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## Regulatory Affairs in Europe

### The Heat Is On: EU Competition Inquiries

The European Commission has stepped up efforts to detect anti-competitive behaviour in the payment cards business, retail banking and business insurance. The first *Interim Report on Payment Cards* was launched in April 2006, followed by the *Interim Report on Current Accounts and Related Services* in July 2006. These sector inquiries have the aim to identify if an investigation is needed into anti-competitive practices by the industry. If this is the case and evidence is found, these practices or arrangements can be addressed by anti-trust action.



Stepping Up Pressure: The DG Competition Team

In the Payment Cards report, the Commission criticised that profits were too high, that competition between cards networks was limited and that consumers would be “taxed” for using credit cards (European Commission 2006a). In addition, it also criticized the price discrimination practice where large price differences (up to 100%) exists for the use of the cards by consumers in indifferent countries. One of the main problems identified by the Commission was that there are no common technical standards for cards payments and that national standards would be even “(...) kept secret to prevent the entry of competitors.” (European Commissioner for Competition Policy Neelie Kroes in a speech in April, 2006).

The underlying industrial organization of payment card networks is network economics. In this sense, it is not surprising to find a concentrated market with a few companies that conduct price discrimination. It is also not much of a surprise to find that markets in payment cards are still national as this is the same in retail banking where cross-border transactions are negligible. During a public hearing, the operators of payment card networks clashed with the European Commission (see Euractive 2006). The industry primarily challenged the findings of the report in the area of profits and interchange fees which it regards as essential. All parties however agreed on the importance of creating a Single

Euro Payments Area (SEPA). In the *Interim Report II Current Account and Related Services*, the Commission made a number of factual statements: concerning markets structure and concentration it found in most countries “mild concentration.” In regards to profitability it found that banks have become more profitable since the 1980s. Average pre-tax profits in retail banking in 2004 were around 29%. In the field of consumer choice and mobility, the survey found that customers usually had long relationships with their banks and that there was low mobility in regards to the current account market segment. Across the EU25, it also found high variation in prices for payment services: “The large dispersion in prices suggests that greater cross-border competition could bring down prices, particularly in those countries where payments prices are still relatively high.” (European Commission 2006b). It also stated that the European market is still be very fragmented and featured a number of market entry barriers, ranging from economies of scale or standardisation to conduct of firms. It also hinted at the fact that credit databases (credit reporting systems) could be a potential obstacle to entry.

On most of these issues, the Commission is seeking consultation and expert views. The consultation on this report is open until 9 October 2006, where affected parties can submit their views and comments on questions raised in the interim report. The final reports in both areas will be published by the end of 2006.

**Further information:**

Euractive (2006) Payment Card Operators Clash With Commission (Financial Services Tuesday 25 July 2006).

European Commission (2006a). Interim Report I Payment Cards, Sector Inquiry under Article 17, Regulation 1/2003 on Retail Banking, April 2006.

European Commission (2006b). Interim Report II Current Accounts and Related Services, Sector Inquiry under Article 17, Regulation 1/2003 on Retail Banking, July 2006.

## **No Agreement on Amended Consumer Credit Directive**

The Competitiveness Council, meeting in Brussels on 29 May, did not yet manage to find an agreement on the draft consumer credit directive, although it was positive to find an agreement “in the near future soon”. One of the contested items of the directive, i.e. the full harmonisation approach, seems to be supported by a large majority member states, according to the Council press release. Member States expressed some doubts on the mutual recognition clause as proposed by the Commission in Article 21(2) of its proposal, especially as this principle could be disadvantageous to consumers. A compromise text, circulated by the Austrian Presidency on 21 June 2006, in fact abolishes Article 21(2), and thus further increases the degree of full harmonisation of the directive. The Presidency says in a note (Council 9332/06) that it held an in-depth

examination on many of the key aspects of the directive, and that it produced a compromise proposal on some of them. This text was circulated by the Presidency on 21 June (Council 10597/06) and further clarifies the scope and increases consistency of the directive. The most important change is in fact the reduction of the scope for mutual recognition, as mentioned above, which now seems left for aspect not harmonized by the directive. Other changes concern primarily the articles 5 on pre-contractual information, 9 on contractual information, 13 on the right of withdrawal, 14 on linked transactions and 17 on overrunning (or roll-over) facilities.

