Mercer Oliver Wyman on mortgage distribution channels in Europe finds that alternatives to the traditional bank branch have gained share in many national markets. Indirect channels, such as mortgage introducers or brokers are more common, and remote channels such as the phone and the internet are also growing in popularity. These changes in distribution have implications for lenders and regulators, and the trends are expected to continue.

Large differences in the mix of channels can be observed across Europe. For example, in the UK and the Netherlands, over 60% of new lending was via indirect channels, compared to 20%-30% in France and Germany and only around 5% in Denmark. By 2010, Mercer Oliver Wyman expects 50% of mortgages in Europe to be distributed indirectly.

The extent to which different channels are preferred depends on the structure and competitiveness of the market, the complexity of available products, the density of the branch network and the level of financial sophistication or capability in the economy. Against these factors, the intermediary channel is said to offer increased transparency, choice and advice.

The report recommends that lenders optimise their branch distribution by making the most of sales opportunities. Providers will be less able to rely on existing banking relationships as a source of new mortgage business - many consumers will investigate other lenders' offers. However, a provider that has invested in and developed strong customer relationships may face less direct competition from intermediaries.

The report suggests that providers take a more disciplined approach to managing their sales forces in their branches. This covers resource allocation, incentives and sales processes and systems. Lenders should also try to increase cross-sales, aided by rapid credit decisions, integrated processes and sales training.

As the mortgage intermediary markets become more competitive, lenders are likely to have to discriminate the product or commissions they offer to intermediaries in order to attract business.

Financially sophisticated customers are increasingly likely to go beyond using remote channels such as the internet merely for research and actually make mortgage applications online. Successful remote channel distribution is either going to be very competitively priced to drive volume, or combine an online presence that generates leads with face-to-face advice.

Andrew Gall – Business Economist, BSA

The report states that customer retention is increasingly important. The most successful strategies are based on fully understanding customers' propensity to pre-pay their mortgages, making retention a core part of all business activities, and implementing initiatives that utilise customer information to "test and learn" what approaches are effective at retaining customers.

The pricing of mortgages could also be utilised to a greater extent than at present. The report recommends that pricing processes and strategies are fully integrated with other business objectives, with supporting analytics and performance measures. Prices may even be differentiated for each customer.

Expansion into other European markets via cross border distribution is seen as preferable to acquisition, with entry either via a simple, low-cost business model, or into a niche market aimed at a distinct segment.

The report identifies six business models that can be successful in the future. These all identify a clear role for distribution in terms of what channels to offer to each market segment, what coverage is required and what procedures and processes are necessary to ensure the elements of the model work together.

Branch focussed lender – use local distribution and customer relationships to increase volumes and cross-sales and protect from price competition (e.g. HSBC UK, Societe Generale)

Scale originator	Focus on mortgage origination, developing relationships with intermediaries (e.g. Northern Rock, ING DiBa)
Direct lender	Use remote channel to focus on a specific market segment, aggressively managing the cost base (e.g. SBAB, ING Direct Italy, Bankinter)
Giant all channel lender	Scale across all channels (e.g. HBOS, Santander, Bank of Ireland)
Branded distributor	Distinguished by a focus on advice, best product and price (e.g.De Hypotheker, Interhyp, Meilleurtaux)
B2B Platform	Provide software and support for lenders and intermediaries. (eg Europace, Mortgage Brain, Empruntis)

Most firms are currently pursuing one or more of these strategies, but are expected to focus their attention to where they have some sort of competitive advantage.

The report states that successful firms will focus on one model, aggressively improve performance in this area, and leave alternative channels to others. According to the report, lenders that stick to the old branch model and merely dabble in emerging channels will be out-competed by focussed distributors.

Significant changes have occurred in the distribution of European mortgages over recent years. The growth of intermediary and remote channels, and improvements in technology and customer sophistication have allowed providers to adopt different approaches to sales, retention and pricing than they have done in the past. These trends are likely to continue, but whether they cause such a radical shake-up of business models across European mortgage markets as the report suggests remains to be seen.

