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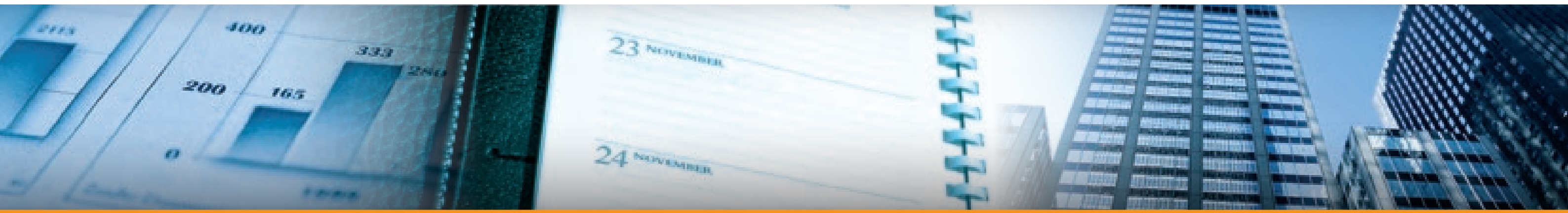

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European Mortgage Federation

ECBC European Covered Bond Council

EMF-ECBC Launches Ground-Breaking Energy Efficiency Financing Project to Create Benefits for Homebuyers

By Luca Bertalot, Secretary General, EMF-ECBC

On the 20th of September 2016, a consortium led by the European Mortgage Federation –European Covered Bond Council (EMF-ECBC) formally launched the European Energy Efficiency Mortgage initiative, with the aim to create a standardised "energy efficient mortgage" based on preferential interest rates for energy efficient homes and/or additional funds for retrofitting homes at the time of purchase. Under this initiative, homebuyers across the European Union (EU) could be offered better borrowing rates on mortgages in return for purchasing more energy efficient homes or committing to implement energy saving work within properties, under a ground-breaking project being pioneered by a unique partnership of banks, property valuers, energy efficiency businesses and utility providers.

The project represents the first time a group of major banks and mortgage lenders, as well as businesses and organisations from the building and energy industries have come together to address the concept of energy efficient mortgages. Alongside the EMF-ECBC, the project partners are the Ca'Foscari University of Venice, RICS, European Regional Network of Green Building Councils, E.ON, and SAFE Goethe University Frankfurt.

Creating a private bank financing mechanism to encourage the energy efficient improvement of households is a key means of helping the EU to meet its energy saving target of 20% by 2020, and to deliver on the ambition of the historic climate change deal, known as the Paris Agreement, which was reached at COP21 last December. It is also particularly timely given the growing global institutional and investor interest in climate finance and private sector investment required to fund low carbon initiatives, which will be the main focus of COP22, the next major climate change conference which takes place in Marrakech in November 2016.

The European Energy Efficiency Mortgage initiative is significant in that it will explore the link between energy efficiency and borrower's reduced probability of default and the increase in value of energy efficient properties. For banks and investors, this could lead to loans which represent a lower risk on the balance sheet and could therefore qualify for a better capital treatment. It could also ensure that banks are able to recognise "energy efficient" assets in their risk profiling, which would begin to help the market to price-in the added value of energy efficient real estate.

The initiative was launched in the context of the World Green Building Council's BUILD UPON Leaders' Summit in Madrid, where 200 renovation leaders gathered to discuss how to tackle energy efficiency in Europe's existing buildings. Full details concerning the initiative can be found in the project's Action Plan, which is available here alongside other related elements of information.

The EMF-ECBC's motivation for this initiative is founded in its belief that it has the responsibility to design a sustainable environment for future generations by developing a pan-European mortgage financing mechanism, according to which energy efficiency investments are made more accessible and affordable for consumers and institutional investors, and the subsequent energy efficiency improvements reduce risk for banks, creating a win-win for all involved.

In terms of next steps, over the coming months, the EMF-ECBC and its partners will begin a mapping exercise in relation to existing or past financing initiatives, energy efficiency indicators and valuation practices, with a view to identifying best practices with which to move the project forward. The experts involved in the project will then meet in Brussels in February 2017 for a private meeting, followed by a public event, to discuss the progress made and decide on the next stage in the work plan.

The Green Side of Success

By Bodo Winkler, Head of Investor Relations & Credit Treasury, Berlin Hyp AG

Following the successful issue of the first Green Pfandbrief in April 2015, Berlin Hyp placed its first senior unsecured green bond in benchmark format on the market on the 19th of September 2016, making the bank the first issuer to offer green bonds in more than one asset class. Berlin Hyp is also the first bank to document and publish a green bond programme that foresees and defines issues in both asset classes. The proceeds from the bond are always used to refinance loans for the acquisition, renovation or development of green buildings.

Over the last few years, the market for green bonds, where the proceeds from the issue are used for defined projects with a positive impact on the environment, has seen a rapid development. The market segment was only established in 2007 when the European Investment Bank (EIB) issued its first Climate Awareness Bond. Multilateral and national aid and development institutions initially dominated the market, with the first banks not appearing on the scene with euro benchmark bonds until 2015, when Berlin Hyp issued its first Green Pfandbrief. Since then, various other banks have followed suit, primarily from Europe and China, but only with unsecured bonds. The volume of outstanding bonds on the green bond market has at least doubled on an annual basis since 2012 and now exceeds the USD 150 billion mark.

Hardly any other market is experiencing such dynamic growth. In the current year, green bonds with a value of around USD 60 billion have been issued, well above the issue volume of around USD 48 billion for the full year 2015. The breakdown of issuers is also an indication of the huge growth potential of the market. For the first time, development banks rank second only behind banks which accounted for more than one third of the issues to date.

The reasons why not even more banks have yet entered the market are varied. The fact that green bonds require much more preparation than conventional bonds appears to be a key factor for many banks. In addition, the intended use of the proceeds of the issue must be clearly defined in detail. Processes for selecting projects must be established and it must be ensured that the proceeds are only used for suitable projects. Investors also demand an annual report on the actual use of the proceeds and the specific impacts of the projects on the environment. Finally, the sustainable effect of a green bond needs to be verified by an independent body or auditing company, usually a sustainability rating agency in the form of a second opinion. The issue of green covered bonds is also restricted by the artificially distorted and low spread as a result of the European Central Bank's (ECB) purchase programme.

The benefits of green bonds are evident – especially in the real estate sector. Real estate, depending on the source quoted, accounts for 30-40% of the energy needs and is responsible for around one third of CO^2 emissions. The bank supports the financing of energy-efficient buildings by granting a discount of between five and 10 basis points for loans. It thereby actively contributes to reducing energy needs and CO^2 emissions. The issue of sustainability is also an integral part of Berlin Hyp's corporate culture. The financing of green buildings and their refinancing via green bonds represents some of the sustainability measures that directly relate to its core business: commercial real estate financing. After all, it offers investors added value that considerably exceeds the interest rate and own creditworthiness. In return, green bonds offer the bank the opportunity to broaden its own investor base.

While Berlin Hyp has attracted 15 new investors with its Green Pfandbrief and generated an order book that was oversubscribed by a factor of four, the order book for the green unsecured bond had as many as 35 investors who had never subscribed to a Berlin Hyp bond before. The composition of the order book, almost oversubscribed by a factor of two and a half, was more international than any other of the bank's previous unsecured benchmark bonds. While German investors generally account for around 80 of such issues, almost half of the green bonds went abroad.

These facts could also encourage other banks to refinance loans secured by suitable real estate via green bonds. This would be highly welcome. If this is achieved through covered bonds, then all the better! The Initiative on Energy Efficient Mortgages launched by the EMF-ECBC on the 21st of September 2016 (see previous article) could make another important contribution towards this.

EMF Hypostat 2016

By Kaare Christensen, Association of Danish Mortgage Banks and Chairman of the EMF Statistics Committee, and Daniele Westig, Economic Adviser, EMF-ECBC

The 2016 edition of Hypostat was published by the EMF-ECBC on the 5th of September 2016 and made available for download via the EMF-ECBC website. Hypostat is an established source of statistics, information and analysis regarding the European mortgage and housing markets. The publication includes historical annual series for over 30 indicators covering, where data is available, the 28 Member States of the European Union (EU) and seven non-EU countries, namely Australia, Iceland, Japan, Norway, Russia, Turkey and the United States.

As was the case in the past, Hypostat 2016 brings together over 30 contributors who provide Country Reports for each EU Member State, giving details about their specific markets and outlining developments observed over the past year. Furthermore, Hypostat 2016 provides a general analysis of the European mortgage and housing markets. Moreover, it also includes a number of external articles which focus on different topics in every edition. This year, one of these articles studies the impact of the migratory influx on the German housing market while the other proposes an international comparative overview of the energy efficient dimension in the mortgage market. Hypostat 2016 has enriched the supply of data available to the reader, inserting a series of new statistics such as the average amount of a mortgage loan, the House Price Index of important cities and the stock of unoccupied dwellings.

