An empirical case for reconsidering the macroprudential lending rules.

We should state from the outset, that this firm has been publicly critical of the rules that there is much we agree on with the Central Bank. We don't want to see asset bubbles, unaffordable houses or to see rapid and damaging credit expansion.

We also agree on the rules almost entirely when it comes to investment property loans, but a little less on those who aren't first time buyers.

Where we are diametrically opposed to the rules is when it comes to first time buyers, the reasons for this will be set out below.

This is mainly due to the effect on personal wealth and the housing market generally. The Housing Minister, Simon Coveney, has himself admitted that mortgage rules set by the independent Central Bank mean some 40pc of the population are "locked out" of the mortgage market.[1]

The Central Bank has called for submissions with empirical evidence, we are partly of the belief that this requirement is only partially sincere given that most of the first round of submissions contained empirical evidence that was subsequently ignored.

Macro-prudential rules should be questioned and tested the same as any other rule, to date we still have not seen a cost benefit analysis by the Central Bank on the mortgage rules, nor to date have we seen a suggestion of one. This is an important consideration as the 'costs' can be widespread and affect people who are not party to the mortgage[2].

Do macro prudential measures even work?

In our last submission we looked at their effect in Hong Kong. This is worth revisiting (see Graph 1 below), it is clear that even when LTV policies were adopted that it didn't prevent price increases and perhaps at best only delayed the inevitable prices rises that came about anyway.

Another large piece of work was carried out in 2015 by the IMF[3] their research was about how LTV and LTI limits worked in practice post introduction. The countries in question were Brazil, Hong Kong, Korea, Malaysia, Poland and Romania. Their conclusion was that it makes debt more sustainable (which is mechanically expected due to lower LTV's) but it doesn't curb house price growth.

We would encourage restraint before any claim that the rules have restrained house price growth, we are simply in the middle of a cycle as we saw from the graph in Hong Kong. The 20% price growth wasn't tamed by these rules, rather the trajectory had started to change already in the summer of 2014. That some have said the subsequent announcement made this happen belies the situation that was seen in the market long before subsequent data was available.

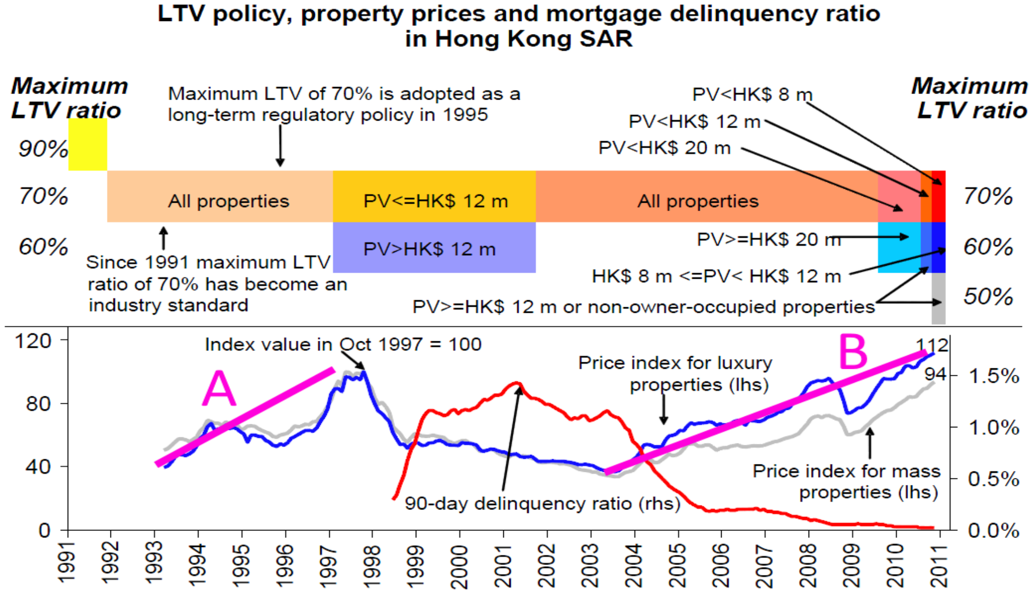
[1] http://www.independent.ie/opinion/columnists/john-downing/we-badly-need-builders-to-start-building-again-it-doesnt-have-to-be-that-difficult-34894828.html

[2] For instance, we saw delays in Q4 with loan drawdowns due to this and it affected vendors and others who were third parties to the transaction.

[3] IMF working paper wp/15/154 'LTV and DTI limits – going granular', Jacome & Mitra.

It also means that calling the rules a victory is a 'cart before the horse' analogy, they can't work prior to existing.

Graph 1

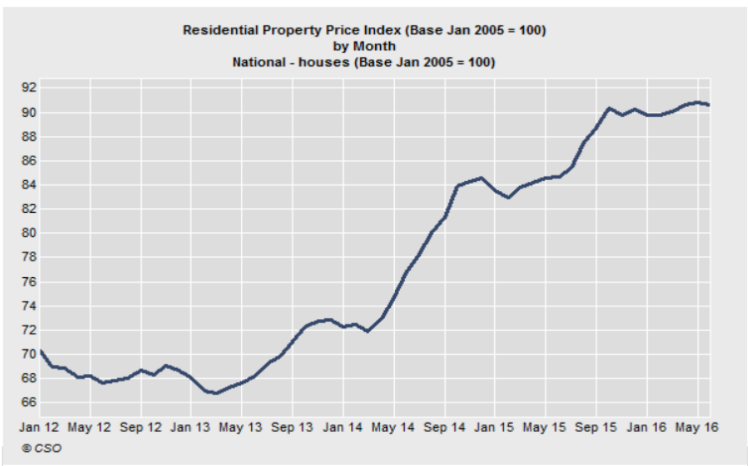


PV = property value

Source: HKMA.

This is best demonstrated via the CSO data on house prices during that time. It is important to remember that the review for the announcement couldn't have made prices drop, in particular given the rising level of mortgage applications and drawdowns in Q4 2014.