A copy of the report can be requested here: http://www.mow.com/en/perspectives/form.asp?title=European%20Mortgage%20Distribution%20Changing%20Channel%20Choices

Growth and Increased Integration for the European Mortgage Industry

by Annik Lambert, Secretary General, the European Mortgage Federation

Looking back over the course of 2006, European mortgage markets continued their strong performance of previous years, with total loans outstanding growing by 11% according to EMF estimations. However, unlike recent years, the continued growth of 2006 has been achieved in an environment of increasing interest rates and, in some parts of Europe, signs of a slowdown in the growth of property prices.

Looking back over the course of 2006, European mortgage markets continued their strong performance of previous years, with total loans outstanding growing by 11% according to EMF estimations. However, unlike recent years, the continued growth of 2006 has been achieved in an environment of increasing interest rates and, in some parts of Europe, signs of a slowdown in the growth of property prices.

Annik Lambert –
Secretary General, the European Mortgage Federation

While such an environment has to some extent and in certain housing markets contributed to less optimistic prospects, growth in home loans has remained very strong due to a combination of continuing favourable general financing conditions, further improvements in consumer confidence and strong housing market dynamics in many regions of the Euro area, as confirmed by the European Central Bank .

Looking more closely at the evolution of house prices also reveals largely positive results. A comparison of second quarter house price growth figures for 2006 and 2005 (which is the most recently available data, see table 1) shows that out of 13 European countries, eight have experienced higher growth in 2006 than in 2005, whilst of the remaining five which experienced lower growth in 2006 than in 2005, two still recorded two-digit growth rates in 2006 .

In addition, the impact of rising rates on the borrowing costs of mortgage holders has been mitigated somewhat thanks to the adaptability and competitiveness of European mortgage markets. Competitive rates and offers by mortgage lenders are continuing to attract new borrowers and in some markets existing borrowers have been able to benefit from new products on the same terms as new borrowers.

A recent trend has been increasing mortgage maturities, allowing home buyers to obtain mortgages with lower monthly repayments. Thus, 30 to 40 year mortgages are now available in certain parts of Europe, while in the UK a new type of mortgage was launched recently that would allow parents to pass on their property and their outstanding mortgage debt to their children.

Furthermore, rising interest rates and expectations of further rises have produced an increase in the demand for initial fixed period rate mortgages, enabling borrowers to shield themselves for some time against the effects of rising interest rates.

Evidence of high levels of competition in Europe's mortgage markets was first presented in a co-branded EMF/Mercer Oliver Wyman (MOW) Study published in October 2003 and more recent evidence supporting this view has come in the form of an update to the 2003 Study, published early in 2007. The EMF's intention with this latest Study was primarily to examine mortgage price developments in the eight markets first analysed in 2003 as well as to increase the coverage of the data to a larger (13) number of Member States.

The Study reveals that between 2003 and 2006 prices of mortgage loans have fallen in all of the markets for which data was previously reported and by an average of 30 basis points. It also shows that the range for the adjusted price across the 13 countries – which was already low in 2003 – is still very narrow (under 1%), even taking into account that five new countries have been added to the analysis.

The Study further highlights that competition levels are continuing to increase across European markets in an environment of increasing demand for mortgages and that this has in turn led to significant benefits for customers in terms of lower prices and a broader product range. It is also pointed out that competitive forces within countries have made terms and conditions much more transparent for borrowers, and led lenders to become more efficient.

As such, these findings clearly reinforce the messages that have been communicated to the European Institutions by the Industry over the past few years in response to the various consultations that have taken place on the possibility of enhancing the integration of European mortgage markets. Competitive mortgage markets in Europe have led to low and falling mortgage prices, with very little difference between the lowest and highest priced countries, and with the consequence that there is therefore little room for further integration.

These views were underlined in November 2006 on the occasion of the European Mortgage Federation's fourth Annual Conference, which was addressed by European Commissioner for the Internal Market, Charlie McCreevy. The Conference provided the Industry with the opportunity to remind the European Commission that market forces by themselves have already achieved and continue to achieve greater integration of Europe's mortgage markets.

This is not to say that there is no room for improvements in the area of mortgage lending in Europe. The European mortgage industry has been communicating for some time now that one central area in which mortgage market integration could be improved is by enabling more efficient funding of mortgage loans across Europe. The European Commission's response was the creation of the Mortgage Funding Expert Group, which published a report on 22 December 2006 containing a number of important recommendations, a certain number of which endorse recommendations that the EMF itself has been communicating to the European Commission since 2003.