Hypostat 2016 highlights some interesting trends observed in the housing and mortgage markets across the EU. These developments must be evaluated within the broader macroeconomic backdrop. The EU saw a growth of 2.0% in 2015 continuing the positive path started in 2013. Moreover, in aggregate terms, for the first time since the start of the crisis, the debt-to-GDP ratio decreased in the EU by 1.7 percentage points to 86.8%. A high level of fragmentation remains in the EU in terms of GDP growth. All countries except for Greece, which virtually reached 0% growth after a number of years of recession, had an economy growing at various degrees. Unemployment went down across the EU by nearly one percentage point. However, here too the picture across the EU remains very fragmented. Inflation, calculated with the Harmonised Index of Consumer Prices in the euro area, after reaching a virtual standstill at the end of 2014 remained around this level throughout 2015.

Against this backdrop, Hypostat 2016 describes and analyses some important developments in terms of housing and mortgage markets. For example, house prices in the EU (according to our methodology) continue the general positive trend of past years. Nonetheless, in those countries with ongoing contractions in house prices the rate has slowed, though recovery could be stronger. Thanks to the new statistics on house prices in cities a more complete picture can be drawn, showing that the heterogeneity in house pricing trends is not only present among countries but also within. Most of the countries registered national house prices moving at different paces depending on the region/city, with capitals and large cities leading the pack, and rural and remote regions retracting. House price increases in capital cities were on average more than 10 percentage points higher compared to the overall situation in their respective countries. At one end of the spectrum, house prices in Vienna increased by nearly 60 percentage points more than in the rest of Austria, whereas in countries such as Bulgaria, house prices in the capital showed a decrease of more than 10 percentage points compared to the rest of the country. Housing supply (as measured by the number of building permits issued, housing projects begun and housing projects completed) continued to pick up timidly approaching the level of 2009, while aggregate completions show an overall flat development since 2010 and housing starts slightly declined with respect to 2014.

From a historical perspective, 2015 saw the first time that the level of EUR 7 trillion in outstanding mortgage loans was reached, marking a 3.5% y-o-y increase confirming the positive trend of previous year. However, the euro area contribution to this positive result was only 1.5%, whereas the non-euro countries grew by 7.6%.

All in all, in line with the macroeconomic situation in the EU in 2015, the picture given of the housing and mortgage markets continued on the positive path already outlined in 2014, though fragmentation remains a major feature, observable through most indicators presented in Hypostat 2016. Fragmentation is, however, also very much present within individual countries, reflecting the many physical and location-specific factors that heavily influence the performance of the housing market, in addition to the macroeconomic elements. Hypostat 2016 also tries to give an idea of what these markets will look like in the coming months and years.

EMF Quarterly Review – Q2 2016

By Daniele Westig, Economic Adviser, EMF-ECBC

INTRODUCTION

The second quarter of 2016 ended with the decision of the UK to sever its ties with the rest of the EU, thus opening a period of potentially high political and economic uncertainty throughout the continent, which will manifest its effects on mortgage and housing markets in the months and years to come. For the time being, house prices in the EU[1] continue their upwards trend, on an aggregate level, while the outstanding mortgage lending figure in our sample, after having reached the peak end of 2015, has slightly contracted by 1.8% since then.

MORTGAGE LENDING

As seen during the previous quarter in the spring of 2016, at an aggregate level mortgage lending continues to increase, nuanced by national specificities with some countries also seeing their amount of outstanding mortgages slightly decrease.

In Central and Eastern Europe, several countries saw a pickup in their mortgage lending figures. In the **Czech Republic** gross lending increased by 20% in the first half of 2016 year-on-year (y-o-y), which, along with record levels of volume of mortgages provided, triggered a discussion around the possible beginning of a real estate bubble. Against this background, the Czech National Bank has introduced a recommendation that tightens mortgages with higher LTVs. Countries like **Hungary** and **Romania** also saw their gross lending increase substantially with respect to the same period of the previous year, by 60% and 113% respectively. In Romania especially the outstanding figures increased by 5% quarter-on-quarter (q-o-q) mostly due to the increase of new mortgages in local currency. The Non-Performing Loan (NPL) ratio for mortgage loans increased to 5.9% from 5.1% in the previous quarter due to the increase in the exposure of debtors deemed unlikely to pay while the volume of loans more than 90 days overdue continued to decrease. Local bank lending indicated an increase in credit standards, which curbed demand for mortgage loans. In Hungary a new decree requires commercial banks to fund at least 15% of their mortgage loan portfolios by mortgage bonds and will enter into force on the 1st of January 2017. Banks will therefore enter into refinancing agreements with mortgage banks. In **Poland** the Central Bank has tightened credit standards for housing loans for the fourth quarter in a row. Banks mainly tightened the collateral requirements by increasing the borrower's own contribution, raising margins and non-interest loan costs and due to a new Act of the 14th of April 2016, which restricts the trade in agricultural properties larger or equal to 0.3 hectares. Notwithstanding this tightening, in Q2 2016 a slight increase in mortgage lending was observed. The main reason was the approaching end of the government-subsidised "Flat for youth" housing scheme, which has already assigned all available funds for 2016 with funds for 2017 also already being fully reserved. In the analysed period this equated to 49,118 new housing loans being granted, an increase of 9.8% q-o-q. The aforementioned tightening is expected to continue into the next quarter with a consequent significant decrease in loan demand.

Moving to Scandinavia, **Sweden**, thanks to favourable macroeconomic conditions, improving household incomes, low interest rates and increases in population and urbanisation, depicts the well-known increase in mortgage lending; however, this seems to have levelled at around 8% y-o-y of net mortgage lending, representing an increase since the beginning of 2016, up from 7% during the same period of the previous year. Increasing household debts and house prices are heavily debated topics, and amortisation rules were imposed in June 2016 following different measures to cool down mortgage lending and house prices. In **Denmark** gross mortgage lending saw a small increase of DKK 16.7 billion in the second quarter of 2016 with respect to previous quarter, but the current DKK 99.8 billion is still DKK 66.6 billion short with respect to Q2 2015. Total outstanding residential loans were DKK 1,781 billion, which marked the highest value seen since Q2 2013.

In **France** the same dynamics as those seen since 2015 are in place, such as a dramatic drop in interest rates and an increased demand for housing. Moreover, the efficiency of government incentives for first-time buyers and investors encouraged the take-off of house building. As a result gross lending increased by 0.64% to EUR 36.1 billion in Q2 2016. In **Belgium** the decrease in credit production in Q2 2016 with respect to the same period in 2015 is mainly due to the exceptionally high and unprecedented number of external re-mortgaging actions taking place in Q2 2015. Indeed, considering only new mortgage loans without refinancing, the figures show a significant increase of 16.29% y-o-y reaching an all-time high of EUR 7.7 billion. Regarding the purpose of the credits granted, housing purchases, construction and purchase with renovation of houses increased by respectively, 12%, 47% and 7% and renovation and refinancing deals decreased by respectively 5% and 37%. As a rule of thumb, the ratio between the number of overdue contracts and the number of outstanding mortgage loans stays stable at around 1.1%, and follows the evolution of the increase of the total number of current mortgage credits.

On the Iberian Peninsula the increase of gross lending in this quarter did not translate into an increase of the outstanding residential mortgage figures. In **Portugal** the stock of residential loans decreased by 3.5% y-o-y, which followed a descending path starting at the end of 2011, flattening since the end of 2014. Gross lending stood at the highest value since Q2 2011 due to the positive perspective on the real estate market and improved macroeconomic and labour market conditions. Equally, in **Spain** gross residential lending has witnessed the best performance since Q4 2010 for the same reasons and despite the ongoing political uncertainty since December 2015. Re-mortgaging also increased notably by 12.7 percentage points, reaching 28.2% of gross residential lending in Q2 2016 with a weighted interest rate of 2.09%. Although the data for total outstanding residential loans in Q2 2016 is not yet available, it is expected to see the same trend as recent quarters with a decreasing, though flattening dynamic, as increased gross lending is still outpaced by amortised and cancelled loans.

[1] In Q1 2016 the sample of the proxy for the amount of total outstanding mortgage lending in the EU28 included BE, CZ, DE, DK, ES, FI, FR, HU, IE, IT, NL, PL, PT, RO, SE and UK. (i.e. around 95% of the total outstanding mortgage lending in the EU28 in 2015). Please, note that at the date of publishing, Q2 2016 data for FI and NL were not yet available and the most recent observations (all from Q4 2015) have been used.

In **Ireland** during Q2 2016 the volume for mortgages drawn down rose by 11.2% y-o-y to 6,803 and the value of mortgage drawdowns grew by 17.9% over the same period reaching EUR 1,286 million. In parallel, the number of mortgage approvals rose by 10% y-o-y. The second quarter marked a significant improvement with respect to the beginning of the year in terms of mortgage drawdowns and volume terms for property purchase, but in year-to-date terms 2016 was similar to 2015 with mortgage drawdowns for property purchase decreasing by 1.4% in volume terms and increasing by 4.9% in value terms. The Central Bank of Ireland has indicated that the limits on LTV and LTI ratios for new mortgages lending (introduced in February 2015), may have led to an initial surge in mortgage market activity, which, in turn, may have inflated the y-o-y drop in approvals in Q1 2016. In the UK the referendum held on the 23rd of June which favoured exiting the EU caused the prospects for the UK economy and the housing market to look very uncertain, as businesses and households adopt a wait-and-see approach for the next few months. Though this decision risks materially affecting prospects for the UK, the starting point is relatively favourable as macroeconomic fundamentals are sound. Gross mortgage lending fell with respect to the previous quarter but was higher than the same period of last year. A reason for the decrease with respect to the beginning of the year was the aftermath of an increase in stamp duty land tax for second homes. This meant that transactions were brought forward into the first quarter of the year to avoid paying a higher rate of tax. For the upcoming six months a slower pace in mortgage activity is foreseen. Lending will be driven more by re-mortgaging than by house purchases. Other factors restricting activity are the already elevated house prices relative to earnings, regulation in the home-owner space as well as the tight supply in the secondary housing market, which continues to cause supply/demand imbalances.