## **Financial Services Consumer Group Founded**

In June 2006, the newly established Financial Services Consumer Group (a sub-group of the already existing European Consumer Consultative Group) in Brussels met for the first time. This group brings together consumer representatives from 26 countries, including Latvia, Lithuania, Czech Republic or Poland. The group is co-chaired by DG Internal Market and Services and DG Health and Consumer Protection of the European Commission. Its primary purpose is to stimulate information exchange and discussion between consumer advocates and policy makers to ensure that consumers do get a voice in the European policy-making process. Another effect is initiation and support of financial services expertise in consumer groups in Europe. With the increasing complexity of financial products it is of utmost importance to strengthen the information base of consumers – an area where consumer associations do play a crucial role. The Commission stated that the creation of this group also was essential for the creation of inclusive retail financial services markets that serve all consumers, but also the industry and small and medium companies. In the first meeting, the Commission explained its latest policy initiatives, legislative developments in the area of consumer credit and mortgages as well as the creation of a Single Euro Payments Area.

**Further information:**

Financial Services Consumer Group website:  
[http://ec.europa.eu/internal\\_market/finances/fscg/index\\_en.htm](http://ec.europa.eu/internal_market/finances/fscg/index_en.htm)

## **DG Internal Markets Launches Newsletter**

DG Internal Markets and Services has launched “Fin-Focus,” a newsletter that gives an overview of the Commission’s initiative in the field of Financial Services that are relevant to consumers. The first issue appeared in May 2006. It provided articles about the competition investigations of the Commission in the area of financial services as well as on initiatives for increasing dialog with consumers. It also provides updates on regulatory news in the area of consumer and mortgage credit. For instance, currently the initiative in the consumer credit segment is to review the Consumer Credit Directive. In

the area of mortgage credit, it reviews the steps made by the Commission in the discussion as to whether there should be action to increase the integration of European mortgage markets.

**Further information:**

Newsletter website:  
[http://ec.europa.eu/internal\\_market/finances/index\\_en.htm](http://ec.europa.eu/internal_market/finances/index_en.htm)



**Activities in the EU Parliament**

The latest activities in the Parliament (Committee on Economic and Monetary Affairs) included a hearing on the “New Legal Framework for Payments” in April 2006. Several experts had the chance to voice their opinion on payments services in the European Union. Experts from BEUC (European Consumers’ Organisation), the Groupement des Cartes Bancaires CB, French Banking Commission and the European Payments Council gave statements.

**Further information:**

Hearing in the “New Legal Framework for Payments:”  
[http://www.europarl.europa.eu/comparl/econ/hearings/20060425/default\\_en.htm](http://www.europarl.europa.eu/comparl/econ/hearings/20060425/default_en.htm)

## European and US Market News

### Microfinance Spreads in Europe

Microfinance is increasingly regarded in industrialized countries as effective tool to fight financial exclusion of the poor by providing them with financial services. This low-scale lending – usually found in development countries – happens in form of small (micro) amounts to the un-served or underserved population. In the area, the division of micro entrepreneurs and households are often blurred. But in general microfinance can help to start up small businesses and or improve welfare-increasing consumption smoothing by the households. These lending schemes are increasingly spreading in Europe.

In June 2006, a major conference took place in Budapest with more than 550 stakeholders – organised by the MicroFinance Centre and the European Microfinance Network. Conference participants discussed microfinance developments in Western and Eastern Europe as well as in Central Asia.

“Microfinance” does not have a common European definition. It captures lending to poor and financially excluded people for the generation of income or as incentive to engage in productive activities. In Europe, some stakeholders use the threshold of 25.000 Euro and below to denote microfinance lending. Traditional providers of such lending are microfinance institutions and Non-governmental Organizations (NGOs) that

receive donor funds. But increasingly also banks are interested to downscale their products for providing loans to poor people. International organizations such as the United Nations (UN) or the World Bank are supporting such lending schemes. Last year, the UN proclaimed the “International Year of Microcredit.” And only recently, the World Bank estimated that 500 million people benefit from microfinance. Other services such as micro-insurance or micro-saving also increasingly attract attention.

In Europe, the European Commission has funded several initiatives, for instance the European Microfinance Network (under the Community Action Plan to Combat Social Exclusion). In June this year, the Commission has also launched a 60 million Euro participation in the European Fund for South East Europe (EFSE) which will support private sector development in the Western Balkans also through extended credit lines to microfinance organizations. Even in highly developed countries, microfinance spreads and the European Microfinance Network reports numerous initiatives in Spain, Germany, Italy and France.

**Further information:**

European Microfinance Network website:  
<http://www.european-microfinance.org>

### Credit Reporting Companies’ Profits Soar

Consumer credit risk products are a good business, especially if further expansion of credit demand is expected. Credit reporting companies’ sales as well as profits have been rising over the past years and the future looks bright for the industry. Although the U.S. credit information market is primarily saturated, the industry expands in countries around the world. Over the past 10 years U.S. companies such as TransUnion, Equifax and U.S.-British Experian have pursued aggressive merger & acquisition strategies in several European countries.