This initiative, alongside that of the Mortgage Industry and Consumer Dialogue Group, has provided the Industry with the opportunity to voice its concerns and recommend courses of action with a view to having input into the forthcoming White Paper on Mortgage Credit, which is expected later in 2007. Indeed, in his speech to the EMF Conference, Commissioner McCreevy referred to these inputs as 'key initiatives' in the context of the White Paper.

Having participated very actively in all of the European Commission's discussions and consultations in this subject area, the EMF feels confident that the recommendations which it has made will be taken into account and reflected in the White Paper. The EMF is looking forward to continuing to work closely with the European Commission and the European Parliament over the coming year – which, incidentally, will mark the 40th anniversary of the European Mortgage Federation's launch – in order to help ensure that the benefits arising from further integration are achieved by the best means possible.

[1] See ECB monthly bulletin, December 2006.
[2] EMF 2006 second quarterly statistics.
[3] See 'Study on The Financial Integration of European Mortgage Markets' , EMF/ MOW, October 2003.

International Real Estate Advisory Network (IntREAN)

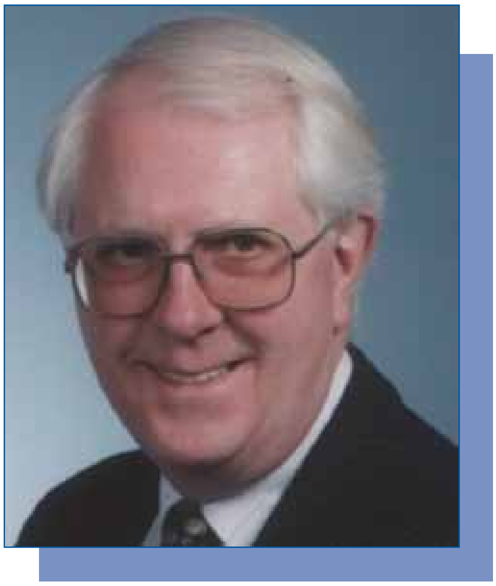
by Brian Emmott

What is the Network ?

This UK instigated Network is a group of practitioners (corporate, individual and associations) all of whom have extensive experience in unlocking the economic resources in land and property (ie all belong to one of the 6 pillars that make up a property market – see below).

They will propagate and develop contacts with their counterparts in transition and developing economies (particularly focusing upon entrepreneurial companies and individuals) with a view to encouraging and helping those people to form local Common Interest Groups (CIGs) whose aim is, with the direct assistance of IntREAN members, to make progress in developing their property markets and instigating actual projects and learning by direct experience how to overcome the pitfalls.

Funding is therefore needed initially for a Secretariat who will assist the members in convening the Common Interest Groups and generally raise awareness in the UK, other Developed Economies and selected transitional and developing countries. It will also develop a website/portal, hold an International Forum and carry out all the activities listed below. It is reasonable to assume that a CIG can be formed (in any willing economy) within 3 months; that it will coalesce into an effective group within 12 months; and that it may have a tangible project under development within 1-2 years and have held a local forum/seminar.



Brian Emmott

Why is the UK instigating this Network ?

We divide the property market into "6 Pillars" that support the market:

1. LAND & PROPERTY ADMINISTRATION
2. LEGAL, JUDICIARY & ARBITRATION
3. FINANCE, TAXATION & RISK
4. VALUATION & SURVEYING
5. BROKERS & AGENTS
6. DEVELOPERS, ARCHITECTS, ETC.

The two main financial centres in the UK, London and Edinburgh/Glasgow, have world class companies and organisations in all of these "pillars" that together create and sustain the UK and many other countryies property markets. They are therefore ideally placed to offer help, advice and support to the transition and developing economies as they build their property markets and related institutions. By working together this can be achieved. With members from each of the "pillars", we can be certain that the necessary help and support is co-ordinated and given in the right places and at the right times.

The Network will not just include indigenous UK organisations, but also those international organisations that choose to operate out of the UK.

Why is the UK a good example ?