HOUSE PRICES

None of the countries of the sample depict a decreasing trend in the house price. The low interest rate environment together with the well-known demand and supply imbalances continue to support this trend with the usual national peculiarities.

In Central and Eastern Europe countries like the Czech Republic and Hungary depict increased property prices reaching new highs. Specifically, in the **Czech Republic** prices of apartments and housing parcels increased in Q2 2016 at the fastest rate since 2010. Overall the growth in demand for real estate remains bullish with some regional differences. In **Hungary** the number of housing permits grew by 77% q-o-q and by 164% y-o-y with Budapest having tripled this figure y-o-y. Despite the growth in building permit numbers, the number of dwellings handed over in Q2 2016 was still relatively low. However, this figure is expected to change in the near future due to the new dynamics in the number of housing permits issued. House prices continued to grow in Q1 2016, the latest available data, and surpassed the peak observed at the beginning of 2008. The growth rate was 7.6% q-o-q in nominal and 8.8% in real terms, showing the most significant quarterly growth observed since the onset of the Global Financial Crisis. The price development evolved heterogeneously throughout the country with Central Hungary and Western Transdanubia increasing by around 16% in Q1 2016 with respect to the average prices in 2015. **Poland** on the other hand depicts quite stable house prices in Q2 2016.

Moving north, in **Sweden** house prices are still growing buoyantly, though at a slower pace with respect to 2015, with one-family homes and apartments increasing by "only" 8.9% on a yearly basis. Prices for tenant owned apartments saw a 14% increase y-o-y, a decrease of 5 percentage points with respect to the previous year, and this lower growth rate is expected to continue into the next quarters. Though construction continued to increase both in 2015 and in 2016 up to Q2, the figures are still not enough to curb price increases and the quite strict building permits and building standards lead few to expect a construction boom in the country. In **Denmark** house price increases slowed down in Q2 2016 to 4% y-o-y with respect to 5.8% in the same period of 2015. This increase was principally due to the increase in both prices of one-family houses and owner-occupied flats, which grew by 3.7% and 4.4% respectively. Along with house prices, transactions increased during 2016, which rose by 22.5% for one-family and 12.9% for owner-occupied flats in Q1 2016, compared to the 4.3% and 4.9% increases respectively in 2015.

In **France** the progressive take-off of the housing market caused the existing house prices not to decline further in Q1 2016, the latest data available. For existing houses by the end of June 2016 a price increase of 2.6% was seen with respect to the same period of last year. The latest data available shows a 0.3% y-o-y drop in collective housing along with a 0.8% y-o-y increase in the country excluding Paris, while new house prices rose slightly for both types of houses during the same period. In **Belgium** prices for both existing and newly-built houses increased by 2.1% and 3.1% respectively y-o-y. In Q2 2016 the average price of an ordinary house was around EUR 208,000, which marked a 2% increase y-o-y, similar for villas which, on average, cost a little more than EUR 347,000. As for apartments, they increased by 1.9% y-o-y reaching an average of EUR 222,000. In **Germany** the ongoing supply and demand imbalance, especially in city centres, together with improving macroeconomic factors and the lack of investment alternatives continues to push house prices upwards. New construction growth currently provides little relief due to the time lag, which is a result of long planning and investment periods. More specifically, the vdp price index for owner-occupied housing, condominiums and semi-detached houses rose by 6.3%, 7.3% and 5.9% y-o-y respectively. In the medium-term rents are expected to continue their upward trends, particularly as the law introduced to cap rent does not seem to be producing the desired effect.

In **Spain** the improved fundamentals improved the house price index by 2% y-o-y setting a price of EUR 1,506 per square metre. **Portugal** also shows a positive trend, which has lasted for the last four quarters, registering a 6.3% y-o-y increase due to the limited construction of buildings against a growing demand of housing purchases and loan requests.

Moving to **Ireland**, a new index has been developed which takes into account the transaction of all properties and not only those based on mortgage transactions. With this new index property prices increased by 4.9% y-o-y and by 3.8% in Dublin, while the rest of the country increased by 11.3%. Rents also continued to increase more outside of Dublin than in the capital and, in general, they increased faster than house prices. As in other countries the reason for this upward trend is to be found in the improved macroeconomic fundamentals and insufficient building activity. In the UK house prices continued to grow, notwithstanding the already elevated house prices relative to earnings. Would-be movers are being put off marketing their property as a result of the heightened uncertainty due to Brexit concerns and perhaps not being able to find properties suitable for them to move to.

MORTGAGE INTEREST RATES

Against the background of the very accommodative monetary policy of the European Central Bank (ECB) and its peers, mortgage interest rates continue to stay very low, but more and more jurisdictions are aware that the bottom floor has been reached and some timid signs of increases have been spotted. The continued low interest rate environment shifted countries to more fixed rate contracts since customers would like to lock-in the benefits of the low price of money for buying their homes.

In the **Czech Republic**, notwithstanding the slight decrease in Q2 2016, subsequent reductions will be unlikely. Moreover, with the approaching of the new Consumer Credit Act, which transposes the EU Directive 2014/17/EU, banks are trying to convince customers to take out mortgages with longer maturities (up to 10 years) to lock-in clients as much as is possible before a renegotiation. In **Hungary** the further cut of the interest rate of the Central Bank from 1.05% to 0.9% led to a subsequent drop in the typical mortgage loan's variable rate to 4.56% at the end of the period. The most typical interest rate is the variable one linked to the three-month BUBOR (Budapest Interbank Rate), but fixed rates are also offered. In **Romania**, with mortgage rates at 3.32%, these were slightly below the level of Q1 2016.

In **Sweden** mortgage interest rates were stable in the last quarter. Variable and medium-term initial fixed rates increased slightly to 1.4% and 1.6% respectively, while the longer initial fixed rates decreased slightly to 2.4%. In **Denmark** interest rates with different initial fixed periods moved in opposite directions with short fixed term loans increasing slightly and long fixed term loans decreasing by 0.32 percentage points to 3.35%. The representative interest rate on new loans rose marginally to 1.26%.

In **France** interest rates continued their downward path reaching an average of 1.69% and in the UK mortgage rates continued to fall in Q2 2016 on a number of measures reaching or setting new record lows.

In **Portugal** the variable interest rate applied by banks is made up of two components, the external index such as the three- or six-month Euribor and a spread. With the former at minimum levels, average mortgage interest rates have also been decreasing since Q2 2014, reaching 1.86% in Q2 2016. From the available indicators it can be said that **Spain** concluded the adjustment process and started the consolidation of a stable recovery of the housing market, but the path is still long. Interest rates in Spain remained low together with the Euribor, the benchmark for 91% of Spanish mortgages, which reached its historic low of -0.056%. The average interest rate for residential loans was 2.04% in Q2 2016, 21 basis points less than the interest rate asked a year ago. On quarterly terms all rates dropped and all except the medium-term fixed registered a historic low in Q2 2016. The ongoing low interest rates, coupled with the benefits in terms of financial stability and planning, increased the attractiveness and therefore the market share of long-term fixed rate loans, which represented more than a third of new loans in Q2 2016, compared to 10.7% in Q1 and to the marginal 1% in Q4 2014. The foreseen lack of change in market conditions will continue to favour long-term fixed loans in the upcoming quarters. In **Ireland** 34% of new mortgage loan agreements, including renegotiations, were based on fixed rates, namely those with an initial fixation period of more than one year. This figure confirms the share of fixed rates since Q1 2015, compared with the long-run average of only 20%. Mortgage rates on outstanding loans are also heavily influenced by the ECB base rate because about half of all mortgages outstanding are on tracker rates, which average 1.01%. In **Belgium** around 91% of loans have a fixed period of more than 10 years while those with an initial fixed period of between three and 10 years count for around 8%, leaving only a marginal amount of loans with an initial fixed period of up to one year.