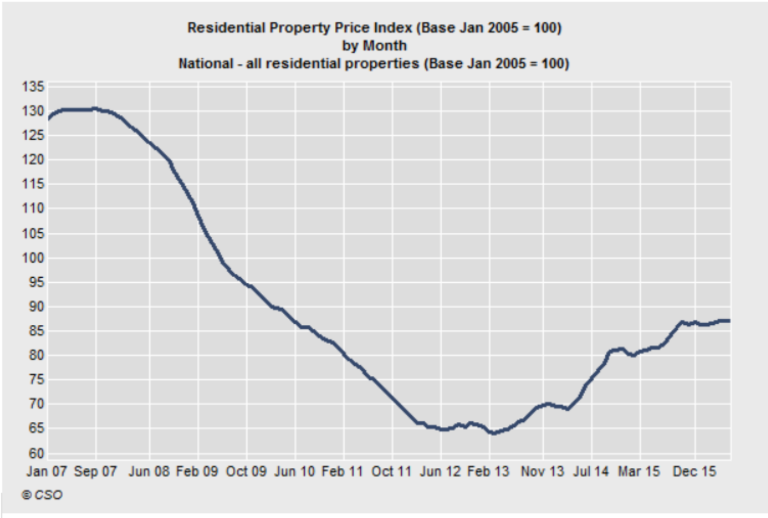
Another point to hold firmly while looking at this chart is that it is a record of delayed transactions which are based on mortgages. We know that from the time you go sale agreed to the time you draw down a loan that it takes about three months, the sums are then recorded in the following month. For there to be any slowdown in prices in October/November 2014 it must have been based on transactions from the summer before that.



The IMF paper was not overwhelmingly in support of the effectiveness of these measures (albeit not based on an Irish context). Some studies like that of Vandenbussche (2015) find no empirical support for these measures.

Perhaps most importantly, the timing of the measures is a vital component in many of the studies that support such measures.

Ireland was and is still far below peak prices (see next chart) during this period. Instead the result has been to reduce investment and this in turn has caused peak rental costs. The idea that a rising price is of itself a problem has to be viewed in relative rather than just absolute terms, this has been overlooked and the danger perhaps overhyped.



Peak rental costs cannot be overlooked[4], because we are concerned from a family balance sheet perspective, it is obvious that high rental costs act like a further tax on a household. One that occurs not because of any negative aspect of their activity, but rather due to their form of tenure.

That they are rising in the face of these rules merely shows what happens when further uncertainty delays decisions, equally, it makes savings harder and this compounds the issue a prospective homeowner faces. The second round effect will be that these new higher yields[5] will in time play into capital values.

We cited this being part of the outcome in our submission in 2014 (emphasis in bold): "*The difference between the last two censuses' indicate that* ***people renting increased 47%[6]. This is heavily represented by Dublin where current supply shortage and the impact of the macro-prudential proposal will hurt people the most.*** *The number of tenancies registered with the PRTB as at the end of Q2 2014 is 300,425. PRTB data show that Dublin accounted for 39 per cent of the rental market in quarter 2, 2014.*

This same cohort represents the people who didn't buy as the market fell, this can be discerned by considering household formation, the low transaction levels in purchases[7], and low credit drawdowns.

Now that the market is no longer in free-fall the same group is looking at purchasing and this is resulting in higher prices and stock shortages, that aside, the issue remains one of stock and this proposal does nothing to alleviate that.

The market is segmented broadly into the people in negative equity or who have trackers and are unlikely to move, those in arrears for whom this policy has no impact, cash buyers who are not impacted and new entrants who are over-represented for structural reasons, whom we expect to remain over represented for some time due to supply constraints meeting demand.

Using a macro-prudential tool to resolve a supply shortage is akin to giving a person with cancer a plaster cast. Like medicine, macro-prudential policy making has particular appropriate applications, this is not one of them".

Upon introduction, the uncertainty resulted in a delay of investment, this has meant that the subsequent shortages experienced now are worse than they may have been were this investment to have arisen at the time it was scheduled to be done in.

The money will flow into property irrespective of what the Central Bank do because higher yields are a core objective of much of the investment community which is a globalized operation trying to find and create value in a world where yield curves are flat or negative.

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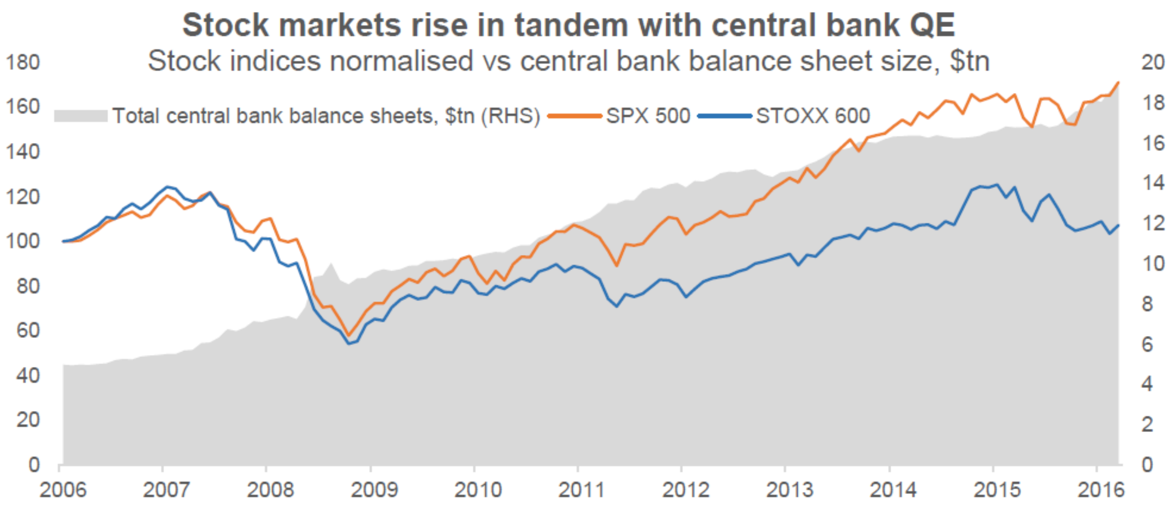
[4] http://www.rte.ie/news/2016/0823/811220-daft-rent-report/
[5] Dublin up 11.1%, Cork city 18%, Galway 13.9%, Limerick 15.5%
[6] Census 2011 - 475,000 households were renting their accommodation
[7] Available from the property price register, and implied by mortgage draw-downs as well as from high levels of listings during that time.

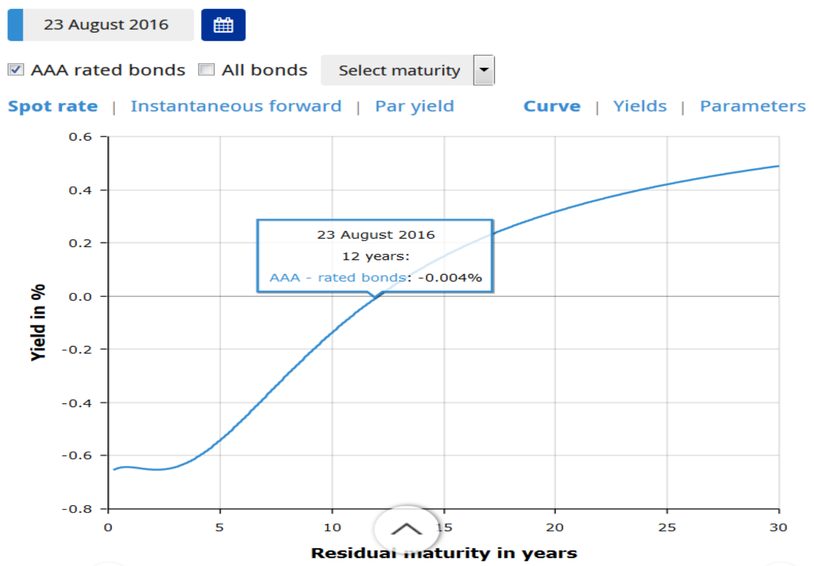
We cannot pretend that Ireland is an island (in the financial sense), the rising values here and attractive yields are part of what have brought so many buyers into this market in the first place many who don't' need a mortgage to complete the transaction[8].