The UK model is very relevant to any country seeking to improve the functioning of its housing market. It is particularly relevant to transitional and developing countries for the following reasons:

- It requires minimal scarce resources – in terms of people, institutions and money. There is no need for example to create new organisation (eg a "National Housing Bank", national land authority, a national house building company or a mortgage market authority).
- It is an evolutionary model that works with market forces rather than against them.
- For the most part it involves the removal of controls and obstacles rather than establishing new procedures and institutions – although some may be needed, particular in respect of land registration and judicial bodies.
- UK based expertise is readily available to provide assistance.

What is the Mission Statement ?

To help the development of functioning property markets in transitional and developing countries by facilitating access to expertise and experience within the UK and other developed real estate markets.

What is the Rationale for the Network?

Well-established property rights (from which various forms of home tenure and ownership develop) form the foundation of a country's economy and a healthy financial system. Despite the sophistication and scale of developed country's capital market, mortgages remain its cornerstone. The existence of this large, stable pool of finance, with a well-diversified risk basis, has been critical in the development of capital markets. Moreover, creation of a "homeowner class" is one of the surest methods to help a society achieve long-term economic growth and political stability.

Many of the transition and developing economies have begun the process of building the institutional capacity and infrastructure necessary to grow their property sectors that will bring broad economic and social benefits. But there is still a long way to go before they achieve a fully functioning and well regulated property market and there is much that developed countries can do to help, in turn helping to create new potential markets for themselves.

The main problems with many of these markets involve land rights and the legal system. It is only by highlighting how other necessary participants in the real estate market are being held back from entering that progress can be made. In the original EU15 countries with average owner occupancy of over 55%, household loans are on average nearly 50% of GDP. In the transition economies (with owner occupation averaging 90%) average household loans are about 10%. of GDP (Figures from UNECE and European Mortgage Federation statistics)

Will the Network work with other International bodies ?

The Network will work with any organisation involved with developing property markets internationally. It is building upon the work carried out since 1997 with the UN Economic Commission for Europe and their Real Estate Advisory Group (UNECE REAG). Following on from the work in the transitional economies, especially in Central & Eastern Europe, and with contacts and knowledge gained, the time is now right to create a more formal group here in the UK, but also with links to other similar organisations in other developed economies. The Network will help broaden and co-ordinate the extensive range of expertise that exists and keep members aware of the requirements, developments and opportunities within these property markets as they develop in these countries.

The Network will join and conform to the UN Global Compact and intends to form the first sectorial Global Compact Network for Property Markets. It will encourage its members to also join the UN Global Compact both here in the UK and also in all other countries where CIGs are formed or it is operating. Membership of the UN Global Compact indicates conformity to its 10 Principles and helps contribute to an organisation's Corporate Social Responsibility (CSR).

What are the Objectives?

- To raise the awareness of the economic and social benefits that a fully functioning real estate market can bring to a country, its businesses and individuals.
- To ensure that the UK and other countries' experience is available to those who wish to draw on it.
- To encourage the establishment of Property Market Common Interest Groups (CIGs) in transitional and developing countries affiliated to the International Network.
- To raise the standard of education, training and qualifications in their property markets
- To strengthen the institutions, professional and regulatory bodies in their markets
- To help overcome inertia and vested interests in transition and developing economies property markets

What will be the Activities ?

- Arrange meetings with the UK Embassies of Developing and Transition Countries to explain and offer the services of this Network
- In the UK to work with the Foreign & Commonwealth Office, UK Embassies abroad, UK Trade & Investment and other relevant bodies to make aware the services of this Network
- Develop links and relationships with other International organisations involved in similar work

- Encourage and support the development of CIGs in Developing and Transition countries
- Create and maintain a website/portal
- Commission a flagship publication on the UK model and market and prepare a promotional leaflet about the Network. These will be followed by a series of publications on specific areas (eg valuations or mortgage insurance) or case studies that Members will be able to contribute
- To hold regular events on land and property markets, both in the UK and elsewhere, including an International Forum
- Carry out regular Benchmark Surveys in transition and developing economies
- Be represented, ideally as speakers, at important seminars and conferences on land and property to highlight the importance and services of this Network
- Work with UK based education, training and qualification bodies to offer international standard courses and qualifications on land and property markets
- The Network will instigate and encourage tangible demonstrator projects in countries that involve all the "6 Pillars" and result in the building of affordable, environmentally friendly and sustainable homes and related infrastructure (see separate paper on Urban and Rural Village concept)
- The Initiative will NOT engage in developing any construction projects in its own name but will encourage its Members and others to do so

What are the main benefits of joining the Network ?