Chart 1a ▶ Countries where gross residential lending has remained below 50% of 2007 levels

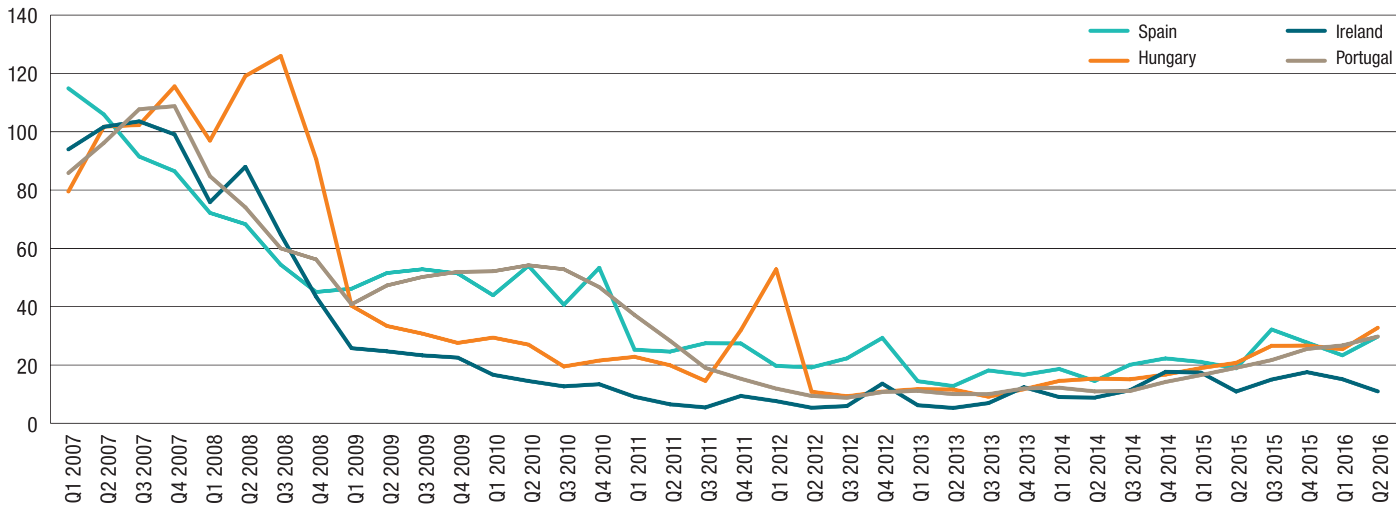


Chart 1b ▶ Countries where gross residential lending has remained below, but above 50% of, 2007 levels

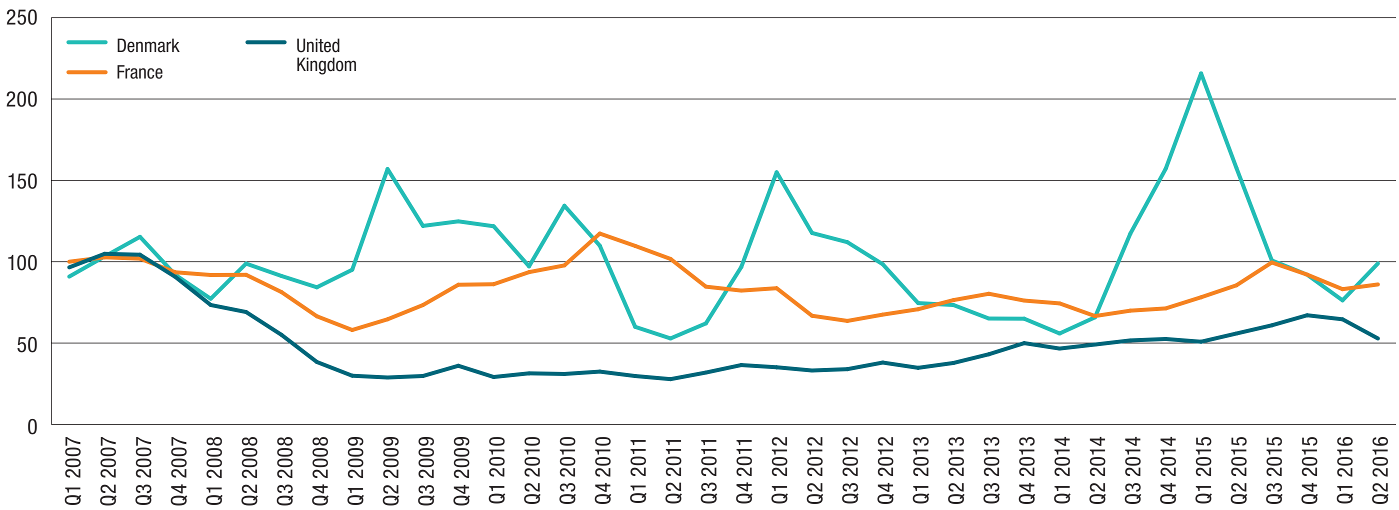


Chart 1c ▶ Countries where gross residential lending has risen above 2007 levels

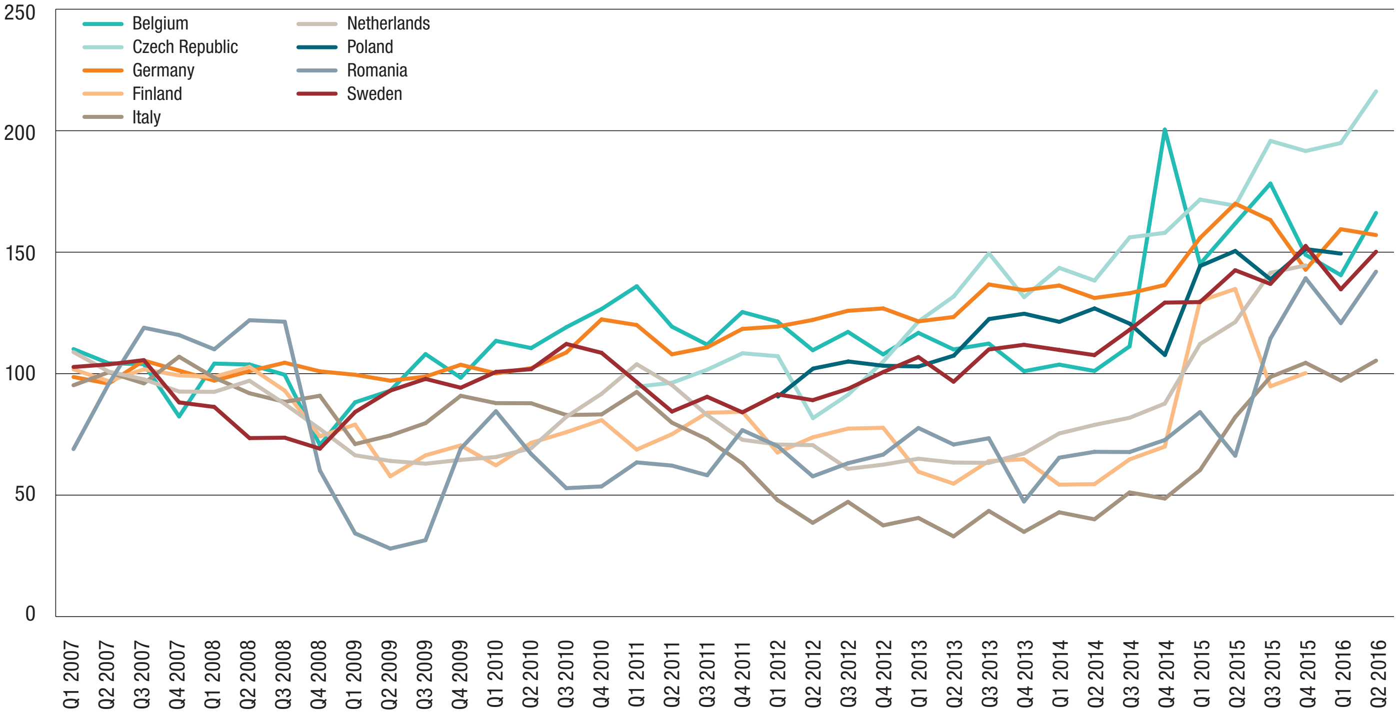
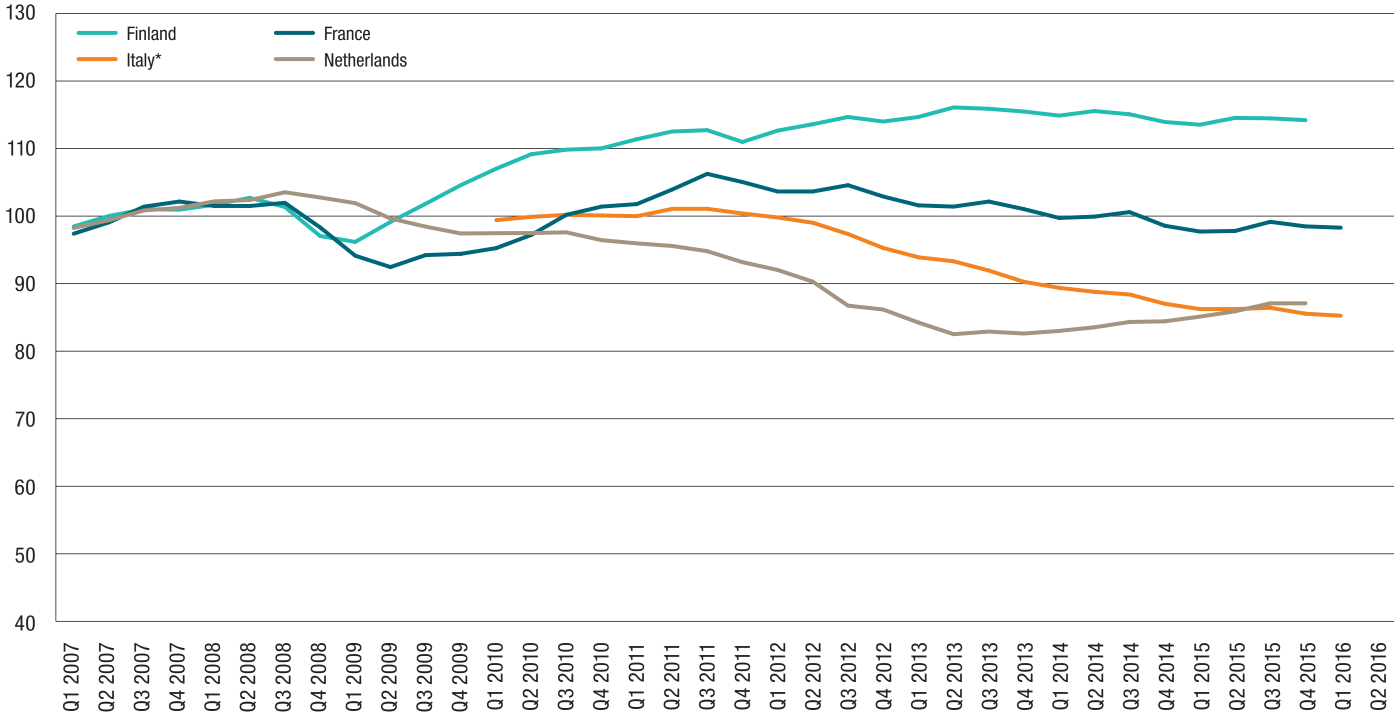


