Mortgage Lenders & Capital Markets supporting an Affordable & Sustainable Housing Ecosystem

Unaffordable housing is a matter of great concern in the European Union (EU). It leads to housing insecurity, financial strain, and inadequate housing. It also prevents young people from leaving their parental home, impacting their mobility in the single market and limiting their labour/life opportunities. These problems directly affect people's health and well-being, embody unequal living conditions and opportunities, and result in increased healthcare costs, reduced productivity, and environmental damage. In the past decade, homeownership in the EU has decreased overall, driven in particular by a drop in homeownership among young people. There has been an increase in Europeans living in apartments, concentrated in towns and suburbs.

At the same time, the last several years have seen a growing urgency to improve the energy efficiency of buildings with a view to saving energy, reducing bills for citizens and small enterprises, tackling energy poverty and achieving a zero-emission and fully decarbonised building stock by 2050. In order to achieve these objectives, the Energy Performance of Buildings Directive (EPBD) requires massive scale renovation of Europe's private and public housing stock.

This dual challenge of delivering both affordable and sustainable housing will require substantial investment on the part of Member States, local authorities and private citizens. Particular attention will need to be paid to the needs of fragile groups, including the younger generation which has limited access to housing and elderly people who are the owners of their homes, but may in many cases have limited access to finance. Against this backdrop, the pressure to achieve a more sustainable and affordable housing landscape is combined with the need to build a social inclusion pathway and structural investments. Addressing these challenges will require vast domestic and international support, mixing public subsidies and injecting private capital market resources, potentially supported by a new set of products, including 'renovation certificates' as tradeable instruments modelled on green certificates in energy markets and carbon credits. Combined and coordinated actions from the public and private sectors will help to ensure the scaling-up of effective housing policies and broader access to capital markets, and foster the development of global opportunities for lenders and investors while benefiting consumers.

It is against this backdrop, combined with increasing geopolitical instability, social inequality, and market volatility, that the EMF-ECBC has identified the need for concrete, tangible measures for citizens and global leadership in implementing common market best practices that will support **sustainable and affordable developments in the European housing sector and the real economy**.

As the market price for housing can be adjusted by increasing the supply of housing, the primary goal should be the creation of more housing units if more affordable housing is to be achieved in the EU. And even though many people may prefer to own their home, it is important to focus not only on homeownership, but also on rental homes. Renovating vacant and/or dilapidated buildings can also contribute to the goal. It is equally important that the different challenges in the individual Member states as well as already well-functioning models are considered when developing a new framework and new financing models.

Mortgage lenders and capital markets have played and will continue to play a crucial and catalytic role in supporting economic transition, providing the means to respond to local, regional and national needs – especially with regards to access to housing, with an overarching European financial infrastructure which supports the EU's leadership in ESG policies as a geopolitical financial model. In this context, designing an affordable and sustainable housing ecosystem that supports citizens, investors, and lenders is an opportunity to generate both macro- and micro-economic growth models.

Established in 1967, the **European Mortgage Federation** (EMF) is the voice of the European mortgage industry, worth over **€9 trillion** at the end of 2023 (*EU27 + UK, Norway, and Iceland*). In 2004, the EMF founded the **European Covered Bond Council** (ECBC), bringing together covered bond market participants worldwide, including issuers, analysts, investment banks, rating agencies, and a wide range of other stakeholders. ECBC members represent over 95% of covered bonds outstanding, which were worth over **€3.3 trillion** globally (*of which €2.9 trillion in the EU27, UK, Switzerland,*

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Norway, and Iceland) at the end of 2023. Through its membership, our organisation represents more than **2,000 financial institutions** in more than **60 jurisdictions** encompassing the entire mortgage credit value chain from retail to funding activities.

We stand ready to assist the EU institutions by sharing knowledge, advice, best practices, cooperating, and supporting the housing agenda with an ecosystem approach, bringing affordability, energy efficiency, and renovation solutions over the coming years. In particular, we believe that we can provide a tangible contribution with our expertise in developing and leading global market initiatives such as the **Covered Bond Label** with its specific disclosure section of the Harmonised Transparency Template for Green & sustainable Covered Bonds, the **Energy Efficient Mortgage Initiative** (EEMI), **Energy Efficient Mortgage Label**, the **International Secondary Mortgage Market Association** (ISMMA) and a global housing and housing finance database (HOFINET). Initiatives, where innovation and harmonisation of best practices have already facilitated a leveraging of the market to scale-up efficiencies, demonstrate both the capacity and willingness of our sector to assume and play its full role here.

During the recent periods of market turmoil, pandemic, and technological innovation, the EMF-ECBC has played a prominent role as a market catalyst through its efforts to monitor and align best practices in promoting dual recourse instruments to support funding in housing, the public sector, and the real economy. Furthermore, through its technical committees, working groups, and task forces, the EMF-ECBC has developed technical knowledge and centres of competence in both the mortgage and covered bond businesses, with a focus on retail considerations, property valuation, prudential regulation, and funding strategies, to name but a few key areas. By adopting a "think-tank" approach and adhering to a clear global market governance structure, the EMF-ECBC has applied this expertise to help minimise market disruption. At the same time, through the initiatives highlighted above, it has sought to deliver active coordination and implementation of an operational market toolkit aimed at harmonising procedures, standards, definitions, and solutions.