This problem is set to continue and will have an upward force on asset prices, if the Central Bank are truly concerned about asset prices perhaps we shouldn't have a zero interest rate policy? See the graph below, the correlation is relatively clear[9].



Source: Algebris Investments (UK) LLP, Central bank websites, Bloomberg. *Central banks included are the Fed, ECB, BoE, BoJ, PBoC and SNB. Stock indices normalised: May 2006 = 100. RHS = right-hand-scale.

Added to this is the fact that the current Euro yield curve is negative a full 12 years into the future (see below), this is hardly a portent of rising interest rates, this is feeding into the search for yield worldwide, of equal or greater concern is that we are far from alone in Europe when it comes to record low rates.



The next chart shows the countries that are on the same boat as the EU, Central Bank Interest rates are the problem. Just to make sure the point is repeated in case there be any doubt, if the Central Bank are truly concerned with asset bubbles then they might do well to consider their main policy area which is at the heart of the issue, that of interest rates.

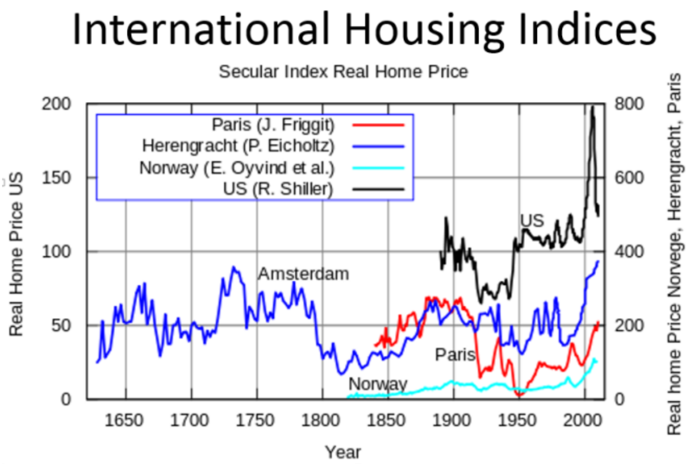
[8] REITs, QIAIF's, international funds, pension funds etc.
[9] Source: Algebris Investments UK

Annual Average Policy Rate, %

	90	91	92	93	94	95	96	97	98	99	00	01	02	03	04	05	06	07	08	09	10	11	12	13	14	15	Now
Australia	13.2	10.3	6.5	5.1	5.4	7.5	7.1	5.4	5.0	4.8	6.0	4.9	4.6	4.8	5.3	5.5	5.8	6.4	6.6	3.2	4.4	4.7	3.6	2.7	2.5	2.1	1.5
Canada		9.0	6.7	5.1	5.8	7.3	4.5	3.5	5.2	4.9	5.8	4.3	2.7	3.2	2.5	2.9	4.3	4.6	3.2	0.6	0.9	1.3	1.3	1.3	1.3	0.9	0.75
Denmark	8.0	9.3	9.5	8.7	5.2	5.4	3.5	3.3	3.8	2.9	4.0	4.3	3.2	2.3	2.0	2.0	2.8	3.8	4.1	1.6	0.8	1.0	0.3	0.0	0.0	0.0	0.0
Eurozone	6.0	8.0	8.3	5.8	4.5	3.0	2.5	2.5	3.0	2.7	4.0	4.3	3.2	2.3	2.0	2.0	2.8	3.8	3.9	1.3	1.0	1.3	0.9	0.5	0.2	0.1	0.0
New Zealand										4.6	6.2	5.7	5.4	5.3	5.9	6.8	7.3	7.9	7.4	2.7	2.8	2.6	2.5	2.5	3.2	3.1	2.0
Japan	6.0	4.5	4.0	3.1	2.2	1.2	0.5	0.5	0.4	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.1	0.5	0.5	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.0
Sweden	11.5	8.0	10.0	9.0	7.2	8.5	6.3	4.1	4.1	3.0	3.7	4.0	4.1	3.1	2.1	1.7	2.2	3.5	4.1	0.6	0.3	1.8	1.3	1.0	0.3	-0.3	-0.5
Switzerland	6.0	7.0	6.0	4.0	3.5	1.5	1.0	1.0	1.0	0.5	3.1	2.9	1.2	0.3	0.5	0.8	1.5	2.4	2.4	0.3	0.3	0.1	0.0	0.0	0.0	-0.8	-0.8
UK	14.8	11.7	9.5	6.0	5.5	6.7	6.0	6.6	7.2	5.3	6.0	5.1	4.0	3.7	4.4	4.6	4.6	5.5	4.7	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.25

Source: Algebris Investments (UK) LLP, S. Krogstrup (2016), Central bank websites, Bloomberg. *Annual average policy rate, yellow = below or equal to 2%, pink = below or equal to 1%, red = below or equal to 0%

The international experience of prices is in the next graph and demonstrates that in every developed country with records being kept that property prices do not remain static and have cycles.



It is also worth noting that the HM Treasury report[10] they noted that LTV/LTI limits were rarely implemented without mortgage insurance schemes, and that they could create household liquidity traps. In the consultation paper this seems to have been overlooked and is only being mentioned ex post which is worrisome in terms of the foresight industry expects from their regulators.

That current experience is showing this to be an issue is not an unexpected outcome, but a fully expected one and the value of these measures to broader society versus the cost and imposition of the same measures to society are unclear in terms of the value of the benefit. If we take the cost benefit view of financial regulation the effectiveness of the policy is not clear cut.

On page 7 of our last submission we spoke about 'classist delineation' being a concern, this has also shown to be an issue in the wake of the rules. Our own internal research shows that the increase in parental support is pervasive with c. 25% not receiving assistance of some sort while the other 75% do need it, this being up from the c. 40-50% amount prior to the introduction of the rules.

This in turn means that people with parents who hold assets/wealth are in a far better position, not because of their own life or decisions, but because of those of their relatives or loved ones and that is the type of classist delineation we feared.