Chart 2a ▶ Countries where house prices have fallen in the available latest quarter



** 2009 = 100*

Chart 2b ▶ Countries where house prices have risen slightly over the latest quarter

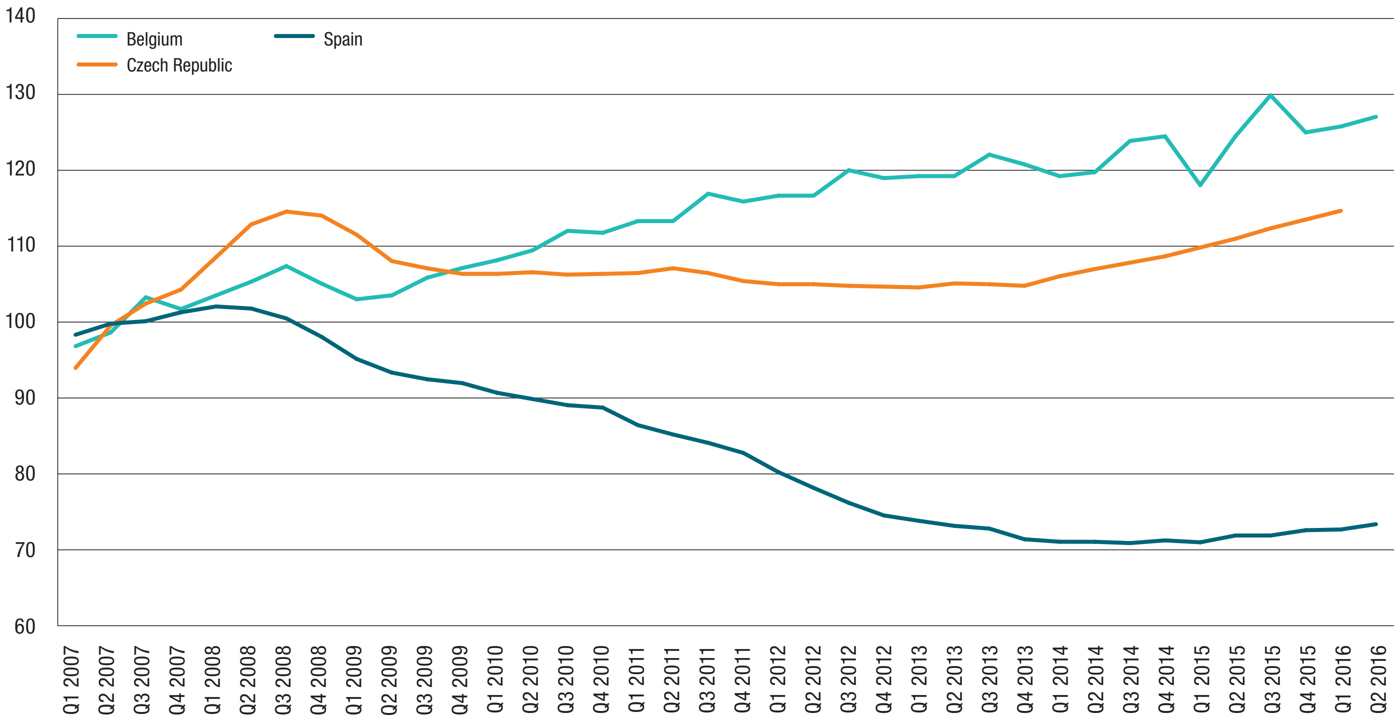
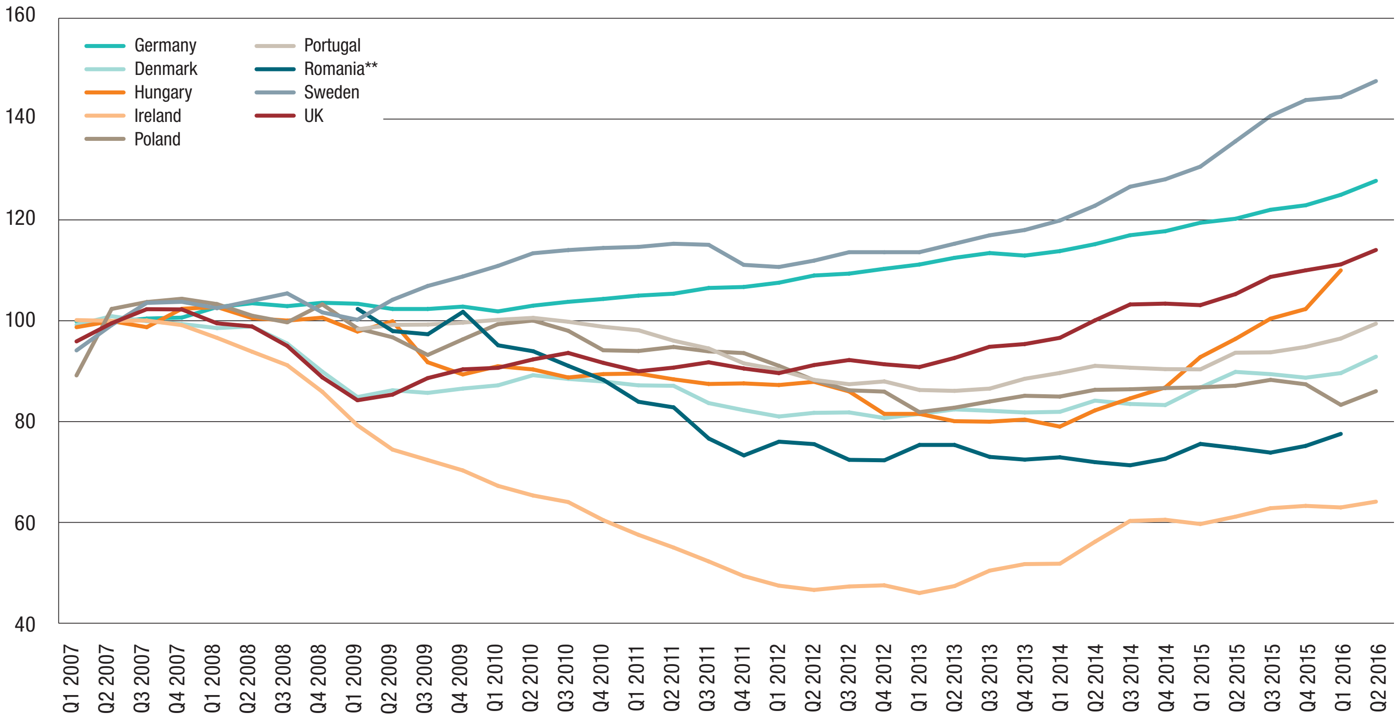


Chart 2c ▶ Countries where house prices have risen by at least 1.5% over the latest quarter



*** 2010=100*

Covered Bond Harmonisation: Where do we stand?

By Alexander Batcharov and Anne Caris, Bank of America Merrill Lynch
& Joost Beaumont, ABN AMRO Bank N.V.

COVERED BOND HARMONISATION: WHERE DO WE STAND?

We address in this article recent developments about the two legs dominating the discussion on harmonisation in the covered bond market: (1) data disclosure and transparency and (2) legal frameworks.