As an industry representing over **€9 trillion** of mortgages outstanding, equal to **40% of the European GDP**, we would like to actively contribute by proposing constructive ideas which can help in creating a sustainable and affordable Housing Ecosystem:

1. Market governance and coordination between public and private sector stakeholders
2. Capital Markets support and guarantee scheme
3. Additional funding options to scale up capital markets resources for a Housing Ecosystem

1) Gathering international industry and institutional intelligence to support the housing sector offering market governance and institutional cooperation between the public and private sectors.

The lack of affordable housing in Europe, particularly in larger cities, is highlighted as an increasing concern in relation to Europe's economic growth and productivity. The affordable housing initiative was announced in the Commission's renovation wave strategy for Europe, which aims to green buildings, create jobs, and improve lives. This strategy intends to at least double renovation rates in the EU by breaking down long-standing barriers to energy and resource-efficient renovation, as well as improving reuse and recycling. By 2030, the construction sector could see 35 million renovated buildings and up to 160,000 additional green jobs.

The EMF-ECBC stands ready to deploy all its market intelligence and international networks for the creation of two intelligence think-tanks: firstly, an **Institutional Advisory Council**. Secondly, an **Industry & Market Steering Committee** in support of housing sector development, securing a steering market governance, fostering cooperation between private and public sectors, scaling up resources and market intelligence for an affordable and sustainable European plan.

(1) The **Institutional Advisory Council** aims to immediately optimise and coordinate public resources available for the sector and align long-term market and supervisory national best practices with European legislative benchmarks. The primary objective of the Advisory Council will be to ensure strategic coordination among government agencies, international financial institutions (IFIS/DFIS), and investment companies in designing and implementing comprehensive policies and reforms in the field of housing in Europe and neighbouring countries.

(2) The **Industry & Market Steering Committee** aims to build capacity and facilitate the optimisation of housing strategies by combining public subsidies and fostering the development of capital market instruments and resources. The primary objective of this Committee will be to secure a scaling-up of the market and of the engagement and coordination among international and domestic stakeholders active in the financial and housing value chain (such as developers, financial intermediaries, lenders, system providers, rating agencies, investors, and others), in designing and implementing comprehensive market actions and best practices in the field of housing. The banking industry's engagement will reinforce the Ecosystem's capacity building, boosting private lending capabilities, consumer awareness, and investors' demand.

Against the background of the strategic importance of the housing sector in promoting social stability, improving citizens' well-being, creating jobs, and stimulating the construction industry and related economic sectors, the Institutional Advisory Council's activities will focus on developing effective financial mechanisms, mobilising investment and advancing regulatory solutions aimed at the sustainable development of housing infrastructure. The development of the capital market sector could enlarge the scope of action of the Housing Ecosystem by deploying solutions impacting public sector infrastructure and SME financing, allowing for the medium and long-term optimisation of the use of public resources in these sectors.

The EMF-ECBC is willing to act as a market and institutional incubator platform to launch a series of initiatives focused on systemic capacity building, developing market and institutional leadership and coordination for the creation of a sound, sustainable and affordable housing ecosystem:

- The establishment of an **Institutional Advisory Council** for the development of the housing sector under the leadership of the European Authorities, to ensure a comprehensive, balanced, and institutionally coordinated approach to policymaking and reform in the housing finance sector. This Institutional Advisory Council is expected to include representatives from the following institutions:

Institutions
European Parliament
Council of the European Union
European Commission as **"Moderator"**
United Nations Economic Commission for Europe (UNECE)
United Nations Environment Programme Finance Initiative (UNEP FI)
Organisation for Economic Co-operation and Development (OECD)
European Bank for Reconstruction and Development (EBRD)
The World Bank
International Finance Corporation (IFC)
Housing Finance Information Network (HOFINET) Wharton School
Università Ca' Foscari (Venice)
Climate Bonds Initiative
Nordic Investment Bank
European Investment Bank (EIB)
European Mortgage Federation - European Covered Bond Council (EMF-ECBC)

- Next to the Institutional Advisory Council, it is essential to gather international market engagement and intelligence with the **Industry & Market Steering Committee**, translating international European capital market resources into local solutions and adapting market action to the dynamic needs of a new Housing landscape. The core tasks of the Industry & Market Steering Committee will include: supporting the development of well-balanced public policies and reforms in the housing sector; facilitating the use of long-term financing instruments such as securitisation and covered bonds mechanisms, including to catalyse sustainable long-term investment in the housing & public sector.

Market Stakeholders
These are expected to number c. 20 participants and include representatives of housing market stakeholders, lenders, covered bond and securitisation issuers, investment banks, system providers and rating agencies drawn from the membership of the EMF and the ECBC.