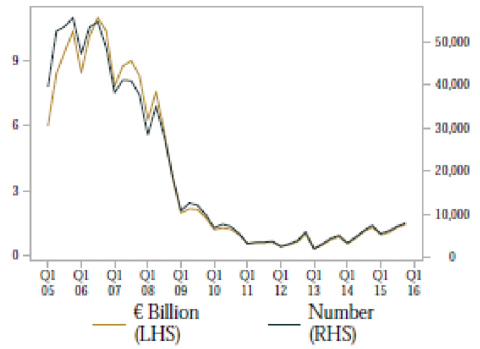
[10] HM Treasury, financial services bill report Cm8434 Sept 2012 page 34

Added to this is the potential for unforeseen consequences, if parents give away nest eggs to help children then what effect may that have? These are all societal prices being weighed against a fallacy that our banking system is any safer. The recent stress tests show we are not out of danger.

Furthermore, lending is one area banks can recoup income and yet their growth is slow, Bank of Ireland is lending twice in the UK what it can lend here, we don't have evidence of the general public mood, but BOI was in receipt of state support in the past and to see their credit flows going abroad at a rate of 2:1 is perhaps not the best outcome, in particular as private household aggregate credit has been on a downward trajectory for almost a decade, new lending has also been subdued (see below).

Figure 11 presents data on new lending from the Banking and Payments Federation Ireland. There has been an increase in the value of new lending between Q4 2014 and Q4 2015 from €1.34bn to €1.45bn. The number of new loans has increased from 7,583 in Q4 2014 to 8,103 in Q4 2015. Lending volumes remain below levels seen in the 2005-2007 period.

Figure 11. New Mortgage Lending by Loan Count and Balance, Q1 2005-Q4 2015



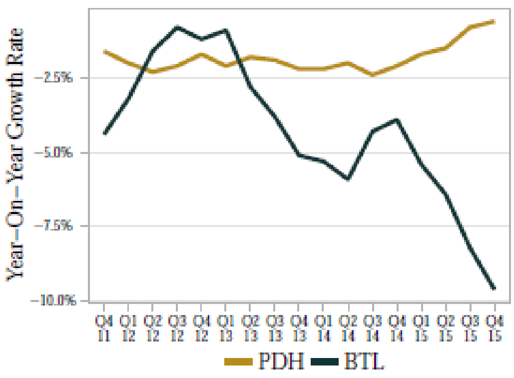
Source: Banking and Payments Federation Ireland.

There is a fundamental question that needs to be answered, do we need to fear lending to this degree when up to 60% of homes[11] are bought with cash?

IMF Research showed that a ten percentage point lower LTV limit has a small but significant effect in lowering the level of mortgage credit by 0.7 percent over time, and counterintuitive effects on real house prices. So what are we hoping to achieve?

This also comes at a time when aggregate credit has been shrinking[12] for a still impaired back book of loans while new credit has remained below expectations at the same time as some banks have excess liquidity.

Figure 6. Growth Rate in Outstanding Mortgage Stocks by Dwelling Type, Q2 2004- Q4 2015



[11] http://www.bloomberg.com/news/articles/2016-08-22/irish-banks-face-consumers-who-don-t-want-their-biggest-product
[12] Household credit market report H1 2016, Central Bank of Ireland, executive summary.

Putting these two concepts together, it seems we are trying to protect a future loan book from an existing back book while stifling some new lending (albeit the majority of purchases are still cash) which is going to be of a higher quality and in turn pushing lenders to park excess funds at the ECB while reducing their capacity to create the loans which would ensure their future health.

Preventing another bubble is an admiral objective, but while credit growth rates are negative (chart above) is that a cyclically correct decision? That cannot be known but is worth of consideration.

Consider again the IMF findings when looking at macro-prudential rules, house price growth taming only occurred in South Korea, and in doing so it also hampered GDP growth (having said that Ireland may need some help there given we have GDP growth of 26%)[13]

Table 5. Effectiveness of LTV-DTI Limits—Country Experiences

Objectives	Romania	Hong Kong SAR	Korea	Malaysia	Poland	Brazil
Curbing excessive credit growth, including speculative growth						
Consumer/auto loans	Green				Green	
Mortgage		Green	Green	Green	Green	
Curbing house price growth	Pink		Green			
Improving the resilience of the system to future adverse shocks						
Curbing household leverage		Green			Green	
Curbing banks' NPLs	Green	Green			Green	Green
Methodology	Dynamic Panel Data, Generalized Method of Moments (GMM)	Vector Auto-Regression (VAR); Demand-Supply econometric model for mortgage loans	Global Vector Auto-Regression (GVAR)	Event Study; Quadratic regression	Survey data analysis	Difference-in-Differences
Policy	LTV, DTI: together	LTV, DTI: together	LTV, DTI: separately	LTV	LTV,DTI: separately	
Other policy instruments		Stamp duties; loan tenor cap of 30 years				Capital risk weights based on LTV

[1]Stated objective, successful (Green), Stated objective, unsuccessful (Pink); Not a stated objective (Blank).

Sources: Neagu and others (2015), Kan (2015), Kim and others (2015), Abdul Rani and Lau (2015), Bierut and others (2015), Afanasieff and others (2015).

There is other research which we undertook with Behavior and Attitudes which have other facts and figures which will be included later in this report.

Do first time buyers default more?

There is an implied concern that we need to protect people from overextending themselves. This would seem an honourable approach to any paternally minded public servant, were it a case that the majority were better served it would be irrefutable, but that isn't the case.

While few would dispute that highly leveraged investors represent a higher credit risk, the issue for a first time buyer is one of options, to rent or not to rent and if the latter do they stay in another person's household (typically a parent or other relative) or purchase a home.

[13] http://www.bloomberg.com/news/articles/2016-07-12/ireland-s-economy-grows-26-as-u-s-companies-chase-lower-taxes

When it is cheaper to buy than to rent[14] even in the areas that face housing shortages the choice ought to be clear, but in some cases it is prevented by arbitrary rules by people who have to face a continuous overhead of housing.

Housing is not optional, while the expense can be variable, the existence of that expense is somewhat fixed unless a person is mortgage free[15]. When a person buys a home there is also a strong savings effect.

The Central Bank's own study about first time buyers[16] raises several important points on the risk they represent, several points are listed relating to this study.