1. HARMONISING TRANSPARENCY

By Alexander Batchavrov and Anne Caris, Bank of America Merrill Lynch

In the covered bond community, disclosure and transparency have been key topics in the spotlight in recent years. On the 16th of June 2015, following on from intense discussions and debates initiated in 2010 under the umbrella of the ECBC Technical Issues Working Group, the Covered Bond Label Foundation (CBLF) and the European Covered Bond Council (ECBC) announced the decision to implement the Harmonised Transparency Template (HTT) across jurisdictions for all covered bond issuers that hold the Covered Bond Label.

The HTT has come into force since 1st January 2016 and is a binding requirement for the granting and renewal of the Covered Bond Label with a phase-in period of one year. Once fully implemented, it will have a direct impact on more than 70% of eligible covered bonds[1] – in Europe but also globally. Singapore was the first to launch the HTT, an initiative seen as a positive and important step by market participants and regulators.

Why the Harmonised Transparency Template (HTT)

The HTT is replacing the 14 National Transparency Templates (NTT) established for the Covered Bond Label. While they contributed to enhanced reporting practices, the NTTs have been heterogeneous and have not fully met market expectations. The HTT was put together by a Transparency Task Force (TTF) organised by the ECBC in November 2014 which consisted of 20 individuals from different countries and backgrounds (issuers, analysts, covered bond associations, data providers, etc.).

The TTF's approach was pragmatic, keeping in mind the costs and benefits for the industry as a whole. The TTF debated at length national differences, an obstacle to full harmonisation, and ultimately reached a consensus in order to harmonise data disclosure and further enhance transparency in the covered bond market. Market participants were consulted extensively during the process – among which investors.

The HTT is notably addressing the following investors' needs and wish list regarding disclosure:

- Harmonised data in a more user-friendly downloadable format (i.e., available in Excel).
- Harmonised definitions by issuers – ideally across jurisdictions and, if not possible, at least within a jurisdiction (definitions should be disclosed).
- Harmonised timing as issuers should disclose relatively recent data.
- Disclosure of key details – e.g. regulatory treatment, maturity structures, involved counterparties, levels of committed over-collateralisation and covered bond structures.
- No loan by loan data was required however, being used only by a small minority of investors. The availability of historical series was seen as more important.

Work done so far

After a few months, the HTT is already global. While Singapore was the first country to adopt the HTT in February 2016, the HTT initiative was followed by several issuers across Europe shortly after – e.g. France, Italy, Spain, the UK. More countries, both European and non-European, are in the pipeline. Implementation has been smooth and has entailed:

- An in-depth review of each new HTT to ensure consistency across countries.
- An active dialogue with the issuers e.g., on how to improve reporting or answer any uncertainty.
- A new logo for the HTT to flag to investors when an issuer has switched to the HTT from the NTT.

Positively, the HTT format allows issuers to further reflect their national specificities – thus enabling a flexible and exhaustive reporting as need be, in an efficient way with all the data being typically disclosed in one single file. A dual format has been highly encouraged and typically made available, or at least the Excel version, even though the later should not be a barrier to the HTT implementation.

What's next

The HTT will remain a dynamic process in order to meet investor and issuer requirements and ensure its appropriateness as the covered bond industry further develops. For example, during the first few months of 2016, some Labelled Issuers as well as investors presented requests for minor modification of the HTT. For example, some market participants would like to have additional information on interest rate risks (i.e., before and after hedging like for currency risks), counterparty risk for swaps or conditional pass through triggers.

Any modification of the HTT will be presented to the Covered Bond Label Committee, which will consider and analyse their merits and any potential modifications agreed will be implemented in 2017. As such, with a view to collecting feedback and/or concerns raised by Labelled Issuers during the implementation phase in 2016, the ECBC has launched a Review Process which will allow market participants to comment while minimise the sudden shifts of the HTT by only introducing changes in 2017. Such review process will guarantee that all feedback is taken into account and help preserve harmonisation efforts.

2. HARMONISATION OF LEGAL FRAMEWORKS

By Joost Beaumont, ABN AMRO BANK N.V.

Another key issue that is currently topping the agenda of the covered bond community is the drive for harmonisation and/or convergence of national covered bond frameworks in the EU. Back in 2014, the European Banking Authority (EBA) noted that more convergence was needed among covered bond frameworks in the EU in order to increase the safety and robustness of the covered bond instrument. It would also strengthen the EU covered bond market more generally, in the end supporting financial stability as well. Overall, the EBA identified some areas where convergence of frameworks was needed in the medium to longer term, also to continue to warrant the preferential risk weight treatment of covered bonds. The key areas were:

- Dual recourse mechanism;
- Segregation of cover assets and bankruptcy remoteness of covered bonds;
- Cover pool features;

[1] That is Capital Requirements Regulation (CRR) compliant covered bonds.

- Valuation of cover assets and LTV limits as well as other requirements on mortgage cover assets;
- Coverage principle and legal over-collateralisation;
- Asset and liability risk management;
- Covered bond monitoring;
- Role of supervisor;
- Investor reporting.

European Commission consultation on Covered Bonds

The discussion on covered bond harmonisation was taken to another level last year, when the European Commission (EC) published a consultation paper on covered bonds in the European Union (EU). This was part of the EC's Action Plan to build a Capital Markets Union.

The consultation paper was published at the end of September 2015 and responses could be submitted until the 6th of January 2016. It was the EC's aim to 'evaluate signs of weaknesses and vulnerabilities in national covered bond markets as a result of the crisis, with a view to assessing the convenience of a possible future integrated European covered bond framework that could help improve funding conditions throughout the Union and facilitate cross-border investment and issuance in Member States currently facing practical or legal challenges in the development of their covered bond markets'.

The consultation was driven by the fact that covered bonds are regulated by national laws, which has resulted in fragmentation as well as inefficiencies according to the EC (and especially fragmentation between the core and peripheral countries). In order to reduce fragmentation/inefficiencies, the EC proposed several options for convergence of covered bond frameworks. These were:

1. Voluntary convergence of Member States' covered bond laws in accordance with non-legislative coordination measures such as targeted recommendations from the Commission.
2. An EU covered bond legislative framework seeking to harmonise existing national laws.
3. A new EU law framework for covered bonds (29th Regime), as an alternative to national laws.

Having said that, the EC also mentioned in the consultation paper that it would take a cautious approach. Indeed, it did not want to disrupt existing covered bond markets, which have actually functioned well.

The Industry's response to the consultation

By the 6th of January 2016, the EC had received 72 responses. In this article, we would like to highlight the response of the ECBC, as it is the main representative of the covered bond industry, including issuers, analysts, bankers, investors, rating agencies and other stakeholders.

The ECBC welcomed the EC's cautious approach, noting that the subjects addressed in the consultation paper are of 'crucial importance to the very different legislative frameworks that exist in Europe'. It further stressed that the reason of national differences are a 'consequence of historical national differences in terms of mortgage markets, housing policies, consumer behaviour, insolvency law, credit and valuation regulation etc.', and that full harmonisation of EU covered bonds laws was an 'utopia'.

Nevertheless, the ECBC noted further that it saw room for improvement and further convergence in specific areas, as this would continue to justify the preferential regulatory treatment of covered bonds, while also enhancing transparency, which would be beneficial for investors.

Overall, the ECBC was of the view that the EC should find a balance between maintaining national covered bond legislative frameworks and establishing a common European framework. It could do so 'by means of (i) a recommendation to encourage Member States to increase convergence and (ii) a high quality principle-based directive ensuring harmonisation of certain minimum standards'.

According to the ECBC, 'a combination of a recommendation and a principle-based directive will ensure that national markets continue to function, whilst safeguarding the prominent role of covered bonds as a crisis management tool able to promote: (i) investors' confidence; (ii) financial stability; and (iii) long-term financing'. Such a solution would also maintain competition among EU covered bond markets, which can be beneficial for investors that will then still have some different flavours to choose from.

The public hearing on 1 February

On the 1st of February 2016, a one-day public hearing on the EC's consultation process was held in Brussels. The EC reiterated that it had no intentions to overhaul the covered bond market. Indeed, EC Commissioner Lord Hill said in his opening speech that the aim is not to have a harmonised framework, but that the goal is to see whether best practices can be used to create a more integrated market and to assess what legal barriers stand in the way. He added that the EC does not want to hurt a well-functioning market, which was in line with general feedback from most participants. The general message from participants at the conference was that an integrated EU framework for covered bonds would not result in a material change in pricing or increase in the investor base. Therefore, a pan-EU framework should be flexible and principle-based, if any.

It seems that the EC has taken aboard these considerations, although it said in its first CMU Status Report that harmonisation would result in better comparability of national covered bond frameworks, which could result in deeper, more liquid and more robust national markets. Meanwhile, it also mentioned that participants had 'encouraged the Commission Services to explore further the potential for greater market integration based on high-level principles, respecting national specificities and building on frameworks that are currently working well'. At the time of writing, the EC considers the next steps, which are expected later in 2016.

Convergence: where do we need to go?

We, the authors, agree the view that if established, a harmonised covered bond framework should be high-level and principle based. Overall, however, we wonder whether it is really necessary to move to an integrated EU covered bond framework. In our view, the EBA best practices already provide a sufficient incentive for convergence of covered bond frameworks, while also harmonising reporting standards. The EBA has been clear that jurisdictions need to implement the best practices in some key areas in order to keep warranted the preferential risk-weight treatment of covered bonds. If implemented, we expect that this will be a sufficient incentive for countries to properly implement these, lessening the need for additional EU wide regulation. The update of the Dutch covered bond law as of the 1st of January 2015 was for instance according to the lines of the EBA best practices, and could be an example for other countries.