- To be able to work with all the other participants within the 6 Pillars of the property market to enhance and influence the development of property markets in transition and developing economies.
- To also enable companies to participate in the development of these markets without the necessity of immediately entering these markets but helping to create the environments for future involvement of their products and services should they wish.
- Ideal and cost-effective way of demonstrating Corporate Social Responsibility (CSR) on an international basis.

How do we join the Network ?

For the Network to be effective it should have a large and broad membership from all parts of the property market. However, as stated above, we have firstly to establish the Secretariat and .a website/portal. This will enable us to:

- commission the paper on the UK Model and Market
- instigate the CIGs
- develop the Training, Education and Qualifications programme (especially as this year it is the main theme for the Lord Mayor of the City of London's term of office)
- run and publish Benchmark Surveys
- encourage the creation of a demonstrator project
- continue to raise the awareness and importance of the subject
- hold an International Forum of CIGs and potential countries
- attend and participate in related seminars, conferences, forums, etc.

Separate papers are available on all the above planned activities.

To now establish the Secretariat, ideally we are seeking the support of several Sponsors from amongst the 6 Pillars to make it representative. We would suggest at least an organisation from each Pillar who would, for the first year only, contribute as Prime Sponsors and similar numbers as Sponsors for the first year.

They would of course receive due recognition on all publications and publicity on an ongoing basis as being our original Prime Sponsors or Sponsors.

We would also be encouraging the participation of a larger Ordinary Membership for companies or SMEs at an annual fee.

After the first year the Founders would revert to normal annual fees but obviously retain the recognition of having been Prime Sponsors or Sponsors.

We will also be offering Associate Membership to like-minded international associations, but especially to the main UK associations such as HM Land Registry/Registers of Scotland, Law Society, Council of Mortgage Lenders, Building Societies Association, Association of British Insurers, RICS, Housing Corporation, Federation of Housing Associations, Institute of Financial Services, Institute of Arbitrators, etc. as well as Academic Institutions on a free reciprocal basis.

Who do we contact for more information ?

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Is the German owner-occupancy ratio too low?

by Andrew Gall, Business Economist, The Building Societies Association (UK)

When comparing owner-occupancy ratios across developed countries, Germany stands out. This is because it has an ownership ratio of little over 40%, whereas some other of the world's largest economies have ratios well over 70% (See chart). While an eye catching difference, a recent study suggests that it is a disparity of little consequence[1].

The link is often made between a high rate of owner occupancy and general economic performance, but the study suggests that if a country has a well functioning rental market, this relationship does not necessarily apply.

The differences in home ownership rates between countries are often due to historical differences in the regulatory and tax regimes as well as cultural contexts.

Source: IUHF and European Mortgage Federation

Historical differences

In Germany, as in other countries after the Second World War, social housing was built quickly to increase the housing stock. This created a solid basis for a private rental market. Crucially, the design and construction of German schemes was of very high quality and also involved the private sector so when fixed rent controls expired, private supply was able to establish itself easily. On the demand side, German households in the 1950s often lacked the means to buy their own home.

Regulatory differences

Germany started to liberalise its rental markets in the early 1960s, twenty years or more before its European peers. Freeing up the market prevented rents being kept artificially low. In other countries such as Spain and the UK, limits on rents reduced the incentive for landlords to hold rental properties, and as the number of quality rental properties diminished, homeownership increased. This trend was accentuated when home ownership was granted considerable tax advantages in many countries.

Cultural differences

The report rejects the notion that the prevalence of long term fixed rate mortgages poses a barrier to home ownership in Germany. Instead this is said to reflect Germans' desire to own a home in which to live permanently. Therefore they do not need flexible mortgage products that assist passage up the "housing ladder", and value the stability when it comes to planning their finances. The report goes further to suggest that in housing markets in other countries, people with credit risks must pay higher interest charges whereas in the German model the rental market enables these individuals to live without this extra cost.