1. Controlling for borrower and loan characteristics, first time buyers default less, in particular where both applicants are first time buyers. The difference is 30% less than non-first time buyers.
2. FTBs face the greatest difficulties accumulating savings to purchase a home, and therefore are disproportionately affected by macro-prudential regulation[17].
3. The differential between FTB/SSB is maximized for LTVs of 80-85%, where the FTB default rate is 45% lower[18]. This would imply that even at higher LTV the FTB is not the main problem.
4. Without a current property to build up equity, FTBs are marginal borrowers who are most sensitive to bank lending conditions and subject to financing constraints. This brings us back to the issue of social engineering. The wealth effect of housing is large and cannot be disregarded as it is so vital to the economy generally and households in particular.
5. The Central Banks own research shows that saving for a down payment is a major goal of most young renter households, and the largest barrier to home ownership. FTBs are also different from non-first time buyers because of lack of credit history
6. FTBs are typically younger, and their future income growth prospects are usually higher; if a mortgage is serviceable early in the income lifecycle, future income growth should give additional ability to meet obligations over time.

That first time buyers normally face improved affordability over time, build up equity, potentially avoid rising rents or the non-savings effect of long term renting are all things that render positive results for homeowners. Even in light of the crash, first time buyers were not only a more minor issue than heavily indebted multiple home owners, but they have also faced a low repossession rate environment so negative outcomes outside of ruined credit histories and some of the issues that go with that are not as widespread here as in other jurisdictions.

Boom rents bust wallets.

Rising rents act like a 'tax' on those who don't own homes (an important consideration is those that would rather own a home but who cannot obtain one due to the CBI rules but who would otherwise show affordability to make the full payments). As more people are left with no choice but to rent it means they have fewer years to make amortizing payments and create wealth.

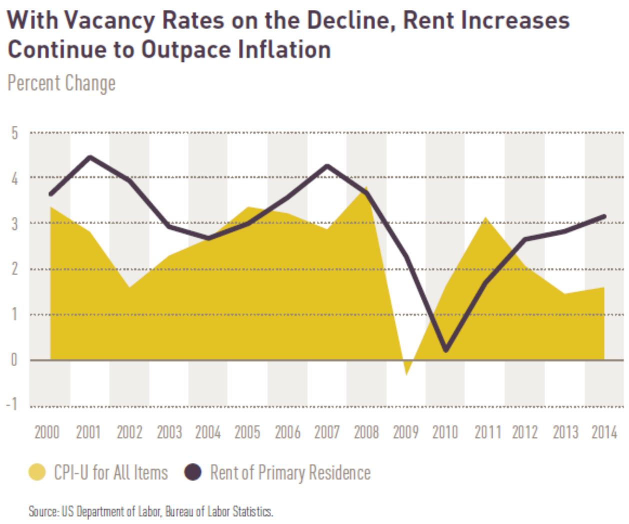
This in turn leaves less time to save for a pension, the high rate of DIRT on savings and low rate environment (courtesy of Central Banks everywhere) compound the savings issue, add this to more anaemic market

[14] http://www.independent.ie/irish-news/home-truths/its-cheaper-to-buy-than-rent-in-80pc-of-the-country-31544029.html
[15] Excluding things like house insurance, property tax and upkeep costs.
[16] Designing macro-prudential policy in mortgage lending: do first time buyers default less? Kelly, O'Malley, O'Toole.
[17] *Ibid,* Non-technical summary paragraph 2 & 3.
[18] *ibid*

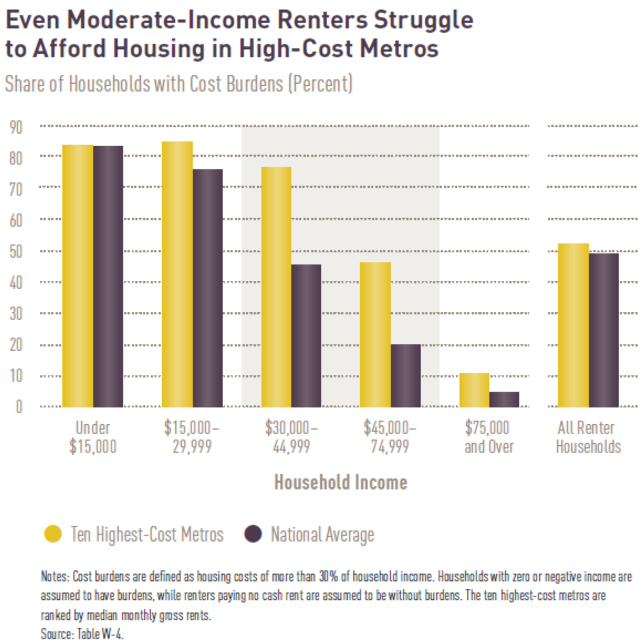
returns and it shows that we'll somehow, against the odds, find a way to turn a housing crisis into a pension crisis.

Irish state pensions weren't designed with renting in mind, when your former deputy proudly declared at the NESC convention in Croke Park that lots of people renting is desirable, it would be great to see that followed by offering to be a renter in receipt of Irish state pension when he retires.

This again is a trend not confined to Ireland, it's happening in many jurisdictions even in nations who's economies dwarf ours completely, which in short should make it clear that priced out buyers, wary buyers and rising rents all make for a damaging dish wherever they are served (see next chart for the USA example[19])



Renters find it hard to afford housing as a result of a low savings rate, a high tax on savings (DIRT) and low returns (Central Bank's feeding through to deposit rates). Again, not confined to Ireland, it would appear that bad outcomes are not always exclusively our own.



[19] Joint Centre for Housing Studies, Harvard, State of the Nation's Housing 2015.

Personally I have a suspicion nobody actually reads these submissions in their entirety, but if you happen to be one of the few that do, please read the JCHS paper on housing wealth[20].

This study showed that the housing crisis and ensuing Great Recession of the late 2000s resulted in millions of homeowners losing their homes to foreclosure and millions more losing substantial amounts of housing wealth as home prices plummeted.

These substantial financial losses have raised important questions about the appropriateness of policies to encourage homeownership as a wealth building strategy for low-income and minority households. In 2013 the Joint Center for Housing Studies published a paper entitled "Is Homeownership Still an Effective Means of Building Wealth for Low-income and Minority Households? (Was it Ever?)".

That study found that despite the severity of the housing crash, the median household who bought a home after 1999 still managed to accrue significant amounts of wealth through 2009, the latest year for which data was available at the time. While about a quarter of new homeowners over this period were no longer owners as of 2009, among those who had exited homeownership, the typical household ended the period with wealth that was little changed from before they bought their homes.

Translation: the change in wealth when losing a home puts them back to where they would have been had they not owned and usually the wealth lost was the wealth accrued due to the effects of homeownership. This is further backed up in the paper findings.

As housing prices continuing to fall in most markets until 2012, there was an open question of whether the study's results were skewed by not capturing the full extent of the housing downturn. The study[21] updates the analysis of the earlier study to include outcomes for these same households through 2013 when the worst of the crash was over.