The latest reported numbers from Experian show that Earnings Before Interest and Tax (EBIT) from its worldwide activities rose by 29% to 416.6 million £ (610.15 million Euro) from 2005 to March 2006. In the years before, its EBIT grew 20% in 2004 and 16% in 2005. The sales primarily stem from information products and to a smaller extent from its business solutions.

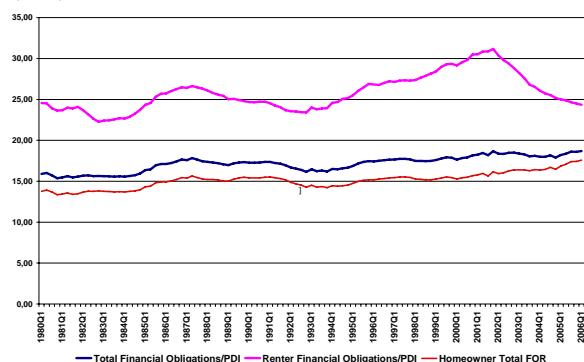
The second large global credit information provider is Equifax. Only recently it reported earnings with record revenue, the latter rising by 7% to 387.7 million USD, approximately 302.85 million Euro (from 2005Q2) while net income rose 11% to 69.9 million USD (54.61 million Euro). The company claims that it has double-digit revenue and profit growth in Latin America, but that also its European activities improved.

The international activities are the fastest expanding business segment for these companies that are under strong competition pressure in the U.S. Especially markets such as India and China are of major interest.

To further reduce operating costs, U.S. companies are already starting to outsource activities to other countries. For instance, TransUnion expects to outsource its dispute settlement to India, Equifax has outsourced data entry to Jamaica and Experian evaluates different options. Although these measures might further increase profits, consumer advocates as well as policy makers are already alert of these developments. Many of these countries do not have functioning data protection laws, the outsourcing is therefore a nightmare for data protection advocates. For credit reporting agencies there might be a bright future in terms of profits, but there are also always regulatory risks such as increasing data protection. Especially developing countries are increasingly regulating the industry, a trend that is globally observable and roughly follows the development in the industrialised countries.

### Latest Trends in US Financial Obligations Ratios

Latest numbers on the US financial obligations ratio show a further downward trend for the credit financing burden of households that are renters and not homeowners. The financial obligations ratio (FOR) adds together debt payments (interest and minimum payments) and components such as rental payments, auto leases or homeowner insurance depending on the type of household for which it is calculated. These payments are then calculated as a ratio to personal disposable income (PDI).



As the figure shows, traditionally, renters do have a higher burden in terms of financing recurrent expenditures as compared to homeowners. Notable is the decrease in the renter FOR starting in 2002. This trend continues according to the latest figures of the Federal Reserve Bank.

However, the burden of the homeowners and that of both groups (renters and homeowners) have continued to slightly trend upwards. The latter series as been relatively stable since the 1980s which has been contributed to decreasing interest rates as well as beneficial cheaper refinancing possibilities in the mortgage market.

## Events and Ongoing Projects

### Second Consumer Financial Capability Workshop

The Second Consumer Financial Capability Workshop at the European Credit Research Institute brought together a wide range of participants from different sectors. It represented the different ideas on consumer financial capability as developed by stakeholders from academia, business and consumer protection associations. The speakers from different backgrounds were assigned to three panels: one with policy makers, one with consumer advocates and one with banks.



Second Consumer Financial Capability Workshop

For each panel, a senior academic chair introduced into latest insights and research in the field. Professor Elaine Kempson (University of Bristol) served as chair for the policymaker panel, Professor Umberto Filotto (University of Rome, Tor Vergata and Assofin) for the banks' panel and Professor Karen Gross (New York Law School) as the chair for the consumer advocate panel.

In the panel on policy making Ginette Nabavi (Health and Consumer Protection Directorate) presented the Dolceta project (see Consumer Credit Newsletter, First Quarter, Spring 2006). She explained that given the emergence of complex products and sophisticated market strategies, the need for consumer education has become increasingly evident at European level. Jurga Stančiūtė (DG Markt, European Commission) informed the audience about a conference to be held on the topic in 2007. Hugues Feltesse (DG Employment, Social Affairs and Equal Opportunities) spoke about combating financial exclusion and overindebtedness and presented the different initiatives with which the European Union identifies and tackles the problem. The International Labour Union was represented by Severine Deboos who spoke about the role of social partners.

In the panel of banks, Dara Duguay (Director of the Financial Education Office at Citibank) presented the activities of her company in the field. Marc Dechevre (Secretary General of the Union Professionnelle du Credit) introduced the audience to the budget tool that his organization had developed together with the Observatoire du Credit and l'Endettement and Fernando Cejudo Sanchez (BBVA) stressed the importance of information transparency in the field of financial products.