In the context of capital market development in a potential long-term alignment with the Savings and Investment Union (SIU) debate, it is essential to underline the critical complementarity in securing optimisation of access to capital markets played by both covered bonds and securitisation, two key mechanisms for bank funding and capital market development, albeit each with distinct structures, risk profiles and regulatory frameworks. In the context of the current political debate, these instruments play unique but mutually reinforcing roles in the financial ecosystem offering:

1. **Diverse Funding Sources:** Covered bonds and securitisation offer banks diverse funding options. Covered bonds offer stable, long-term funding with lower risk, while securitisation allows banks to achieve efficient capital management with the benefit of redeploying capital in segments of interest and free up regulatory capital. There is very little overlap between the two investor groups, and the complementarity in the funding mix allows the use of both tools, mobilising two very different parts of the market to the needs of housing finance.
2. **Market Stability and Resilience:** The dual recourse nature of covered bonds contributes to financial stability, particularly in times of crisis. By distributing risk across a broad base of investors, securitisation enhances market resilience through accrued risk sharing and supports credit availability.
3. **Enhanced Liquidity:** Both instruments contribute to market liquidity. Covered bonds are typically highly liquid, making them attractive for institutional investors. Securitisation can create liquidity for less liquid asset classes, broadening access to funding.
4. **Investor Diversification:** Each asset class's different risk profiles and structures attract a wide range of investors, from conservative to risk-seeking. Diversifying the investor base enhances the robustness and depth of capital markets.
5. **Regulatory Balance:** Harmonised regulatory frameworks for covered bonds and securitisation under the CMU ensure high standards of transparency, quality and investor protection, fostering trust and participation in European capital markets.
6. **SME Financing:** European Secured Notes (ESN) and SME securitisation are mutually complementary as ESNs would be issued based on an issuance programme, therefore acting as a resilient funding instrument for SMEs, especially in times of market volatility where issuers can react quickly according to the economic context, whereas securitisations would finance SMEs through investors' differing risk appetites and would be issued via stand-alone transactions in periods of market stability. Furthermore, ESNs are also complementary to the importance of balance sheet SME securitisations, which are currently allowing banks to off-load portions of their regulatory capital, allowing new credit issuance to the real economy.

7. **Economic Growth:** Both instruments support economic growth by improving banks' and businesses' access to finance. Covered bonds provide stable funding for mortgages and public sector projects, while securitisation facilitates credit for a wide range of economic sectors, including SMEs and consumer lending.

This strategic complementarity also offers unique value in terms of the ability of these asset classes to support housing solutions and the transition to a climate-neutral economy due to their pivotal role in forging a path to sustainable growth, stability, and shared prosperity. Capital market solutions continue to evolve and expand, transcending borders and bridging gaps between capital markets and the real economy.

2) Single Market Initiative: Quality labels, transparency for investors, lenders and consumers, the way forward

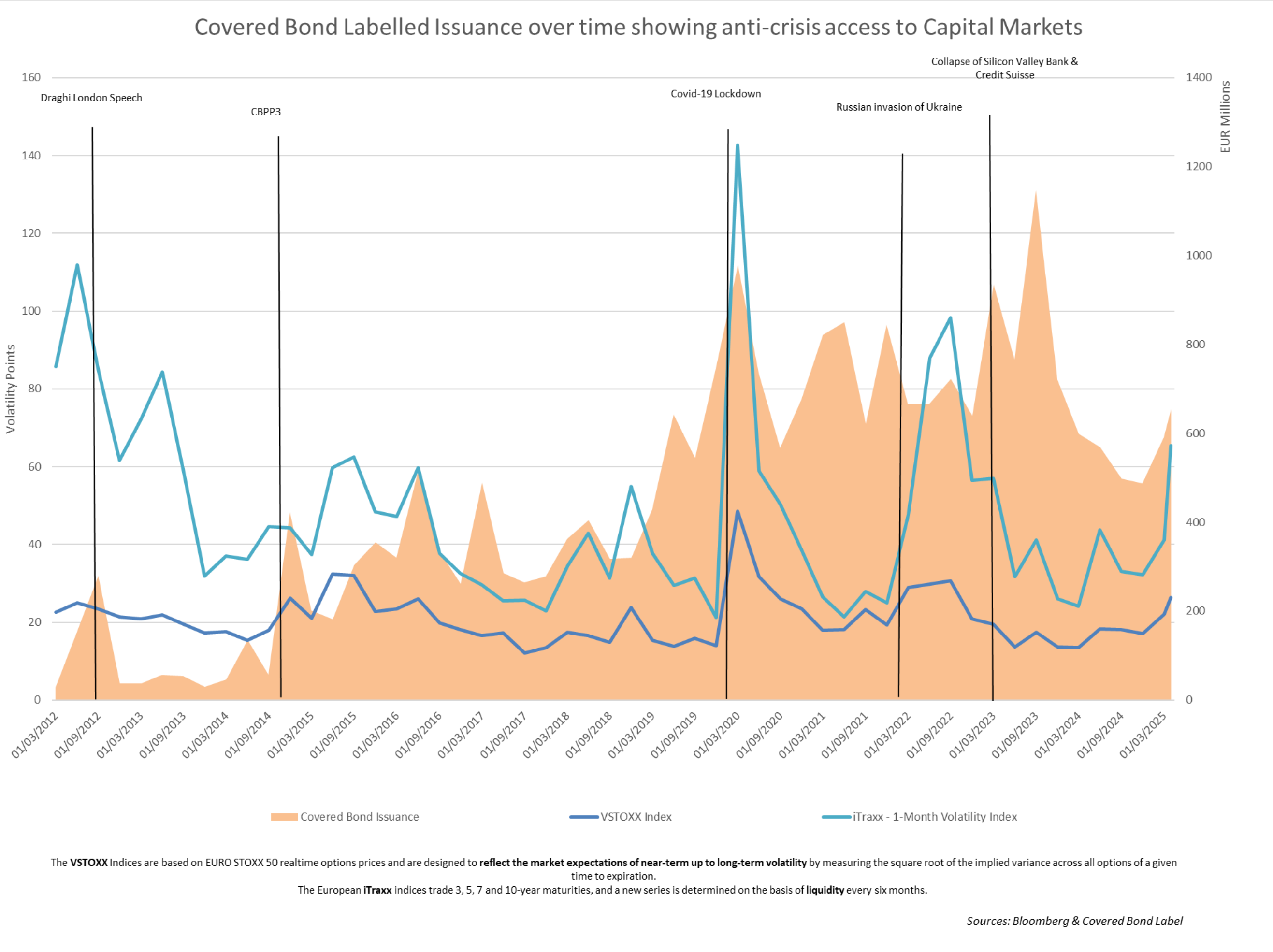
A European Mortgage Label supported by a guarantee scheme to boost market convergence, digitalisation, sustainability, affordability and competitiveness.