What is more, we see a risk that the setup of a pan-EU covered bond framework could create some uncertainty, harming an already well-functioning market. More important is that covered bond frameworks will continue to show differences, which we do not see as a bad thing. It often reflects national specifics (e.g. legal, housing) and it also offers room for diversification. In the end, harmonisation/strengthening covered bond frameworks is a good thing, but it is no panacea.

This article is taken from the 2016 edition of the ECBC's European Covered Bond Fact Book, the full copy of which can be accessed here.

NEWS IN BRIEF

EBA Says That Core Funding Ratio Cannot Replace NSFR When Assessing Funding Risk

On the 8th of September 2016, the European Banking Authority (EBA) published a Report analysing the core funding ratio across the EU. The Report, available here, is in response to a request from the European Commission to explore the possibilities of the core stable funding ratio (CFR) as a potential alternative metric for the assessment of EU banks' funding risk, taking into account proportionality. The Report concludes that, overall, it would be misleading to rely only on the CFR to assess banks' funding needs because, unlike the Net Stable Funding Ratio (NSFR), the CFR does not look at the whole balance sheet of a bank and, therefore, cannot fully assess a potential funding gap. This Report is based on the same QIS data used for the NSFR Report published in December 2015 comprising 279 banks. The reference date of the analysis is December 2014.

The report shows a lack of correlation in terms of outcome and conclusions between the NSFR and the CFR for the whole sample of EU banks and particularly for the smaller ones. This is mainly due to the fact that CFR assesses the funding risk only considering the liabilities side of banks irrespective of the stable funding needed by the various types of assets they may have. The NSFR, on the contrary, provides a full funding risk assessment considering both sides of the balance sheet.

For this reason, the EBA believes that the CFR cannot replace the NSFR, which appears to be the most accurate metric for assessing banks' funding risk.

Background and Legal Basis

To recap, following the publication of the NSFR Report in December 2015, on the 12th of April 2016, the European Commission sent a call for advice to the EBA requesting an assessment of the CFR as a potential alternative metrics to the NSFR for the analysis of funding risk. The EBA responded to the Commission on the 11th of May 2016 informing that some quantitative information would be provided on the basis of the data available at the moment. The EBA report has been submitted to the Commission.

ESAs Reject Proposed Amendments from European Commission to Technical Standards on Non-Centrally Cleared OTC Derivatives

On the 9th of September 2016, the three European Supervisory Authorities (ESAs – European Banking Authority (EBA), European Insurance and Occupational Pensions Authority (EIOPA), European Securities and Markets Authority (ESMA)), published their Opinion addressed to the European Commission expressing disagreement with its proposed amendments to the final draft Regulatory Technical Standards (RTS) on risk mitigation techniques for OTC derivatives not cleared by a central counterparty (CCP), which were originally submitted for endorsement on the 8th of March 2016.

Following the European Commission's communication on the 28th of July 2016, of its intention to endorse the ESAs' final draft RTS with amendments, the ESAs issued an Opinion rejecting some of the proposed changes. In particular, the ESAs disagree with the European Commission's proposal to remove concentration limits on initial margins for pension schemes and emphasise that these are crucial for mitigating potential risks pension funds and their counterparties might be exposed to.

In addition, in the Opinion the ESAs observed the following:

- As with other thresholds in the RTS submitted to the European Commission, the calculation of the threshold against non-netting jurisdictions should consider both legacy and new contracts.
- With reference to covered bonds, the additional condition included in the European Commission's proposed amendments would have the effect of ranking derivatives counterparties after bond holders, which is contrary to the reasoning established in European Market Infrastructure Regulation (EMIR) to grant a preferred treatment to cover bonds.
- The ESAs recommend providing clarity that non-centrally cleared derivatives concluded by central counterparties are not covered by this regulation. This has been a source of concern for stakeholders.
- More clarity should also be brought to the application of the RTS to transactions concluded with third country counterparties, in particular non-financial counterparties.
- The delayed application to intragroup transactions should be maintained to allow national competent authorities to complete the relevant approval process before the obligation will start applying.

The ESAs believe that the introduction of a number of wording changes proposed by the European Commission may lead to a different application of the provisions compared to their original text of the RTS and, therefore, advise amending them accordingly.

A version of the draft RTS containing all the aforementioned corrections in detail is included as an Annex to the Opinion, which is available here.

ESAs Highlight Main Risks for the EU Financial System

On the 7th of September 2016, the Joint Committee of the European Supervisory Authorities (ESAs – European Banking Authority (EBA), European Insurance and Occupational Pensions Authority (EIOPA), European Securities and Markets Authority (ESMA)) published its latest Report on Risks and Vulnerabilities in the EU Financial System (available here).

This Report focuses on recent developments concerning the low growth and low yield environment and its potential effects on financial institutions' profitability and asset quality, and highlights concerns related to the interconnectedness in the EU financial system. These risks have persisted for some time and can be related to lasting effects of the 2007 financial crisis. However, the EU financial system is also vulnerable to more immediate risks such as the result of the UK referendum on EU membership which has added political and legal uncertainties to those already affecting the financial system.

Commenting on the publication of the Report, Gabriel Bernardino, Chairman of EIOPA and the current Chair of the Joint Committee, said, *"The Joint Committee proactively considers key risks to financial stability and assesses risk mitigation policies in cooperation with national and European institutions. We are considering the possibilities for further enhancing monitoring of financial industries, reinforcing adequate capital or risk buffers as well as ensuring adequate resolution arrangements for affected sectors. The Joint Committee is committed to providing a strong and streamlined supervisory response both on a micro- and macro prudential level, which is required by the challenging economic environment."*

Low Growth and Low Yield Environment

Low growth and low yields affect the financial services industry through various channels. Interest rates and growth expectations have decreased further and are posing new challenges to the entire financial sector. Low interest margins significantly constrain banks' profitability, while life insurers' and pension funds' liabilities increase as it becomes more difficult to generate high investment returns. This environment may lead banks, insurers, pension funds and other investors to engage in risky search-for-yield behaviour, adding to already elevated risks around asset valuation and adjacent concerns about market liquidity.

The Joint Committee considers it essential to further develop effective recovery and resolution schemes in all relevant sectors, to employ adequate stress testing procedures and to enhance the monitoring of relevant risk drivers.

Profitability of Financial Institutions

Low quality of assets in many countries, conduct costs and growing competition from non-bank and non-insurance financial institutions negatively affect the profitability of banks and insurers. Subdued returns, further lowered by fees and charges, reduce the attractiveness of investment funds. While the EU-wide bank stress test results have demonstrated the importance of a better capitalised banking system, the high levels of non-performing loans (NPLs) exacerbate concerns about medium-term sustainability. Addressing NPLs as a major driver of uncertainties in the financial system has become a key challenge, and further NPL resolution requires comprehensive and proactive action among all relevant stakeholders. Following the UK referendum, profitability risks may be further intensified. Expectations of weaker macroeconomic conditions are amplified by growing political risks within the EU and globally. In addition, traditional financial service providers are facing increasing competition from Fintech providers which will further challenge the sustainability of their business models.

Responding to this risk, the ESAs say supervisors need to encourage steps to adjust business models in search for sustainable income, to address excess capacities as well as to monitor and assess the impact of emerging innovative technologies and market practices.

Interconnectedness within the Financial System

The ESAs see that the interconnectedness between the financial sector outside of the banking, insurance and pension fund industries with the wider financial system is increasing, as cross-sectoral exposures, asset price commonalities and the interdependency of business processes augment. The Joint Committee therefore considers that related stability risks should be assessed thoroughly to mitigate the increasing risk exposure outside the traditional financial system.

EBA Publishes Results of CRD IV-CRR/ Basel III Monitoring Exercise

On the 13th of September 2016, the European Banking Authority (EBA) published its 10th report of the CRD IV-CRR/Basel III monitoring exercise on the European banking system. This exercise, run in parallel with the one conducted by the Basel Committee on Banking Supervision (BCBS) at a global level, presents aggregate data on capital ratios – risk-based and non-risk-based (leverage) – and liquidity ratios – the liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) – for banks across the European Union (EU). It summarises the results using data as of the 31st of December 2015.

Overall, the results of this exercise show a further improvement of European banks' capital positions, with a total average Common Equity Tier 1 (CET1) ratio of 12.7% at end December 2015 assuming full implementation of the CRD IV/CRR. The banks in the sample largely respect the future regulatory capital requirements, with only a very small number of institutions showing potential capital shortfalls. The shortfall amount to meet the full-implementation minimum CET1 requirement (7%) has been continuously shrinking since mid-2011, and was at its lowest level (EUR 0.4 billion) at end December 2015.

The analysis of the leverage ratio shows that there has been a continuous increase in the last periods. A significant number of institutions in the sample would be constrained by the minimum leverage ratio requirement (3%) rather than by risk based standards.

