Central Bank Commentary on Standard Variable Rate

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Contents

Section 1

27 April 2016. Annual Report 2015 Press Conference Extract:

Arthur Beesley, Irish Times: There was a controversy over SVRs, the Banks were called into the Minister for Finance. Fixed rates came down a little but really the banks haven't responded. What would you say if the government asked you, would it be a good idea to legislate the rates that the banks are charging. Would it be a good idea or a bad idea?

Governor Lane: Our view would be fairly clear: that the correct answer to excessive interest rates are to...are at two levels. One is, if there are barriers to entry deterring new entrants who might come in and try and compete some of those high rates away, the system should work on any barriers to entry that may exist. If there are risk factors contributing to the high interest rates, the more the economy can be de-risked, the more interest rates can come down. If you set a legislative ceiling on rates, what you're going to see is 1, a deterrent to entry. If you set a ceiling where essentially it's unattractive to new entrants to come in, that's going to, if anything, solidify any existing lack of competition. If rates are too low essentially it also changes the nature of who can raise a loan. Because essentially banks will focus on super safe customers as opposed to an SME...an SME who might be a bit risky may well decide they can take on a higher interest rate loan because their projections, they may be able to cover it through a high-risk, high-profit-type strategy. So it's a very crude instrument which has many downsides and really is treating the symptom rather than the underlying factors.

Section 2

19 June 2016. Transcript of Sharon Donnery Interview with Sunday Independent's Dearbhail McDonald:

DMcD: Dearbhail McDonald

SD: Sharon Donnery

DMcD: And what about, it is kind of going back, but what about the SVR cohort, you know, obviously you have to look at it at a broader view but what about that cohort? What in reality can be done for them?

SD: Policy issues around SVR rates are very complex and the Governor has spoken a little bit about this in recent times in the context of the potential for proposed new legislation. The market in Ireland is very disrupted after the crisis and there has been a lot of commentary around there being fewer players in the market and the impact of competition and so on. I certainly think, if you take a more medium term perspective or view, is that regulating interest rates is not necessarily the best way to drive competition. We also published some analysis last year on the factors that underlie the current state of interest rates in Ireland. There are a large portion of borrowers on tracker mortgages which has an impact on the banks, I know that is not of much comfort to people who are on SVRs but that is the wider context and then there are issues around pricing of mortgages in Ireland to do with –

DMcD: Are we pitting different types of home owners against each other? It almost seems that way. It is the trackers versus the SVRs?

SD: Yes and I think that is the challenge. If you are an individual borrower and contractually you have one thing you are obviously in a very different position to someone who contractually has something different. I think when you take the system as a whole though, that research that we published last year has showed that there are many factors that are impacting on rates. Pricing for credit risk, some of the legacy issues that we continue to have since the crisis but I would say again on the policy issue around SVRs that our view has been clear that we don't necessarily think it's the best way to get the outcome that we want. There may be unintended consequences particularly if other institutions are looking at coming here. Obviously if that's the mandate that we are given then it is incumbent on us to do that.

DMcD: And obviously there is legislation there that can give you those powers. There is probably a big question over whether or not you would use it in part because of the whole system of analysing what constitutes a market failure but what would be the impact on other institutions, you know, come in? There seems to be an underlying concern that would we deter both the Vulture Funds and indeed with the SVRs, would we deter other entities coming into Ireland if there were -- if it was perceived that there were restrictions or things that would affect their collateral or other issues?

SD: And that is the critical issue when we talk about the potential for unintended consequences that potential entrants into the market will look at the circumstances in the market and if they feel that there isn't a viable business proposition here that they wouldn't enter the market. So when we talk about a concern around that, that's primarily what that's about.

DMcD: And would for example our lack of repossession culture, there is a lot of people in mortgage arrears particularly I know the situation is improving but if you look at the long term mortgage arrears people in two years or more but there is a sort of cultural reluctance for repossession. Is that something again that might deter other players from coming into the market if it's perceived that the value of their collateral cannot be enforced?