During the recent years of market turmoil and volatility of deposits, lenders have been able to secure access to capital market funding by relying on the 250 year old DNA of covered bonds and their macroprudential characteristics, including low volatility, exceptionally low transaction execution risk, superb credit ratings and decreased refinancing costs, and limit banks' reliance on riskier funding means and interbank markets.

This anti-cyclical, long-term financing instrument has become a pillar of financial stability and is the nexus between harmonised European financial innovation and the traditions that sit within national legal frameworks.

Together, via the harmonisation and convergence of efforts through the entry into force of the Covered Bond Directive and the ongoing pursuit of third-country equivalence for non-EEA countries, our industry continues to push geographical barriers.

Figure 1: Covered Bond Labelled Issuance over time showing anti-crisis access to Capital Markets

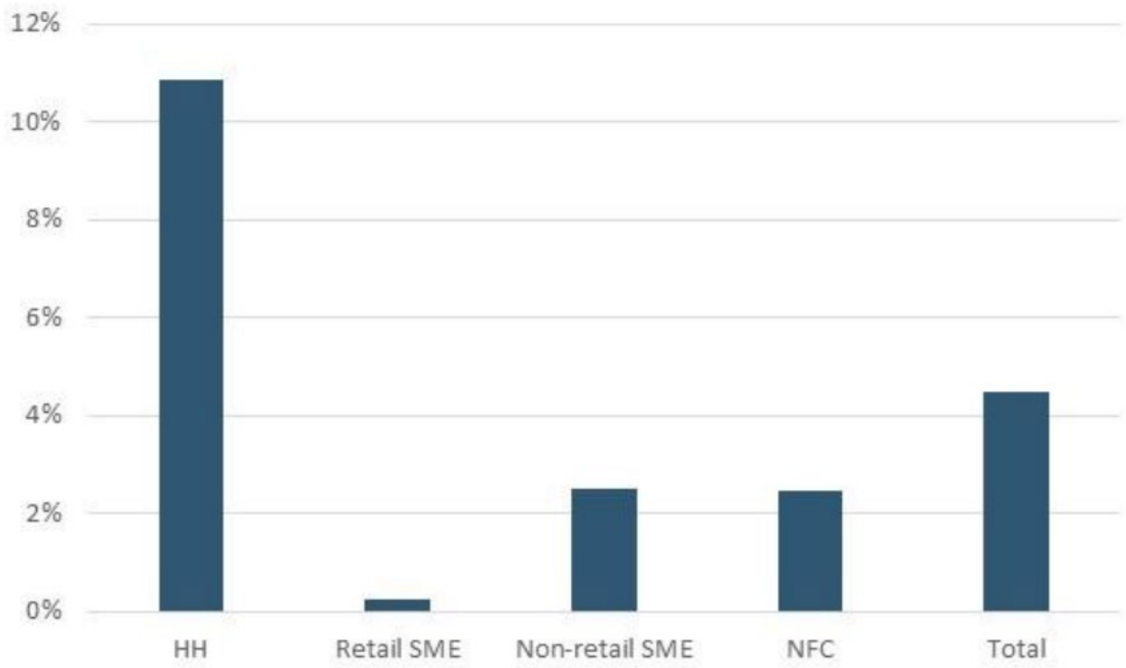


Source: Bloomberg & Covered Bond Label

Following on from the success of initiatives such as the Covered Bond Label, a market "reopener" in stress scenarios which has delivered a globally recognised quality label for a 3 trillion euro asset class, the Mortgage Industry has developed the Energy Efficient Mortgage Label as a strong sustainable European Label for the entire Industry, which allows lenders to converge from national market practices to standard European best practices, thereby boosting sustainability and transparency and therefore investor confidence, as well as digital solutions which support data gathering and disclosure with alignment to the EU Taxonomy.