Differing perspectives

The authors of the report also provide an alternative perspective to other studies that link home ownership to economic advantage. For example, the report quotes US research that finds that people who own their house care more about their wider living environment than those in rented accommodation. However, the authors' view is that this social stability stems from living in the same property for a long period of time, rather than the type of tenure. As such, long-term renting yields the same benefit as home ownership.

The paper also claims that a high level of home ownership leads to structural problems in the labour market as people are slow or unwilling to move houses to match the job opportunities in the country. A well functioning rental market helps to make the labour market more mobile, benefiting the whole economy.

In recent years countries such as the US, the UK and Spain have experienced strong economic growth alongside considerable rises in property prices. The report concedes that any spur to economic activity stemming from capital gains in property prices and lower mortgage interest rates did not occur in Germany because of the lower home ownership ratio and the prevalence of long term fixed rate financing. However, the authors point out that the risk remains that interest rates will rise and that these drivers of growth could go into reverse.

Even if low inflation becomes embedded, the correspondingly low interest rates offer only a one-off boost, and will then stay at lower levels. In this scenario, the authors state that the advantages of long term fixed rate financing then become persuasive, as households can then plan their finances with more certainty, and the home ownership ratio is irrelevant.

The authors' proposals indicate a distinct ideological difference to the traditional relationship between home ownership and economic performance. This rejects the idea that home ownership itself confers benefits to the wider economy, as long as there is a well functioning rental market.

Instead, the efficiency of a housing market is to be gauged by how assured private households' access is to residential uses, whether via rental or ownership.

Therefore, it is important to take owner-occupancy ratios as only a very rough indicator of an economy's development, and be aware that considerable exemptions, such as Germany, provide informative counter-examples.

[1] "Two sides of the same coin", Verband Deutscher Pfanbriefbanken, December 2006.

Good loans for bad debtors

by Niels Tørslev, Group Managing Director of Nykredit Realkredit A/S (also responsible for Totalkredit)

A number of industrialised and developed countries are currently working hard towards improving the terms for housing loan funding. The purpose of this process is to eliminate as much risk as possible and to make lending procedures as simple and accessible as possible in order to create even more competitive products.

Niels Tørslev –
Group Managing Director of Nykredit Realkredit A/S

This process is a further improvement of already sophisticated financial systems - a refinement for the benefit of borrower groups which already have access to a wide range of financial solutions.

We all compete to position our companies as favourably as possible in the market place.

However, we often forget that there are very large groups of people who will not benefit from these improvements simply because they lack the education or understanding of the meaning of being a borrower - and specifically an attractive borrower.

It would probably be worth starting a dialogue to put focus on this issue as well. What can be done to enhance the terms for customers with inadequate borrowing experience to enable them to optimise their borrowing processes and get better chances of realising their dreams.

Within this area, one is often met with a sense of "insuperability" when it is discussed how to procure financing opportunities – on reasonable terms – for the millions of children in the least developed countries who will grow up in the years ahead and wish to build a home and start a family.

For many reasons – not only human and geopolitical/economic – it is important to develop the "disadvantaged" countries in order to secure a development process leading to democracy, equality and justice within the geographical areas in which the population lives today.

For the individual and society, the greatest misfortune is the realisation that you are or have been unable to live the life you wanted.

When individuals realise this, there is a risk that they will escape from an unsatisfactory reality into an often glorified, but unattainable dream life, and quite often - whether or not they are disappointed by staying or by not having their dreams realised through an escape - they end up living a life where they have made the ultimate sacrifice, namely their self respect and respect for others.

We therefore see many good reasons for attempting to foster more decent conditions.

To offer housing loans as such is a simple business. Investors and homeowners must have a long-term agreement with financial services providers as intermediates.

Where investors have the upper hand, they will win with views that mortgaging property is a very cost-consuming and risky process, and homeowners then end up paying too much for both this and that.

Where homeowners have the upper hand and are able to prove that the risk is low and the distribution process simple, they will obtain a completely different and lower price.