The LCR analysis is based on data in accordance with the Commission's Delegated Regulation. The average LCR is at 133.7% at end December 2015, and 91% of the banks in the sample show an LCR above the full implementation minimum requirement applicable since January 2018 (100%). In addition, time-series analyses show that the weighted average LCR has increased since June 2011, mainly due to an increase in banks' liquidity buffers.

In the absence of a finalised EU definition, the report monitors the NSFR compliance with the current Basel III standards. The analysis shows an overall average ratio of 107.0% with an overall shortfall in stable funding of EUR 240.1 billion.

Around 79% of participating banks already meet the minimum NSFR requirement of 100%. Compared with previous periods, there has been a continuous increase in banks' NSFR, which is mainly driven by the increasing amount of available stable funding (ASF) for both groups.

The full EBA report on the monitoring exercise is available here.

24th ECBC Plenary Meeting – Video Highlights

On the 14th of September 2016, the ECBC hosted the 24th Plenary meeting in Düsseldorf, Germany, with the kind support of **DZ Bank**. The event saw over 340 stakeholders in the covered bond space from around the world come together to discuss the key issues affecting the market at this time, including:

- Demographic and social changes impacting on mortgage markets
- Legislative evolution towards bond-holder protection, with a particular focus on the German Pfandbrief
- Liquidity in covered bond markets
- Harmonisation of covered bonds
- Covered bonds post-Brexit
- Global developments in covered bonds
- European Secured Notes (ESNs)
- Green Covered Bonds and Funding Energy Efficiency

The full **Agenda** for the 24th Plenary meeting can be accessed here and we are pleased to announce that a series of short **videos** highlighting the key issues discussed are now available to watch here.

The 25th Plenary meeting will take place in **Oslo**, Norway, on the **6th of April 2017** with the kind support of **Finance Norway**.

ESAs Fourth Joint Consumer Protection Day

On the 16th of September 2016, the European Supervisory Authorities (ESAs – European Banking Authority (EBA), European Insurance and Occupational Pensions Authority (EIOPA), European Securities and Markets Authority (ESMA)) organised their fourth Joint Consumer Protection Day in Paris. Key amongst the topics addressed during this event was the European Commission's Green Paper on Retail Financial Services.

Speaking on this subject, the following points were made by Olivier Salles, Head of Unit – Retail Financial Services and Payments, DG FISMA, European Commission:

- An Action Plan will be published by the end of the year.
- Very similar concerns were raised within the various respondent groups - i.e. consumers raised similar concerns, industry raised similar concerns etc.
- Consumers in particular raised concerns about access to information, trust of foreign providers in a cross-border context and actual access to products.
- Potential areas of follow-up are likely to include the following:
  - An analysis of comparison websites.
  - A focus on improving redress mechanisms, with an emphasis on the better exchange of information and cooperation between national competent authorities (including a boost to FINNET), and more powers for financial ombudsmen.
  - An assessment of the potential for an optional harmonised cross-border product with certain features inspired, for example, by the UCITS directive.
  - An assessment of the differences in national regimes which can limit accessibility to and eligibility for products and services.
  - An analysis of the potential that digitalisation is bringing, as well as the opportunities and threats. Particular attention will be given to e-recognition and digital signatures.

The EMF-ECBC will keep monitoring developments in relation to the Green Paper on Retail Financial Services insofar as they impact upon European mortgage and covered bond markets, and further information will be reported in future editions of Market Insights & Updates as is necessary.

EBA Harmonises the Definition of Default Across the EU

On the 28th of September 2016 the European Banking Authority (EBA) published its Final Report on the Guidelines on the Application of the Definition of Default (available here) and a Final Report on Draft Regulatory Technical Standards on the materiality threshold of past due credit obligations (available here). The result of the quantitative and qualitative impact study aimed at assessing the impact on the regulatory capital requirements of selected policy options to harmonise the definition of default used by EU institutions was also released (available here).

To recap, under a CRR mandate according to Article 178 (7), the EBA launched in September 2015 a public consultation on guidelines intended to harmonise the definition of default across the EU prudential framework, which is intended, in turn, to improve consistency in the way EU banks apply regulatory requirements to their capital positions. In addition, Article 178 (6) of the CRR mandates the EBA to specify the conditions according to which a competent authority shall set the materiality threshold for credit obligations past due.

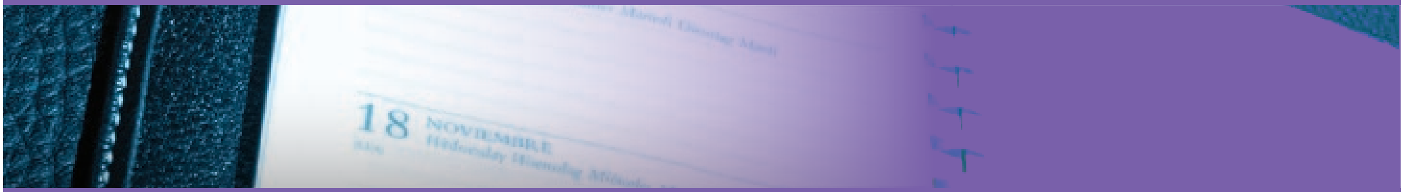
The **published guidelines** provide detailed clarification on the application of the definition of default, which includes aspects such as the days past due criterion for default identification, indications of unlikeliness to pay, conditions for a return to non-defaulted status, treatment of the definition of default in external data, application of the default definition in a banking group and specific aspects related to retail exposures. The guidelines are intended to increase comparability of risk estimates and own funds requirements, especially when using IRB models, and will help reduce the burden of compliance for cross-border groups, thus reducing overall risk-weighted asset variability across institutions. The guidelines will apply from the 1st of January 2021, but institutions are encouraged to implement the changes prior to this date in order to build the necessary time series.

The **draft Regulatory Technical Standards** (RTS) specify the conditions for setting the materiality threshold for credit obligations that are past due and harmonise the structure and application of the threshold, which will entail an absolute and a relative component. The levels of the threshold will be set by competent authorities and will be subsequently implemented by all institutions in a given jurisdiction. It is suggested that the relative threshold should be set at the level of 1% for both retail and non-retail exposures. However, if a competent authority considers that this suggested level does not reflect a reasonable level of risk it may set a relative threshold at a different level, which in any case must be lower than or equal to 2.5%. The EBA foresees the implementation of the draft RTS may have a significant impact on the operations of some institutions, in particular those that use the IRB Approach and where the threshold will change significantly, the implementation of the necessary adjustments may require some time. Hence, it is recognised that institutions will need sufficient implementation periods that will allow the changes to be introduced in an efficient manner.

The **quantitative and qualitative impact study** (QIS) presents detailed information about the current practices of institutions with regard to key aspects of the definition of default and provides an estimated impact of selected policy scenarios on the capital requirements and capital adequacy ratios of institutions. The QIS results are the basis for the impact assessment carried out on the guidelines and the RTS.

It is worth highlighting that the published guidelines and the draft RTS are part of a broader regulatory review of the Internal Ratings Based (IRB) Approach carried out by the EBA as outlined in the Report published on the 4th of February 2016 (available here). However, the harmonised definition of default will apply to all institutions, including those using the Standardised Approach.

In terms of next steps, competent authorities will report whether or not they comply with the EBA's guidelines within two months of the publication of the guidelines in the official EU languages.



AGENDA

OCTOBER 2016

04/10	Hungarian Green Building Council Conference on Economic, Environmental and Social Aspects of Green Buildings – Budapest
05/10	European Covered Bond Council (ECBC) Supervisory Task Force Meeting with the European Banking Authority (EBA) – London
06-07/10	15th International Conference on Credit Risk Evaluation: Credit Solutions for the Real Economy: Implications for Investors, Financial Stability and Policy Design – Venice
07/10	European Mortgage Federation (EMF) Legal Affairs Committee Meeting – Bucharest
14/10	European Mortgage Federation (EMF) Economic Affairs Committee Meeting – Amsterdam
18/10	Swedish Green Building Council's Building Sustainability 2016 Event – Stockholm
19/10	European Parliament Financial Services Forum (EPFSF) Event on Cyber Security – Brussels
20/10	Long-Term Investment and Reindustrialisation Intergroup Debate on "Energy Renovation: A long-term viable investment for the EU" – Brussels
21/10	Maastricht University Conference on Sustainable & Healthy Homes – Maastricht
27/10	ICO & IE Business School Seminar on the Importance of Bond Markets to Finance Projects and Industry, Including SMEs – Madrid

NOVEMBER 2016

07-18/11	Conference of the Parties (COP 22) in session – Marrakech
08/11	European Parliament Financial Services Forum (EPFSF) Event on Global Standards for a 'Bail-In' Tool: Implementation Challenge in the Context of an Effective EU Resolution Framework – Brussels
10/11	European Mortgage Federation (EMF) Valuation Committee Meeting – Brussels
14/11	UNECE Real Estate Market Advisory Group (REM) & vdp Conference – Berlin
17/11	European Covered Bond Council (ECBC) Steering Committee Meeting – Brussels
18/11	European Mortgage Federation (EMF) Executive Committee Meeting – Brussels
22/11	IMN Conference on Italian & European Non-Performing Loans (NPLs) – Milan