Moreover, the significance of the transformative impact of the Energy Efficient Mortgage Label Initiative in the mortgage market towards innovative convergence in sustainable best practices has made Housing Loans the greenest asset in the single market as recognised by the EBA Report delivered in response to a call for advice of the European Commission on Green Loans and Mortgages (link). According to the EBA, the share of green loans and advances contributing to the Green Asset Ratio (GAR) is 11% in the household portfolio, 98% of which finances residential real estate (RRE). This compares to a total share of credit institutions' green loans and advances across all business lines of on average 4.5% of their total loans.

Figure 2: Share of green loans in total loans (by business line)



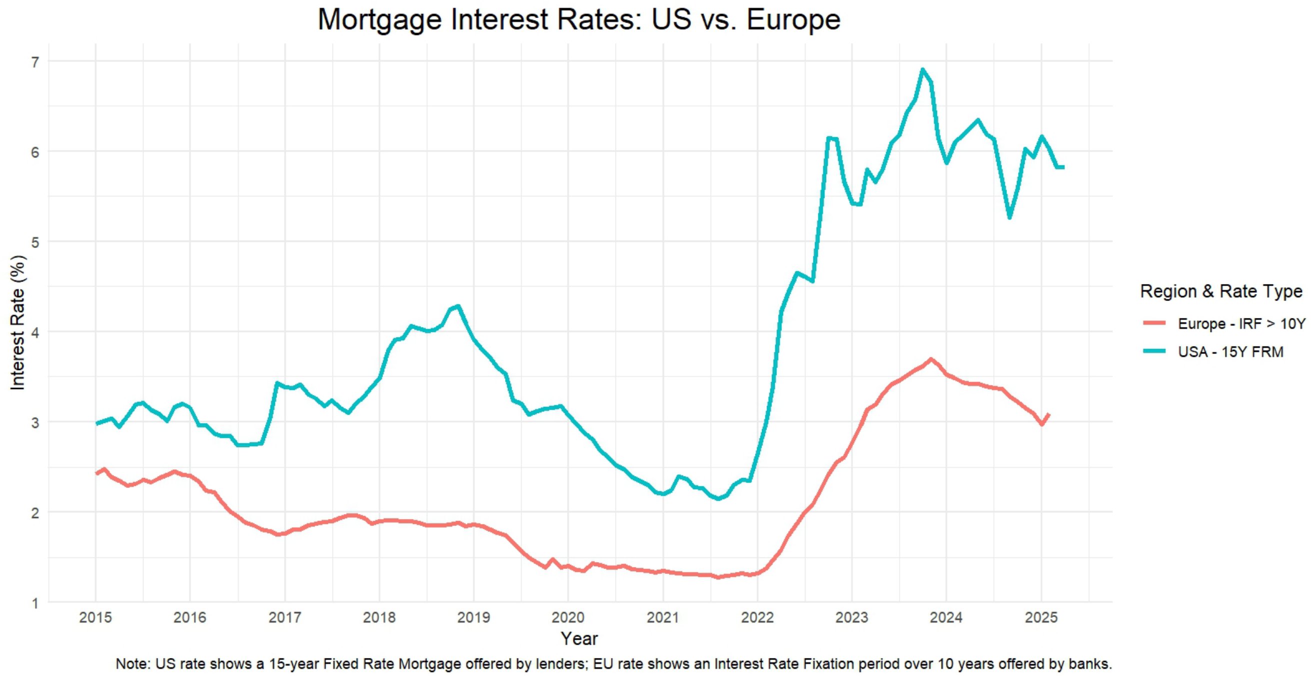
Source: EBA

These initiatives, rooted in the sound legal framework of the Mortgage Credit Directive, the Banking Union, and the Covered Bond Directive, have created a genuine European anti-crisis financial umbrella, providing financial stability, supervisory alignment, and long-term, cost-efficient financing of national mortgage portfolios via a real single market European financial asset class.

All in all, these developments have made the European mortgage sector particularly resilient to crisis scenarios. The Industry has remained extremely attentive to responsible lending and borrowing practices, optimizing Asset Liabilities Management (ALM). Funding strategies have reinforced ALM's financial stability by keeping mortgage portfolios on balance sheet, using long-term funding instruments, such as covered bonds. Incidentally, long-term funding capabilities, among other factors, have facilitated the provision of a range of product options for consumers, amongst which fixed-rate mortgages, in particular, have shielded European families from unexpected increases in their housing costs due to rising interest rates in the wake of an inflation crisis, coupled with protection from rising energy prices through sustainable financing solutions under the Energy Efficient Mortgage Label.