In Denmark all borrowers pay between 0.3% and 0.7% in addition to an AAA rate for a housing loan. In Mexico and South Africa, the richest and best customers pay the same, while the weakest pay up to 5-7% on top of a BBB rate.

This makes it easy for the affluent, but impossible for the poorest and the medium income groups to obtain a decent standard of living. The poorest can under no circumstances afford it. This is a social problem.

The intermediate population category can ill afford decent living conditions as borrowers in this category lack the ability to demonstrate that they represent a fair credit risk.

Lowering interest rate spreads from 7% to merely 2% or 1% would be of immense value to society.

It would be fairly easy to introduce or offer structures or models that incorporate funding-related or administrative improvements. However, if distributors and borrowers fail to understand that a loan implies an obligation, and if they do not have the morals/inclination to repay it, all such initiatives will be futile.

Improved technical efficiency may reduce the interest rate spread by 1%.

Improved credit efficiency may reduce rates by three or four times as much.

In consequence, the task can be solved only if the credit process is improved both technically and in terms of education/conduct.

Herein lies the challenge. How do we solve this?

New Members

The Union is delighted to welcome the following new member since the publication of the last Newsletter.

Federal Ministry of Environment & Housing, Nigeria

Pioneering Business - Enabling Cross-Caribbean Mortgage Finance

by St. Bernard J Sebastian

In March 2007, TransCaribeMortgage Services Inc was established as a regional business, with its Headquarters in Anguilla, dedicated to provide services that will enhance the quality of the real estate sector, in the Eastern Caribbean, to start, and then to the wider region. The Company, TCeM, is pioneered by St. Bernard J Sebastian, the former Chief Executive Officer of the Eastern Caribbean Home Mortgage Bank (ECHMB). The other partners in the Company include, L. Ronald Scheman, formerly the US Director on the Board of the Inter-American Development Bank; George W. Prime, Attorney-at-Law on Grenada; and Joseph Brice of Private International Trust Corporation in Anguilla. The operations are structured to take advantage of modern telecommunications infrastructure connecting the Caribbean islands with the world, to bridge the gap that has prohibited the effective integration of the real estate market. The Company will install a lender/investor friendly international electronic mortgage registration and tracking platform, and thereby provide the means by which institutions could access information that can help structure securitized mortgages especially for the US market.

In light of the initiative by Governments of the region to create the CARICOM Single Market and Economy (CSME), the real estate sector will emerge as the pre-eminent sector for investment. It represents the ideal sector to advance the principle of a single economic space, and the free movement of capital, and in particular the capital that embodies a mortgage as security. Due to the strong link that currently exists between "credit" and the "physical property", there are administrative and infrastructure constraints that could hinder the free movement of capital. However, it is envisaged that with the full implementation of the CSME, lending institutions will be driven towards a system that allows real property records, including Mortgage Notes to be stored and transferred in electronic format.

St. Bernard J Sebastian

TCeM has formed an alliance with MERSCORP to establish a central source for registry of mortgages from multiple country origin, such as the Caribbean, as well as a source of information about registered mortgages. The facility will simplify the business process by which residential and commercial mortgage ownership and servicing rights are organized, sold, and tracked. The company, MERSCORP was created by prominent players in the mortgage industry, in the USA, to streamline the mortgage assignment process. TCeM will operate in a similar fashion, using the technology platform created by MERSCORP. Its operations will be structured so that TCeM acts as nominee in the country land records, for the lender and servicer of the mortgages. In effect any loan that is registered on the TCeM system is inoculated against future assignments because TCeM remains the "nominal mortgagee", irrespective of the number of times the mortgage servicing is traded.

Currently, in all the member countries of CARICOM, the responsibility to administer the "land registry" system is carried out as a public service at the national level by a Department of Government. But these agencies are used mainly as a source for collecting and storage of information. However, in an environment in which global finance requires easy transfer of capital, collecting the information on a mortgage, and lodging it at the Land Registry is not enough. The information has to be protected and used effectively in a way that facilitates growth in lending business.