The updated analysis presented in this paper upholds the bottom-line result from the earlier paper: for most households, homeownership was associated with significant gains in household wealth, even when viewed across the tumultuous housing crisis period of 1999-2013. However, including the additional period from 2009-2013 did reduce the magnitude of the annual gains in wealth associated with owning, and also found a higher share of Hispanic and low-income households that failed to sustain homeownership.

Again, we see very positive outcomes despite the more widely publicised negative outcomes, and while in Ireland we are not at a point where we racially profile results, it is clear to see that where homeownership does accrue wealth that the effect on lower earners is higher than the wealth effect on those who are already asset rich by other means.

Overall, the study's findings indicate that while homeownership continues to offer a majority of households the opportunity to build up wealth, owning is not without significant risks, especially for minorities and lower-income households.

Some of the most important findings were in wealth trajectories throughout the study, as a firm of financial advisors this is near and dear to our core belief that by helping people to make better financial decisions that create wealth for them that we are contributing to both households, families, the market and the economy at large.

What they saw was that the wealth creating power of homeownership was strong across all periods and all types of owners who remained owners, so anything that prevents a reasoned and well underwritten buyer

[20] JCHS, Update on homeownership wealth trajectories through the housing boom and bust.
[21] *ibid*

from being able to own a home (such as arbitrary rules which are not underwriting oriented) effectively strips a person of the ability to formulate more future wealth, we see that as a bad thing.

Controlling for multiple home indebtedness is sensible, but for first time buyers the same argument just doesn't hold as strong. The changes in net wealth are below, of great interest is the fact that another study found that African American's are highly affected in terms of net wealth by years of homeownership.

Table 2a: PSID Sample Net Wealth by Demographic Characteristics, 1999-2009 Sample

2013 Dollars

	Median Net Wealth			Mean Net Wealth		
	1999	2009	Median Change	1999	2009	Mean Change
Race/Ethnicity						
White	68,500	149,600	51,900	254,600	591,700	337,100
African-American	7,000	18,000	2,800	49,600	135,600	86,000
Hispanic	15,400	32,000	5,600	67,200	144,800	77,600
Age in 1999						
Under 25	3,900	24,200	10,600	16,900	90,100	73,200
25-34	15,700	62,700	24,200	74,100	311,200	237,000
35-44	56,600	107,500	25,900	214,400	393,600	179,200
45-54	139,100	188,900	51,600	370,200	826,200	456,000
Average Income 1999-2009 (2013 Dollars)						
Less than $40,000	2,900	3,300	300	26,700	54,800	28,200
$40,000-69,999	18,700	39,600	11,300	64,500	448,900	384,400
$70,000-109,999	54,100	128,100	52,500	173,400	285,200	111,900
$110,000 and Up	196,600	422,400	172,100	478,500	967,300	488,700
Total	***44,700***	***105,300***	***29,700***	***208,700***	***482,700***	***273,900***

The Institute on Assets and Social Policy showed that[22] amongst the biggest drivers of wealth inequality are years of homeownership, to the tune of 27% of the difference, a bigger contributing factor than both household income or college education (5%). It might be counterintuitive to advise buying a home over going to college, but in at least some respects it might be the wiser choice. The chart above puts numbers on it.

In Ireland we do have a broadly classist society with the 'haves' and 'have not's', but our view is that the best way to level the field isn't to try to bring down those who have, but rather to raise up those who have not, in that respect homeownership is a good vehicle for doing so and has proven the test of time over many decades in Ireland with some notable exceptions.

Even for those who bought in the boom and who have negative equity, often their cash flow position is advantageous (as many have trackers) versus other mortgagors in similar properties and those who rent similar properties. The cash flow element cannot be overlooked, in particular as we already have mentioned that in many areas it is cheaper to be a buyer than a renter.

[22] Roots of the widening racial wealth gap: explaining the black-white economic divide 2013

The former Governor was hinting at some of these points in his own words "*The empirical evidence is, however, suggestive of the positive role played by financial development in reducing poverty and easing inequality*[23]".

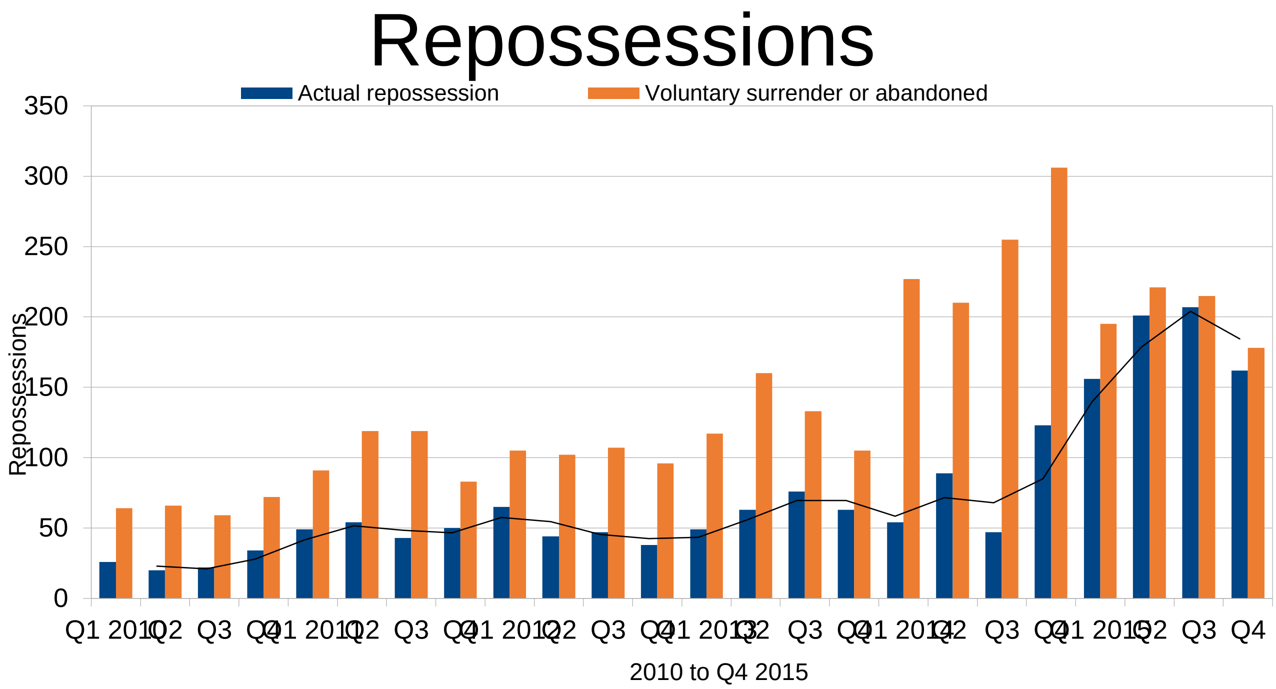
Should we protect first time buyers from their own bad choices?