In the EU, almost one in three people were unable to meet unexpected financial expenses (32%). Housing costs typically represent one of the largest expenses for Europeans, therefore representing a critical element from both a micro perspective for families and citizens more generally, and from a macro perspective, in terms of economic growth, financial stability, and public resources. The European model has made mortgage markets an essential social lift, supported by capital markets resources, whilst freeing up public resources. Indeed, a key element to make home ownership accessible for private households is the provision of affordable loans by banks. This is equally true for the energy-efficient renovation of existing buildings and the construction of affordable (rental) housing. We would therefore like to take this opportunity to underline the importance of also addressing potential obstacles stemming from banking regulation, that make lending unnecessarily burdensome and expensive. Furthermore, securing a global level playing field and the preservation of the current important but fragile equilibrium between public and private financing is even more crucial in this geopolitical moment, and with the implementation of the Basel III framework where every euro coming from capital markets resources is a euro saved on public debt (see Figure 3). The competitiveness of the European model is therefore of paramount importance. European banks compete globally on capital markets, where capital and funding costs determine their capacity to actively serve households and families.

Figure 3: Residential Mortgages rates US and the Euro area



Source: ECB, Freddie Mac

With the strategic aim of scaling up private investment in the housing and renovation sectors, the Industry stands ready to use this quality Label as benchmark for retail and funding activities, thereby establishing clear European affordability criteria and a data toolkit, which allow the entire Industry to provide a European sustainable and affordable housing finance solution based on a level playing field for citizens, consumers, lender and investors.

The Institutional Advisory Council, in liaison with the Market Steering Committee, could advise and develop a housing roadmap whereby a pool of public guarantees could support the market activities of lenders in providing housing loans to fragile borrowers such as first home buyers, young families, and elderly people for renovation. For guarantee facilities, the larger and the more diverse the pool, the easier it becomes to manage the risk. These guarantees could be linked to the European Mortgage label, which will frame lenders' activities in a clear, sustainable, and affordable European perimeter.

The combined use of European Labels for retail and funding activities, together with a European guarantee scheme[1], would:

- Create a single market initiative to improve consumers' access to finance, boost demand and market offer, securing a broad set of options and protection for citizens, and raising awareness of sustainability and climate change
- Improve competitiveness of the banking sector by optimising retail and funding strategies, reinforcing their positioning in the new Basel III landscape
- Improve lending volumes for SME, local authorities, and citizens, all players in the overarching Housing Ecosystem
- Scale up & focus public and private resources on common targets and objectives aligned to the EU Taxonomy
- Enhance the speed of execution and data quality in the mortgage value chain with a digital solution for consumers, lenders, and investors

[1] This should not be seen as an EU Government-Sponsored Enterprise, such as Fannie Mae in the US.

- Gather building passport and EPC data, facilitating the value chain, and efficiently creating sustainable retail and funding products and bonds.
- Facilitate access to credit for borrowers through the presence of the guarantee, which will further speed up the execution of the lending process
- Ensure industry engagement and steering alongside institutional and market coordination, providing for monitoring and calibration of market and policy actions

Taking inspiration from successful national guarantee schemes, such as Fondo Prima casa "First Home Loan Guarantee Fund" (IT), Prima / Noua Casa (RO), Spiti Mou (Greek for "My Home") (GR) , where based on an initial state guarantee, banks have been able to lend with a leverage factor of 10 /12 times. Taking the example of Italy, a state guarantee of 500 mn euros generated 50 bn euros of banking lending volumes with a probability of default of 0.8% and streamlined access to finance to fragile borrowers, such as first home buyers, low-income households, and young families. This has helped banks in scaling up lending volumes to fragile borrowers as a result of reduced execution risk, whilst optimising Risk Weighted Assets (RWA). This has been a major achievement:

1. Accessibility: The fund has made it easier for young people and families to access homeownership, especially in cities with high property prices.
2. Subsidised Loans: By providing subsidised loans, the fund has lowered the financial burden on first-time buyers, making mortgages more affordable.
3. Encouragement of Sustainable Living: Many initiatives under the fund promote energy-efficient homes, contributing to environmental sustainability.
4. Economic Boost: By facilitating home purchases, the fund has positively impacted the real estate market and stimulated related sectors, such as construction and home furnishings.
5. Awareness and Education: The fund has raised awareness about homeownership opportunities and provided educational resources for navigating the buying process.

As mentioned above, it is important to not only focus on homeownership but also on the adequate provision of rental homes. For instance, the public housing sector in Denmark is the leading participant in the rental housing market, supplying high-quality youth, family and senior housing to a diverse section of the Danish population as regards both age and socio-economic standing. Public support in the form of capital contributions, mortgage subsidies and guarantees for mortgage loans are central elements of public housing financing. Regardless of whether it is a new build or a renovation project, the financing is based exclusively on loan capital.

One potential initiative among the members of the Institutional Advisory Council could be to gather resources for the creation of a European guarantee scheme that could help the banking sector lend retail products to targeted borrowers, social segments, in a framework that enhances affordability, sustainability, and data quality.