Notwithstanding the virtues of the single market formed from the multi-island jurisdiction of the OECS, business is handicapped by limited infrastructure. In particular, the localized system of land registry reinforces the traditional link that exists between the availability of credit and the physical location of the property that serves as collateral. Accordingly, lenders that are located in one island, are averse to doing business in another island, outside of where they are located. This logistical constraint serves to stymie the growth of business from a regional perspective and restricts consumer choice. One of the major challenges inhibiting the growth of the real estate sector is the relatively slow process of perfecting security on a loan. Furthermore, with the frequent turnover of individual mortgages in the asset portfolio of lending institutions, there is a high incidence of improper information by the receiving bank, on the updated ownership of the mortgage. The electronic mortgage registry service will trigger a more efficient system to enable tracking of transfer of ownership of the asset that is embodied in a mortgage.

The demand for high value real estate in the Caribbean is on the increase, and with that comes increased use of innovative products and services. Accordingly, the demand for more efficient business processes is also rising. TCeM will be offering a technology solution, providing the services as a centralized electronic registry, thus assisting lenders to overcome the traditional constraint between "location" of the source of credit and the "physical location" of the property. The TCeM registry system will be especially useful for lending institutions, which have a branch network, throughout the islands. Whereas some banks may be comforted that their mortgage portfolio may be geographically diversified, each country may have different legal requirements and foreclosure procedures. In the circumstances, a centralized electronic mortgage registry would be even more critical. In this manner, the system provides for greater liquidity, transferability and security for lenders, and will also bring greater efficiency to the real estate market, as well as broadening its appeal among international investors.

While the mortgages will have to be registered in the respective countries, to protect against various kinds of liens, the services provided by TCeM will facilitate and ensure that proper registries are maintained within each jurisdiction, as well as within the regional registry system. This system is not a replacement for the Land Registry, but a reinforcement of the security system. Lenders will be empowered with the technology to register and transfer ownership of a Mortgage Note to any participating investor at the click of button.

To date the Caribbean remains an attractive tourist destination due to its tranquility, political stability, and the diverse ecological features in the sea, mountains, rivers, sunshine, and sand. In the last five years many international celebrities, have sought to purchase their second homes in the Caribbean. This has triggered new avenues for investment by the private sector in real estate, while enhancing the services to the tourism sector. In effect, the tourism plant in the Caribbean has been given a luxury upgrade that has triggered the search for alternative means of financing, with higher quality and efficiency. For their part, some Governments have specifically redesigned their investment policies to foster growth of residential tourism, by encouraging property development, targeting persons of high net worth in the USA and Europe. These persons can enjoy the Caribbean climate for longer periods than normal tourists.

While TCeM will be accessible to provide alternative financing for completed and seasoned mortgages, its focus will be on mortgage finance for relatively new properties, through strategic partnerships that it has built with developers across the region. From its Headquarters in Anguilla, the operations of the Company are structured to enable financing for high value real estate domiciled in other countries of the Caribbean.

For more information on the services provided by TransCaribeMortgage Services Inc. and its subsidiaries, please contact us as follows:

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IUHF Accounts for 2006

The Annual Accounts for the IUHF for 2006 have recently been published and show a healthy financial situation. The Accounts, copies of which have been sent to all members of the Executive Committee and are available on request to any member of the Union, show that the surplus for the year was just over £31,000. Subscription income was virtually the same in 2006 as in 2005, but overall income increased as a result of the modest profit sharing arrangement which the Union had with the organisers of the 2006 World Congress, the Canada Mortgage & Housing Corporation. Expenditure was controlled and came out below budget at around the same level as in 2005. At the end of 2006 the Union had cash reserves (invested in British building societies) of just over £190,000.

IUHF

INTERNATIONAL UNION FOR HOUSING FINANCE

The International Union for Housing Finance is a multinational networking organisation that enables its members to keep up-to-date with the latest developments in housing finance from across the world, to learn from the experience of others, and to anticipate trends in their own countries before they happen.

How does the Union do this? By communicating!

We do this in six different ways

- We run a website - www.housingfinance.org Please pay a visit!
- We publish a quarterly journal, Housing Finance International.
- We publish a Newsletter three or four times a year.
- We draw the attention of Members to new material posted on the IUHF website through a regular series of Email Alerts.
- We run a World Congress every two or three years and collaborate with other organisations to sponsor various conferences.
- We facilitate the exchange of information, and networking, between members.

For more information, please visit our website at:
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