FEDERATION HYPOTHECAIRE EUROPEENNE EUROPÄISCHER HYPOTHEKENVERBAND EUROPEAN MORTGAGE FEDERATION

Ms D. NOUY
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BY FAX AND LETTER

Brussels, 30 March 2001
00.105 – ref. 6200 - DM/ds

Re: Bank capital adequacy

Dear Ms Nouy,

The European Mortgage Federation welcomes the publication of the Basel Committee's second consultation document on capital adequacy and anticipates responding fully to the Committee within the deadline. The Federation would like to make a number of initial comments on the treatment of residential and commercial mortgage lending.

Residential mortgage lending

The Federation welcomes the continued recognition of residential mortgage lending in the revised standardised approach.

However, European mortgage lenders question the benefit versus the cost of switching their residential mortgage portfolios to the advanced internal rating based approach (IRBA) given the tentative calibration of risk weights and the stringent minimum requirements for retail exposures.

In addition, the Federation understands that an average three-year maturity has been proposed for the calibration of retail risk weights in order to take into account residential mortgages and that the Committee intends to provide a revised calibration on the basis of ongoing quantitative impact studies.

The experience of European mortgage lenders suggests that a mortgage loan is less risky over time. Over time capital is repaid, collateral remains enforceable and historically increases in value over a property cycle. Typically, mortgage loans in Europe are granted from ten to fifteen years or longer and are on-balance sheet. In Europe, the punitive treatment of longer maturities could be a disincentive to long-term lending and seriously disadvantage mortgage lenders. It could threaten financial stability, increase systemic risk and, ultimately increase the cost of borrowing for consumers.

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Commercial mortgage lending

The Federation welcomes that under the revised standardised approach commercial mortgage lending may, in exceptional circumstances, receive a preferential risk weight of 50%. The Federation would like, however, to draw the Committee's attention to the inconsistencies in the definitions of commercial real estate between the revised standardised approach and the foundation IRBA for corporate exposures.

One of the main criteria permitting the 50% weighting for commercial mortgage lending is that the property has rental income with which to service the loan. In the foundation IRBA this type of lending is excluded and therefore there is no incentive for lenders to move to the IRBA. The Federation <u>would welcome clarification by the Committee on the above inconsistencies</u>.

Yours sincerely,

J. Hardt

Judith HARDT

Secretary General