The elements that a guarantee/guarantee fund must have in order for the mitigation instrument to be an effective measure for access to credit are as follows:

(i) The guarantee must be 'Basel-compliant', i.e., it must allow for a reduction in the prudential ratio applicable to the exposure covered. In general, for public funds, the State counter-guarantee allows a 0% weighting to be applied (it is understood that the guarantee must comply with all other subjective elements, including the fact that the coverage is on first demand (i.e. immediately enforceable upon default of the guaranteed party), direct, irrevocable and unconditional;

(ii) The guarantee must be easily and quickly activated, without administrative burdens that increase management time and costs, and the guarantee should not diminish the eligible outstanding for the cover pool;

A European scheme providing a calibrated 30%-50% guarantee of the loan with 0% RWA would help banks in:

- **Setting a European single market framework:** Setting a common single market product perimeter using a common eligibility framework with a set of criteria & data requirements at the European scale

- **Gathering sustainable data:** Building passports and EPC data requirements in digital format would boost the Taxonomy compliance of the mortgage portfolios and optimise banks' data management processes
- **Accessing capital markets**: This data quality will increase the banks' capabilities to issue green and social bonds, generate a European critical mass, and open up a new sustainable investor base for covered bonds, securitisation, and senior unsecured bonds.
- **Serving fragile borrowers & ensuring social inclusion**: The calibration of the guarantee in a range of 30% for LTV < 80% and 50% > 80% would prevent any form of moral hazard, reinforce financial stability, global competitiveness and level playing field for European lenders keeping mortgages on balance sheet and at the same for increasing volumes to fragile borrowers and limiting the downpayment for young and fragile borrowers who can benefit from extra resource for the part about 80% LTV with a 50% guarantee.
- **Securing competitiveness and a global playing field**: In the context of Basel III, the 0% RWA would reinforce the competitiveness of European banks where mortgage portfolios represent 1/3 of their balance sheet for a total of 9 trillion euros outstanding and stimulate the supply of green and social product in the entire value chain with a spillover effect from the mortgage sector to consumers credit loans and SME loans.

3) Housing Ecosystem, Public Sector, infrastructural investments, and SME:

3.1 The potential of freeing capital markets resources for energy and infrastructural investment with Public Covered Bonds

The real power and competencies of housing policies are generally at a local level (cities, local authorities). Local authorities designate building land, provide building permits, and transpose their local housing policy.

Regarding the use of public funds or subsidies, there might be a target ranking: A main target could be to provide housing to citizens, i.e., subsidising rents and supporting the construction of rental housing for low-income citizens. Another target could be supporting access of citizens to ownership. A further target could be climate aspects and sustainable housing (not only newly built but primarily the existing housing stock). All this must be structured, and different tools apply.

Public funds are at the forefront for the achievement of these targets. The challenge is how to integrate private capital into these policies.

Additional capital markets financing tools, already available and fully enshrined in the Banking Union framework, could be used to reinforce the Housing Ecosystem and support member states and local authorities in planning and making long-term investments in Energy and infrastructure.

Public sector covered bonds are, Capital Requirements Regulation (CRR)- and Covered Bond Directive compliant, pillars of the financial tradition in countries like Austria, Germany, France, Italy, and Luxembourg. Public covered bonds are a type of secured debt instrument issued by banks or financial institutions, backed by a cover pool of high-quality assets, such as mortgages or public-sector loans. What sets public covered bonds apart is that the underlying collateral specifically consists of public sector assets, such as loans to sovereigns, local authorities, or government-related entities and debt securities issued or guaranteed by public bodies.

Historically, the public covered bonds sector massively contributed to the reunification of Germany, but more generally, to supporting infrastructure investments for public authorities across Europe, and, last but not least, during the COVID crisis to restructure health facilities. The use of public covered bonds could be extremely relevant at this critical moment when public authorities are required to rapidly and significantly increase the availability of affordable housing and implement the EPBD, for example. Essentially, a European asset class could be used to finance local needs, relying on capital markets and creating a level playing field. A bank from country XY might issue a covered bond backed by loans to European municipalities in a different country. If the bank fails, investors are still protected by the pool of municipal loans. This asset class is attractive to institutional investors needing safe, long-term assets and is eligible for preferential regulatory treatment (e.g., lower capital charges for banks) with the following key macroprudential features:

- Dual Recourse: Investors have a double claim—on the issuer and on the cover pool if the issuer defaults.

- High Credit Quality: Due to the backing of public sector loans, these bonds tend to carry high credit ratings.
- Regulated Instruments: In the EU and many jurisdictions, covered bonds are governed by strict legal frameworks.
- Low Risk: They're considered low-risk investments because of overcollateralization and public-sector exposure.

3.2 The potential of using public undertakings in the context of the EU Covered Bond Directive (Directive (EU) 2019/2162)

Covered bonds are a fundamental long-term funding tool for mortgages and the public sector, as mentioned above, but we see potential to develop a broader Ecosystem to provide financing for investments, not limited to that kind of collateral. Under Article 6 and related provisions of the Covered Bond Directive, public undertakings are eligible debtors in the cover pool when they meet certain criteria, but they are not compliant with CRR Art 129.

The directive refers to public undertakings as defined in Directive 2006/111/EC, which means:
"Any undertaking over which public authorities may exercise directly or indirectly a dominant influence by virtue of their ownership, financial participation, or rules." This includes:

- State-owned enterprises
- Municipal companies
- Public utilities (energy, transport, etc.)