Professor Karen Gross chaired the panel of consumer advocates. Here, the Chief Executive of the Personal Finance Education Group, Wendy van den Hende presented how to teach money matters to pupils. And Loretta Pegoretti (Adiconsum in Italy) stressed that too much information for consumers was no information at all. Nikolov Bogomil (Bulgarian National Consumers Association) informed the audience about the problems for consumers in Eastern European states, where they are not used to face choices. Finally, Werner Sanio (Executive Committee Member, BAG Schuldnerberatung and Expert Debt Advice Center SFZ Mainz) introduced a “financial driver’s license” for young adults in Germany. In the afternoon, the workshop participants had the opportunity to discuss with MEP Ieke van den Burg (Dutch Labour Party) ideas for European action in the field of consumer financial capability.

**Further information:**

Program, minutes and other workshop material you will find on ECRI’s website [www.ecri.be](http://www.ecri.be)

## News about ECRI

### ECRI Publication Sales Are Up

ECRI plans to diversify its financial base in the near future. Apart from providing statistics and analysis to the members, it is planned to provide independent expert advice and research to policymakers such as the European Commission, but also governments of developing countries in the area of retail finance regulation and supervision. The fastest growing area of income for ECRI is its publication line such as the ECRI Statistical Package which provides retail credit market data on EU member countries. The work on the new ECRI Statistical Package will start in August 2006.



### New Databases for ECRI Members

ECRI has set-up a number of new databases for its members related to banking, credit and credit reporting. The databases keep track of the legal and regulatory changes in countries around the world. The legal observatories cover 100 countries based upon the World

Bank's Doing Business sample (see World Bank's project website <http://www.doingbusiness.org/>).

**ECRI Banking Law Observatory:** This database provides an overview of banking laws in 100 countries. It reflects the legal status of these laws as of 2005. It also gives the year of enactment, the title, the legal status and the online source where one finds the law. This database enables the user to quickly search through laws as they exist around the world and as they are applicable to banking institutions or institutions that are regulated by the Central Bank in a country.

**ECRI Credit Reporting Observatory:** This database provides an up-to-date overview of laws that are applicable to credit reporting in 100 countries. These laws might either be general data protection laws or laws that are tailored to the credit reporting industry. Of the 100 countries maintained in the database for comparative purposes, approximately 40 have laws in effect. The database gives the year of enactment, the legal status (as of 2005), the title of the act, and the online source where one may find the law. In addition, it includes the rules and regulations for implementing the law (and their online sources).

**ECRI Data Protection Observatory:** The Data Protection Observatory is an overview of data protection laws around the world (data protection laws only, not credit reporting regulation). As above, ECRI maintains 100 countries in the database, although not all of them do have data protection acts. The database displays the title of the law (or if a bill is under review in a country it provides the title of the bill if it was available). In addition, it reflects the legal status as of 2006Q1, the regional influence on the law (for instance, EU) and the adequacy with EU standards insofar as this has been publicly acknowledged by the European Commission. It also provides a link to the online source. The database gives the names and web addresses of data protection officers around the world and as to whether a country is member of a treaty covering data protection (such as the European Council Convention).

**ECRI Public Credit Registry Observatory:** This database provides an overview of the existence and the names of public credit registers (PCRs) around the world. ECRI maintains 100 countries in the database, although not all of them do have public registers. The database is currently still under development. It presents the names of the PCRs, the authority in charge for the PCR, among other information.

### Website Re-launch

The ECRI website will be re-launched this year. This is due to the fact that the former website did not contain specific functionalities. The re-launch also enables us to re-organize the website to increase its usefulness for the user, for instance, by including search functions. There

will be again a member's area that is password protected. Publications of ECRI such as the newsletter, research reports, etc. will remain freely accessible.

### **News on ECRI Statistical Databases**

ECRI is currently implementing major restructuring and reorganization of its statistical databases. This project is ongoing and will take several months. The purpose is to provide members of ECRI with up-to-date statistical information on household debt (mortgages and consumer credit) on European countries and selected other countries of interest such as the U.S. These new files will include quarterly and annual data as long time series as available. In future, these series can be used for predictions as well as for historical reviews. The format will enable the user to easily import the data into statistical programs such as Stata or EViews.

### **Planned Publications**

Within the next months ECRI will publish the following documents:

*Paul, S., S. Stein and D. Kaltofen (forthcoming). Retail Loans: How Banks Can Use Portfolio Segmentation to Reduce Their Capital Requirements, ECRI Research Report, see [www.ecri.be](http://www.ecri.be)*

*European Credit Research Institute (forthcoming). Consumer Financial Capability: Empowering European Consumers, see [www.ecri.be](http://www.ecri.be)*

*Minutes of the Second Consumer Financial Capability, see [www.ecri.be](http://www.ecri.be)*