Unemployment alone cannot explain our arrears and the Central Bank's own economists have shown this despite the conventional wisdom that job loss is the sole driver[24], 80% of households in arrears have no unemployed adult member in the home. When it comes to heads of households in arrears.

As per the Harvard JCHS study, it showed (as we will see in time in Ireland too) that even through a crash that those who are able to hold out experience positive wealth effects. It may be premature to push that point too much in this jurisdictions example, but it will in time prove true.

Should we go too far to protect people from themselves we risk locking out those who don't want the protection on offer, there ought to be some acknowledgement of the right to make a questionable decision. Good regulation doesn't mean fools and their money are never parted, merely that they are not easily parted or parted in a manner which rewards those who encourage bad decisions.

Taking into account the default rates we haven't seen repossessions, it is also worth noting that many are handed back voluntarily or abandoned (see below)



The Arrears and Repossession Study Group[25] observed over 4,000 court appearances in 2015[26] some of the key findings are below[27].

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[23] IIS 399: Honohan & King 2012.

[24] Yvonne McCarthy Barrington lecture – 'Disentangling the mortgage arrears crisis'.

[25] Brendan Burgess, AskAboutMoney, Seamus Coffey, UCC, and Karl Deeter, Irish Mortgage Brokers.

[26] Some of this data was also presented at the Dublin Economics Workshop in 2015

[27] This information was already shared in part with Central Bank economists and the Department of Finance.

We witnessed 151 orders for possession of family homes being granted:

Borrower did not attend court and was not paying anything	85	56%
Vacant property and was not paying anything	At least 29	At least 19%
Consented to order	15	10%
Attended court but was not paying anything	10	7%
Rented out	2	1%
Paying something but did not attend court	2	1%
Paying something and attended court	2	1%
Total	151	100%

The Bigger Picture

Homes actually repossessed on foot of a court order during 2015	687
Orders for possession granted to lenders during 2015	918
Legal proceedings issued during 2015	4,088
Mortgages restructured by the lenders during 2015	48,000

Key findings

- In up to 98% of the cases where we witnessed an order being granted, the borrower was not paying anything.
- In at least 19% of the cases, the house was vacant
- The borrower was present in court on only 10% of occasions where an order was granted against them.
- Although, there are around 30,000 borrowers in arrears over two years, there are only 11,000 cases before the courts.
- Borrowers who pay something and show up in court almost always get an adjournment, no matter how deep their arrears are.
- In 2014, lenders launched 8,293 new court cases for possession. This fell to 4,088 in 2015.

Contrary to the widespread belief, there is no tsunami of repossessions. There is not even a tsunami of court cases. That being the case, the choice is clear that first time buyers don’t need to be saved from their own decisions. The most negative possibility would be if there were high rate loans greater than 100% and nobody is advocating for that.

What we are clearly advocating for is that 90% loans should be, in the main, allowed for people who can afford them if they are a first time buyer.

Here are some more of the details of that study

Data collection

Between March 2015 and February 2016, the authors attended 2629 repossession cases[28] in 5 separate Registrars’ Courts. (Dublin, Cork, Wicklow, Donegal and Meath)

As far as possible, we have included family homes only. Where we have known that the case refers to a buy to let or commercial property, it has been excluded. However, we have included houses which were originally family homes which are now abandoned or let out, as they are treated as family homes by the courts.

[28] The high number of appearances observed (>4,000) is due to cases appearing multiple times in the court list.

Table 1 Latest outcome of cases attended

	Total
Court appearances attended	4,000 +
Separate cases	**2629**
Adjourned as first time listed	525
Cases at second or subsequent hearing	**2104**
Orders granted	151 (7%)
Struck out	449
Generally adjourned	76
Transferred to Judge's List	58
Adjourned	1370
Borrowers in attendance	623 (24%)

This table includes only the latest appearance in the court. So if a case has been adjourned three times and then struck out, only the strike out is included in the table.

Table 2 Only 22% of Circuit Court cases we observed being concluded ended in an order for possession

Orders granted	151
Struck out or adjourned generally	525

Most cases are adjourned. Of the 2,629 cases we have observed, only 676 have been concluded. Only 22% of these ended in an order for possession. There are currently around 11,000 cases before the courts. If our figures are anything to go by, most of these will be struck out. Only 2,000 actual orders for possessions will be granted.

When a court case is struck out, we are not usually told why. It could be because the borrower has agreed a revised payment arrangement or it could be because the borrower has agreed a voluntary surrender.

Many orders do not result in loss of the family home

Even after an order is granted, if the borrower resumes mortgage payments, the lender will often not enforce the order. Unfortunately, we don't have statistics for the number of orders enforced.

Table 3 Profile of the 151 orders granted

Did not attend court and not paying anything	85	56%
Vacant property and not paying anything	At least 29	At least 19%
Consented to order	15	10%
Attended court but not paying anything	10	7%
Rented out	2	1%
Paying something but did not attend court	2	1%
Paying something and attended court	2	1%
Total	151	100%

In at least 19% of cases, it was confirmed that the house was vacant.

However, in most cases where orders are granted we get no information on whether the house is occupied or not. It is likely that in many of the cases where the borrower is paying nothing and does not attend court, the house is empty.

In many cases, the lenders have to get the court's permission to serve the civil bills by what is known as "substitute service" because An Post could not deliver the registered letter and because no one collected it from the Post Office after An Post left a notification of attempted delivery. Furthermore, the borrower could not be traced by the summons server. It is likely that many of these homes are empty. One would have thought that if the borrower had been living in the house, they would have collected their post.

We have seen many cases where properties were vacant and the lenders were unable to get an order for possession. This could be because of the Registrar's reluctance to grant any orders for possession, or because of some technical fault such as the inability to serve the papers on the borrowers.

Supply creation

The issue in the wider market is supply and while the Central Bank has correctly stated that this is outside of their remit, their decisions can have an impact on the capacity for the market to create supply.

One such example was cited in a recent meeting we attended where the developer said that they had gone sale agreed on several new properties in North county Dublin only to be told that many of the buyers couldn't get a mortgage due to the new rules. For this reason, they were not going to proceed with the second phase of the development as planned. It is in tangential ways such as this that financial regulation can materially impact supply creation even though the two are not categorically linked to one another.

This is verbatim from our 2014 submission and it remains the same, it could have been written yesterday and remain as relevant.

The most worrying aspect of this proposal is that it will neither fix supply (which is the core problem) nor address affordability, arguably it will make the cost of entry or opportunity cost higher to the detriment of the potential buyer.

It may even hamper supply because credit constraint in an already constrained market may mean that purchases which require a certain price in order to obtain higher than cost selling values will take longer to occur and prevent the next unit of supply. Virtually all housing supply at present in the capital is marginal supply.