To be eligible for inclusion in the cover pool, exposures to public undertakings must:

1. Be low risk (as judged by the competent authority or ratings)
2. Be sufficiently transparent and stable
3. Be fully secured or guaranteed by public bodies or satisfy credit quality standards

This could open the door to long-term finance energy or another kind of investment, such as loans to municipal companies fully owned by the city and debt from a state-owned operator.

3.3 SME financing and "European Secured Notes" (ESN) linking capital markets to the real economy

The financing of Small and Medium Enterprises (SME) is critical for the entire competitiveness of the Single Market, and the adequate financing of this sector in the capital markets is a strategic opportunity for Europe. The banking sector can play a crucial role by providing anticyclical long-term access to finance, boosting taxonomy compliance. To support the transition economy, it is not only necessary to provide financing to consumers and households, but it is of paramount importance to develop and support strategic investments for SMEs working in the renovation and ancillary sectors.

European Secured Notes (ESNs) are designed as dual-recourse funding tools aimed at supporting SME financing in a stable and targeted way, distinct yet compatible with other instruments like securitisations. Following early attempts more than a decade ago, the renewed focus on SMEs—key to employment and sustainability—makes ESNs increasingly relevant to Europe's recovery plans.

SMEs employ nearly 85 million people and generate over half of the EU's economic output, yet face growing difficulties accessing finance due to rising rates and stricter lending conditions. ESNs could efficiently complement bank funding, offering a middle ground between covered bonds and securitisations. They promise investor appeal through a robust structure, higher yields, and potential regulatory advantages, especially if structured with ESG objectives in mind. A critical mass of eligible SME loans, including guaranteed ones, would support granularity and diversification. ESNs could gain traction if backed by a clear EU-wide legal framework.

Beyond funding, ESNs can be a catalyst for ESG transparency among SMEs. Ultimately, ESNs may serve as a long-term, market-based solution for financing Europe's sustainable recovery, particularly as public support programmes phase out.

Currently, the European Banking Authority, in response to a call for advice of the European Commission, is assessing the added value of creating an ad hoc legislative framework for European Secured Notes, mirroring the success of the Covered Bond Directive, which has provided a strong legal framework for all stakeholders of the "Old Continent".

Conclusion

The intellectual leadership and market governance guaranteed by the EMF-ECBC, through its analytic and technical work and proactive coordination of market dynamics, amalgamate different cultures and market perspectives in a common way forward, and, more importantly, legal and financial features into a common qualitative and quantitative perimeter. Over the years, this approach has become the true *fil rouge* of our industry's *modus operandi*, and we are always ready to adapt to challenges whilst preserving asset quality and ensuring consumer and investor protection.

In this way, our community has fostered a housing philosophy that responds with international solutions to local needs, fostering clear macroprudential characteristics and ensuring capital market accessibility and financial stability for mortgage and housing markets.

Our Label initiatives reinforce the role of the European mortgage market as a driver for growth and risk reduction. These initiatives lead stakeholders towards a cathartic renovation of market best practices across the Single Market, reducing market fragmentation, which constitutes a major source of risk for the real estate market in Europe, as identified in the Report "Assessing real estate risks and vulnerabilities. Hidden cracks in the financial system?" prepared by the Economic Governance and EMU Scrutiny Unit (EGOV) of the European Parliament at the request of the European Parliament's Economic and Monetary Affairs Committee (ECON).

This Report concludes that too many national segmentations remain across Member States, and there is ample room for bringing national markets closer to the best practice, and that asymmetries should be investigated, aiming to promote a faster alignment to best practices.

The EMF-ECBC remains at the disposal of the European authorities to play a market catalyst role and share its expertise on housing policies, covered bonds, securitisation, and mortgage credit sectors to ensure a strong, stable, and sustainable future for all.

Notes:

1. Established in 1967, the **European Mortgage Federation** (EMF) is the voice of the European mortgage industry, representing the interests of mortgage lenders and covered bond issuers at the European level. The EMF provides data and information on European mortgage markets worth over EUR 9 trillion at the end of 2023 (EU27 + UK, Norway and Iceland). As of April 2025, the EMF has 13 Full Members across 11 EU Member States and several Observer Members.

2. In 2004, the EMF founded the **European Covered Bond Council** (ECBC), a platform bringing together covered bond issuers, analysts, investment bankers, rating agencies and a wide range of interested stakeholders. As of April 2025, the ECBC has over 120 members from across the more than 30 active covered bond jurisdictions and many different market segments. ECBC members represent over 95% of covered bonds outstanding, which were worth over EUR 3.3 trillion at the end of 2023.

3. Established by the World Bank in 2018 and administered by the EMF-ECBC since 2022, the **International Secondary Mortgage Market Association (ISMMA)** is the first global association to bring together secondary mortgage market institutions to focus on advocacy on regulatory issues, share information and provide support to newly-established institutions in this space. The association provides a platform for member countries to exchange ideas on how to improve access to housing finance for their citizens and ultimately reach the goal of adequate, safe and affordable housing for all. As of April 2025, the ISMMA has 18 members from around the world.
