PIBA's Submission to
Macro-prudential policy for residential mortgage lending

NOVEMBER 2014

Introduction

The Professional Insurance Brokers Association (PIBA) is a representative body of Mortgage, Financial and Insurance Brokers. With over 860 member firms PIBA is the largest representative body for brokers in Ireland.

As mortgage intermediaries, PIBA members and their clients will be greatly impacted by the new requirements outlined within the Macro-prudential policy for residential mortgage lending.

PIBA has fundamental concerns about the proposed requirements. We acknowledge that in the past there was reckless lending by banks in relation to residential properties. However we firmly believe that the market has since corrected itself and the current lending practices put in place over the last number of years are prudent and go a long way towards addressing the concerns of the Central Bank.

We acknowledge the Central Bank's reference to the introduction of loan-to-value (LTV) restrictions in other countries to dampen the credit market and also property prices. However we also note that these restrictions were introduced in these countries ahead of a potential property crash.

We would like to draw the attention of the Central Bank to Lamorna Rogers paper for the Reserve Bank of New Zealand on an A to Z of loan-to-value ratio (LVR) restrictions which states:

> "*LVR restrictions are to be used only occasionally, at those points in the financial cycle where there is a real danger of growing systemic risks leading to financial instability. The Reserve Bank does not intend to operate LVR restrictions in a continuous fashion to smooth the cycle, but rather aims to limit the extreme peaks in house price and housing credit cycles*".

If LTV restrictions are introduced, it should be varied over a credit cycle and not fixed.

There are clear regional trends emerging in the property market, and Dublin and surrounding counties have very different trends from those of the rest of the country. This should be acknowledged when considering any measures that will affect the entire property market.

We note that there are a number of countries that use LTV restrictions. However unlike what is proposed in this consultation there is no lender portfolio level restrictions. In other countries lenders can lend over the LTV cap where there is mortgage insurance in place.

PIBA believes that this is not the time to introduce such measures into the market which is still somewhat fragile. The current issues with property prices are more an issue of supply than that of credit and it is this issue that requires urgent attention by policymakers.

Question 1: Which of the tools or combination of tools available to the Central Bank would, in your opinion, best meet the objective of increasing resilience of the banking and household sectors to shocks in the Irish property market and why?

PIBA believes that the tools outlined within the consultation paper are not appropriate to deal with increasing the resilience of the banking sector at this point in time and we would be strongly opposed to any such measures being introduced.

Such measures would destroy the lending market which is only recovering after the devastating effects of the last downturn and could, potentially, cause a further property crash.

Over the last number of years, underwriting and calculations introduced by lenders are more stringent, with the burden of proof now firmly on the borrower to demonstrate ability to repay the loan. Potential borrowers must now provide evidence of a build-up of savings, their accounts must be maintained in good financial order, and they must show a comprehensive work history. In effect lending is quite restrictive at the moment without the introduction of these proposed measurements.

The suggested tools would impact greatly on First Time buyers and remove them from the market for a period of up to 3 years. For example a person on a gross salary of 50k under the new regime would qualify for a mortgage of 175k and would need to save a deposit of 35k. With outgoings such as tax, rent etc., what the average a person would save typically would be approximately €1,000 a month.

The measures proposed would also impact people who have recently emerged from negative equity and who wish to trade up. While most reasonable people would agree that another property bubble is undesirable and should be prevented if the market were to go in that direction, these proposals will only impact certain areas of the property-buying market. So someone who happens to have plenty of equity in their home will be able to trade up without being affected by these new proposals. On the other hand those who arguably should be helped most by the Government are the ones who would be hit hardest by these proposals.

Take for example the young family who were trapped living in an unsuitable apartment by negative equity as a result of the last boom. They have recently emerged from negative equity thanks to a combination of paying down their mortgage and rising property values. Now they find that they'll have to save a 20% deposit in order to move on.

In the event of the First-Time-Buyer(FTB) market cooling dramatically since it will be far more difficult for potential FTBs to save 20% of the total property cost while also paying rent, then a natural consequence of this will be that the demand for rented accommodation will increase, thus pushing up rents and causing a vicious circle for those attempting to save up the deposit.

A way of introducing LTV restrictions but allowing buyers to still obtain funding up to 90% LTV, would be to allow consumers take out a Mortgage Indemnity Guarantee policy that would protect the lender in the event of a default by the mortgage holder.

Such dramatic changes as proposed to the current mortgage market would mean that more consumers will be stuck in rented accommodation; this will drive rental prices up and will leave vulnerable families at the behest of overseas investors who are bulk buying rental properties in Ireland for investment purposes.

The issue that the government needs to deal with is not restricting lending, but the current lack of supply in the market. There are a number of measures that could be taken to stabilise the current property market in Dublin, the surrounding areas and larger cities without dampening the market in rural Ireland by introducing such draconian measures.

While not under the remit of the Central Bank, some measures that could be undertaken are as follows:

- Properties put on the market should have clear title and be in a position to close once the loan offer has been accepted.
- All offers to be made in writing with the names of the buyers and held by the selling agent to eliminate bogus biding.
- Transparent and reliable bids should be made publicly available by the selling agents i.e. the amount of the bid.
- If a property is put on the market and a purchaser has proof of funds to purchase at that price, then that price must be accepted.
- Following repossessions the banks should place properties on the market in a timely manner.

Exemptions from the LTV limits

Question 2: Do you agree that the measures should apply to all lending secured by residential property (which will include lending on property outside the State)?