SD: The situation has changed quite a lot during the crisis on that issue. When I was first starting to work on this issue in early 2010 there were lots of uncertainties around the legal framework in Ireland, around the ability to repossess, around bankruptcy and the judicial process, around the Central Bank's own rules and codes. There is a much clearer framework now if someone is looking at Ireland in terms of coming here around everything from the Central Bank's requirements but also the insolvency approach now is much clearer and everybody understands what that is. The government was very clear around that time that the policy objective was to the extent possible to keep people in their homes. That's well understood. One of the things that potentially causes a problem is uncertainty. If people look at a market, not just on this issue but on any issue, if there's uncertainty in the legal framework, there's uncertainty in the regulatory framework, it makes people think twice about decisions. And, not to bring up Brexit too much, but some of the talk around Brexit has been around that. Uncertainty drives people to stop making decisions while they just wait and see what happens.

DMcD: And obviously the legislation again, it's not mandatory but it's a 'may' rather than a 'shall', do you think that there would be uncertainty around just the fact that you've been given that power potentially. Do you think that that creates its own uncertainty?

SD: If the Bank is given those powers, it will be really important for us to set out the framework under which we will consider them. So again, if I just use the mortgage rules as an example, when we were given those powers, which don't just constitute the mortgage rules but constitute a whole range of other tools like capital buffers and so on, we did set out at the very beginning the framework in which we would assess things. In terms also of our public accountability it is very important that we set out how we would implement such powers were they to be given to us.

Section 3

6 October 2016, Quarterly Bulletin 4 Briefing Pack Notes:

Issue	**Standard Variable Rates (SVRs) – incl. pass through of ECB rate cuts**
Message owner	[redacted]
Key messages	**Governor Lane comments from media doorstep on 18 May 2016:** ▪ *"We don't think having legislated caps is the best way of ensuring competition in the mortgage market. Of course, we are subject to laws passed by the Oireachtas so we will work not just to the letter but to the spirit of any law that comes in, so there should be no question about that…As always, we stand ready to assist, whether it's the Government or any member of the Oireachtas. We're always very happy to discuss and talk to whatever member of the Oireachtas or whatever committee seeks our assistance."* **Private Members Bill** ▪ Variable rate mortgage interest rates are driven by a large number of different factors and the residential mortgage market cannot be assessed by only looking at standard variable rate mortgages, as it comprises, inter alia, fixed interest rate, loan to value managed variable rate mortgages, trackers etc. ▪ When all mortgage borrowers are considered, the average interest rate paid in Ireland as at February 2016 is 2.63% - close to the euro area median. ▪ With regard to the proposal to legislate for SVRs, it is unclear whether the aims of the Bill will be delivered through the Bill. Such measures could result in unintended consequences, including negative impacts on the longer term level of competition in the Irish market, and subsequently result in poorer consumer outcomes. ▪ Therefore, as the Governor has previously made clear, we don't think having legislated caps is the best way of ensuring such competition. ▪ But of course, we are subject to laws passed by the Oireachtas so we will work not just to the letter but to the spirit of any law that comes in. ▪ The ECB will also have a legal opinion with regard to effective monetary policy transmission and banking supervision **Consumer protection & transparency** ▪ Taking out a mortgage is one of the biggest decisions a consumer will make in their lives and it is essential that they can deal with regulated lenders with confidence, that the process is transparent and their interests are protected. In the case of variable rate mortgages, this means lenders must be clear with the borrower about the variable nature of the loan and the factors that might cause that rate to change. ▪ We believe there is scope for increasing the level of transparency of mortgage rates.

- We introduced measures aimed at increasing transparency and facilitating consumer choices in July, which set out specific requirements for lenders on the level of information which should be provided to consumers. They should also give borrowers sufficient notice and information to enable the borrower to switch to a different product where they wish to do so.

Pass through

- New lending rates and the spread between the official ECB interest rate and the standard variable mortgage rate are high in Ireland both by historical standards and compared to European peers.
- In May 2015, the Central Bank published its analysis of Influences on Standard Variable Mortgage Pricing in Ireland. The report looked at reasons for the relatively high lending rates in Ireland compared to other EU countries.
- It was found that a range of economic and financial factors are contributing to higher margins including credit risk, competition and profitability considerations.