Current underwriting and lending is being done in the most responsible manner we have seen since our firm's inception and beyond that for the duration of any of our staff's memories. Perhaps some method that enshrines current lending standards for the next five years would be a better tool than one which has obvious circumvention opportunities such as mortgage insurance.

If lending was kept the same there would be no opportunity for 'reckless lending' under current standards, it is the easing of underwriting standards more than anything which contributed to bad lending, the LTV was of secondary concern.

Further empirical evidence:

We were also part of a group that took part in the Behaviour and Attitudes survey[29] of those affected by the Macro-prudential rules. The findings in full are attached to the submission. A synopsis of some of the headline findings are below.

Of the people surveyed:

- 4 out of 5 were aware of the Central Bank's new rules in relation to deposits/income limits.
- 71% of both FTBs and movers are impacted by them, the vast majority negatively.
- Those yet-to-save envisage a six-year process; existing savers tend to have been two years saving already and imagine a further two years of saving still ahead of them.
- 54% are considering purchasing a home in the €300,000 plus bracket, with 23% between €300,000 and €400,000, 31% €400,000 plus.
- 35% spontaneously referenced deposit size as a negative influence (as many as mentioned "high prices").
- 44% of FTBs referenced deposit size negatively.
- 42% acknowledge that they will need to borrow from family … a quarter of intending buyers are already factoring this in.
- 52% have excluded the area where they actually want to live on the basis of unaffordability.
- Many are endeavouring to save while paying out high rents: 2 in 3 are thus impacted, and a knock-on effect on higher rents seems inevitable.
- The social cost is high, with many moving away from family networks and to areas of lower amenity or infrastructural inappropriateness (poorer transport, childcare facilities, schools, roads, and further from work.) 2 out of 3 are having to look more than 6kms from where they would like (and 3 in 10 more than 15kms).

Concluding remarks:

We didn't agree with the rules when they were introduced, we believe that it has made the situation facing a first time buyer generally worse and that the rules have not had the desired outcomes of tempering prices and have instead seen both prices rise and a second-round effect of rising prices outside of cities in regional towns and a destructive rise in rental costs.

The move to bring in the rules when they occurred were lauded by many of the general intelligentsia, but what it also did was confuse some of the regular people who build and develop homes and this delayed

[29] **Participants:** Irish Mortgage Brokers, Construction Industry Federation, Hooke and MacDonald, Douglas Newman Good, Lisney, IPAV, Property Industry Ireland, Irish Brokers Association, Association of Expert Mortgage Advisors, Banking and Payments Federation, Society of Chartered Surveyors. The research was conducted using an online survey methodology. As the agents hold a wealth of active leads, it was agreed that the survey be sent to these contacts for completion. In compliance with the requirements of Data Protection legislation, the agents received survey links from Behaviour & Attitudes and sent these on to members of their own databases. Behaviour & Attitudes hosted the survey platform, but at no point received personal details/contact information for respondents. It must be noted that respondents were contacts of three different agencies: Hooke & MacDonald, DNG and Irish Mortgage Brokers. No weighting was applied to the data resulting from the survey. The fieldwork was conducted between 22nd July and 4th August, 2016.

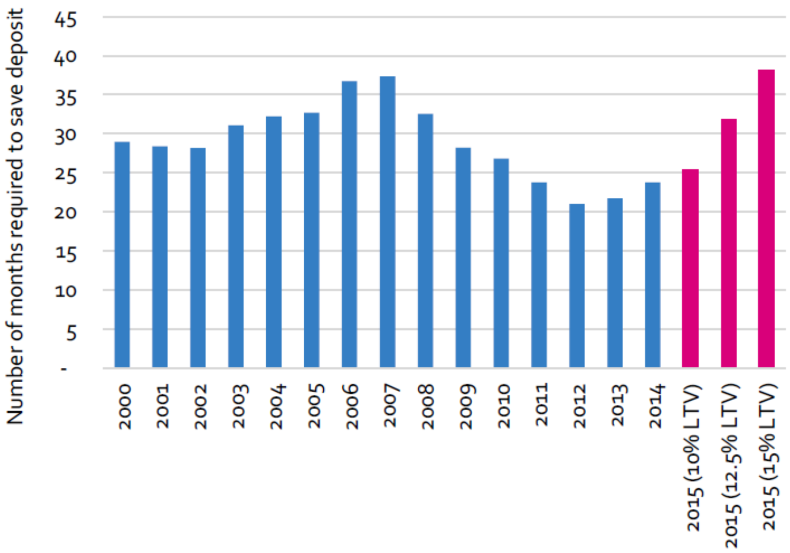
investment has fed into ongoing supply issues which will ensure the issues we face in the next leg of this market are perhaps worse.

In short, the Central Bank through low interest rates and ill timing, has made a situation less optimal than it needed to be albeit the intentions were good.

The current findings on the time taken to save a deposit are showing that in live cases observed that it is going to take people a long time to access housing, our findings are not the only ones supporting this, the Indecon study[30] on the affordability of housing estimated 38 months to save a 15% deposit but this was based on stylized assumptions whereas our findings are on actual people involved in house purchases.

As we have demonstrated, first time buyers were not the core problem of the past, nor will they be in the future – so preventing them from purchasing when they normally otherwise would reduces their life time savings, we don't believe the Central Bank should have a role in that process. It also keeps people in a static (supply) rented sector while reducing capacity to save due to rising rents that are set to rise further.

Figure 3.5: Number of Months Required to Save for a Deposit for a Notional Family



Source: Indecon analysis

We believe the rules are important, that the adherence to regulation is vital for the market in general and every firm in particular, but that the reporting structure was flawed and lead to some loans not drawing down on time in 2015, again a sub-optimal outcome.

For this reason, we are of the view that the 90% rule for first time buyers should be generally universal because they cannot represent a systemic risk, rather it is highly indebted multiple owners who have been the greater concern (all BTL loans and SSB loans combined vs FTBs). Equally, as people have to live somewhere there is always going to be a housing overhead cost.

[30] A study to examine the affordability of Irish housing, July 2016 pg 30-31.

The constraints will still exist in the loan to income (LTI) limits, while we believe 3.5 times is very conservative and that 3.75 times should be the base amount prior to any exceptions.

Our experience shows that deposit saving is a far bigger issue across the market generally (it has a larger impact on borrowers, vendors and developers).

We would temper most of this critique by also adding that perhaps doing nothing right now would be a good choice, these rules have only become properly embedded in recent times and the continuous changes and tinkering may give the market mixed signals, or may lead to a different set of issues that cannot be foreseen.

With that in mind, we leave it all up to the Central Bank, in the past our opinions were valueless, and we assume that they will be treated consistently in that respect.

Sincerely,

Irish Mortgage Brokers
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