No, these measures should not be applied to lending outside the state as it would create a competitive disadvantage for lenders seeking to grant mortgages in a jurisdiction where these restrictions would not apply to domestic lenders.

PIBA believes that if 80% LTVs are imposed, borrowers may be tempted to borrow unsecured loans for the additional 10-20% of the property price from other sources, where the consumer would not be protected by processes such as the MARP process.

90% LTV lending, that has been in place long before the financial crisis of the last few years should remain as the normal benchmark and perhaps restrictions on over 90% LTV lending should be introduced instead of the 80% restrictions proposed.

Question 3: Do you agree with the exemptions set out? Are there any additional exemptions which you consider appropriate, taking into account the objectives of the proposal and the balance between the benefit of any exemptions and the resulting increase in potential for unintended consequences?

PIBA believes that anyone who is purchasing a principal dwelling home should be exempted from these measurements. If a cap on LTV is introduced it should be at 90% LTV to inhibit lenders increasing the LTV above this but we believe that 90% LTV should be the maximum.

Restrictions like those outlined in the consultation paper should only be applied to those purchasing Investment properties and in these cases we believe that the restriction could be decreased to 70% loan to value as proposed in the consultation. For those who are classified as professional investors the loan to value could be restricted further to 50% LTV.

This would prioritise consumers looking to purchase a principal dwelling home above investors.

Question 4: If there are any *significant* operational difficulties envisaged by regulated financial services providers in complying with the measures as outlined above and in the draft Regulations (Annex 1) and the proposed exemptions, please submit brief details of same.

PIBA believes that enforcing the cap on lending above the LTV ceiling is going to be extremely difficult for the lending institutions to manage as it cannot be done in a fair manner. It would mean that potential borrowers submitting an application for a mortgage at the end of a 6 month reporting period would be less likely to be granted a loan than a potential borrower who submits their case earlier in the reporting period.

Question 5: Should some adequately insured mortgages with higher LTVs be exempted from the measures and if so what should be the criteria for exemption?

As mentioned, PIBA strongly opposes these new suggested measures. However, if the Central Bank does proceed with the implementation of these new requirements, we would like to see the introduction of Mortgage Indemnity Guarantee (MIG) Insurance.

In Australia, borrowers must pay Lenders Mortgage Insurance (LMI) for home loans over 80% of the purchase price. In the UK this can be waived in certain circumstances but in most cases when it is over a certain LTV, MIG Insurance is required.

Exemptions from the LTI limits

Question 6: Do you agree that the measures should apply to all lending secured by residential property (which will include lending on property outside the State)?

As per our response to question 2, these measures should not be applied to lending outside the state as it would create a competitive disadvantage for lenders seeking to grant mortgages in a jurisdiction where these restrictions would not apply to domestic lenders.

Question 7: Do you agree with the exemptions set out? Are there any additional exemptions which you consider appropriate, taking in to account the objectives of the proposal and the balance between the benefit of any exemptions and the resulting increase in potential for unintended consequences?

The exemptions under this section seem to be quite comprehensive.

Question 8: Do you consider restrictions on loan-to-income ratios as suitable for buy-to-let mortgages? What impact would a restriction on such loan-to-income ratios have on buy-to-let lending in the State?

No, buy-to-let mortgages should be exempted as per the exemptions outlined in the consultation document. As highlighted LTI would be less relevant to buy-to-let mortgages where repayments are covered by rental income rather than earned income. We would agree that a more demanding LTV cap for buy-to-let mortgages should be imposed.

Question 9: If there are any *significant* operational difficulties envisaged by regulated financial services providers in complying with the measures as outlined above and in the draft Regulations (Annex 1) and the proposed exemptions, please submit brief details of same.
As outlined in our response to question 4, PIBA believes that enforcing the cap on lending above the LTI ceiling is going to be extremely difficult for the lending institutions to manage as it cannot be done in a fair manner for the borrower. Timing of applications would mean that some potential borrowers who require a higher LTI may be disadvantaged by the limits.

Compliance with the limits
Question 10: What unintended consequences do you see from the proposed measures and how could these be avoided?
If these limits are introduced without a lead-in period this could cause a lot of issues for borrowers who already have approvals in principle (AIPs) but may not have signed loan offers. Some borrowers may already have committed to purchasing a property and paid their deposits, hence losing money if they cannot get the LTV that they were originally approved for. Some AIPs only have a validity period of 4 months which may not give the borrower enough time to complete the transaction.

Also an introduction of measures of this magnitude could cause a grinding halt to many property transactions within the next year. We suggest that if the Central Bank is adamant about bringing in these restrictions that they do so, on a phased basis over a period of time, decreasing the percent of lending over the LTV/LTI limits over a longer period of time.

Monitoring
Question 11: Is the threshold of €50 million over 2 quarters an appropriate threshold and time period for reporting requirements? If not, please indicate a threshold you believe to be appropriate and provide reasons why you believe this is the case.
As per our response to question 10, PIBA would like to see a larger threshold of €150million decreasing to €50million over a period of 2 years to allow greater flexibility by the lenders in the introduction of these measurements into their lending policies.

Question 12: Are there any *significant* obstacles to compliance by regulated financial services providers with the limits?
PIBA believes that this is a question focused more on the logistics of reporting and compliance that would be best answered by the lending institutions.

Annex 1: Draft Regulations
Question 13: Please provide comments on the following draft Regulations.
As per our previous comments, PIBA strongly opposes the introduction of these new regulations and we would urge the Central Bank to consider other options to stabilise the market including looking at the underlining issue of supply within certain areas.