ZIA Response to EBA FOR DRAFT RTS ON RWS/LGDS – ARTICLES 124 AND 164 CRR

ZIA, the German Property Federation (Zentraler Immobilien Ausschuss e.V.), represents German real estate business in its entirety, including real estate funds and real estate fund managers as well as the listed sector of the industry. ZIA speaks on behalf of individual member firms and more than 20 member associations, thus representing 37,000 branch members.

ZIA welcomes the opportunity to respond to the consultation on DRAFT RTS ON RWS/LGDS – ARTICLES 124 AND 164 CRR. The real estate industry is interested in contributing to the work on how to handle systemic risks on the EU-level. The financial crises of the past have taught that the economic and financial system depends on the abundance of collateral provided by the real estate industry. The availability of collateral is crucial for the functioning of the modern financial system. The well-functioning of the real estate industry thus is of utmost importance to the world economy. ZIA represents the German real estate market, which is the largest in Europe.

Particularly, the real estate industry is an industry that depends on the availability of capital. Especially in those parts of the industry where profit is low, the industry is also very sensitive to deteriorations of the capital supply, even when such deterioration is minor in scale.

General remarks

We would like to make some general remarks regarding (1) the strong connection between the crucial function of the real estate industry for the functioning of modern capital markets and the financial system in general and (2) the contributions of the industry to the real economy and the society. For many regulators, it seems that real estate and its availability is a given, maybe because the industry seems to lack appeal due to its long-term nature. This, however, is a view that is not in line with the sophisticated nature of modern real estate financing and the diverse types of funding of real estate investments contemporarily used.

With regard to the German market, we would like to stress that it acts as a role model: German real estate is financed most conservatively. Especially, loans with variable interest are used rarely. Long term fixed rate loans effectively bring the time horizons of financing and investing in line. This helps to keep risks stemming from credit intermediation in check.

EBA´s proposal on RTS on higher risk weights and minimum LGD values may cause risks for the German real estate market when the authorities might come to false conclusions in regard to the development of the financial stability and if there is any real estate bubble. The financing of real estate is also financing of the real economy because of 30 % of the real economy rents their property from the real estate companies e.g. listed companies, open ended or closed ended funds or other stock holders.

Please note that we strongly support Deutsche Kreditwirtschaft´s comments and give only additional comments regarding German real estate markets.

Question 1: Do you agree with the three main categories of conditions specified for the setting of higher risk weights (paragraph 1) and the setting of higher minimum LGD values (paragraph 2)?

The three main categories of conditions specified for the setting of higher risk weights and the setting of higher minimum LGD values are in the line with CRR and therefore appropriate. From our perspective the historical losses should build the basis for the analysis and should be combined with the different expected losses due to the current development in the markets. Only if a higher volatility is expected the financial stability considerations should be taken into account as a next step. We want to point out that even for that assessment sufficient data collections are needed which are not easily available. A suitable database has to fulfill different criteria: a high frequency without a time lack, a deep regional split, based on real transactions, and a sufficient market coverage. This is very ambitioned because the transaction data are not publicly available in Germany.

Question 2: Do you agree with the conditions for specification of the loss experience and the loss expectations? Do you agree with the adjustments allowed to be made to the loss experience on the basis of the forward-looking immovable property market developments?

The proposed recourse of collected data on behalf of Article 101 is suitable. But we think that the proposal on the adjustments is very complex and the national specifications must also be taken into account.

Question 3: Do you agree with the indicative benchmarks for the assessment of the appropriateness of the risk weights and to guide the setting of higher risk weights across immovable property markets in different member states as specified in Article 4(3) and 4(4)? What levels of these indicative benchmarks would be most appropriate and why?

In our view the benchmark should be close to 0.5 % because even that is very low compared to the most real estate markets. The benchmark of 0.5 % was introduced for the hard test in Article 101 CRR and therefore suitable for the assessment as well.

Question 4: Do you agree with the specification of the term of “financial stability considerations”?

In line with the comments of Deutsche Kreditwirtschaft we believe that the specification of the term of financial stability considerations is not clear enough. We suggest therefore to have a closer look on the spill-over risks for the financial stability. We believe that the risks differ from country to country. For example the owner occupation in Germany is lower than the European average and therefore the risk of a spillover of a price development onto the financial stability via the credit channel is lower than in other countries. Another stabilising effect is generated by the dominance of fixed rate loans which reduce the price elasticity regarding changing interest rates. We therefore think there should be more indicators taken into account which describe the credit chancel and the risk for the financial stability. Insofar we refer to the IMF-proposal in “The IMF-FSB Early Warning Exercise” to have a closer look on the correlation between house prices and consumption over the past ten years, the portion of fixed rate mortgages, the term of typical loans, the home ownership rate and the lending standards. This is very helpful in our view, because in Germany the LTV is lower than in other countries (lower than 70 %). The fixed interest loan is the dominant form of loans in Germany, mostly over a term of more than ten years.

Another stabilizing factor is the valuation with regard to refinancing. In many countries the mortgage lending value is derived from the current market value. In Germany the mortgage lending value (“Beleihungswert”) is calculated according to the German Pfandbrief Act

(Pfandbriefgesetz) and the Regulation on the Determination of the Mortgage Lending Value (Beleihungswertermittlungsverordnung) when the refinancing is planned via a Pfandbrief. The Beleihungswert differs considerably from the current market value. It is determined in a way that leads to a value that in all probability will never exceed the current market value of the asset, even if the market value falls to its possible low. But moreover this very conservative mortgage lending value (Beleihungswert) is multiplied by 0.6 to determine the value that will be taken into account as cover for Pfandbrief purposes (Lending Limit/Beleihungsgrenze).

Question 5: Do you agree with the other conditions for the setting of higher risk weights? (Please provide your feedback related to the indicative benchmarks (in Article 3(3) and 3(4)) in your response to Question 3 above.)

No response

Question 6: Do you agree with the conditions for specification of the exposure weighted average LGD and the LGD expectation? Do you agree with the adjustments allowed to be made to the average exposure weighted LGD on the basis of the forward-looking immovable property market developments? Do you agree that it is not appropriate to set indicative benchmarks for the setting of higher minimum LGD values because of the specificities of national immovable property markets and because of the relationship of the LGD parameter with the other internal model parameters?

No response

Question 7: Do you agree with the other conditions for the setting of higher minimum LGD values?

No response

Question 8: Do you have any suggestions on the Impact Assessment?

No response