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European
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Consumer Credit Newsletter

CONTENTS

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REGULATORY ISSUES

State of play in the Consumer Credit Directive saga

Progress on the legislative procedure concerning the draft Consumer Credit Directive (CCD) has stalled in the last few months, while the EU Council has awaited the Commission's amended proposal.

Article 251 of the Amsterdam Treaty makes it clear that after the first reading by the European Parliament (EP), it is up to the Council to further the development of the legislative procedure. As reported by ECRI's Newsletter of July (No. 13), immediately after the EP plenary session, the Council circulated a questionnaire to member states on the key points of the draft CCD. Since then, no further meetings or discussions have taken place in the Council.

Meanwhile, according to the Directorate General for Health and Consumer Affairs (DG SANCO), the Commission is working on the amended proposal, which it expects to adopt in early October.

ECRI has ascertained that the Council will restart discussions in the autumn. Although the last few months have been characterised by little action, the results of the Council's questionnaire combined with the Commission's amended proposal could be a new starting point for discussions.

The controversial political debate surrounding consumer credit reform reduces the likelihood that the Directive will be adopted before 2005. In any case, future developments will also depend on the Commission's reaction to the outcome of the parliamentary vote.

This major step in the consumer credit legislative process reveals once again the strong differences at the institutional level on this particular issue.

The CCD is the subject of an ECRI seminar on 28 October. See full write-up on page 5.

Germany and the UK: Common letter to Commissioner Byrne

The German and UK consumer credit market together account for around 60% of the total EU consumer credit market. Hence, the future Consumer Credit Directive will have a special impact on these countries. The German Ministry of Justice and the Department of Trade and Industry (DTI) have developed common positions in certain key issues of the draft CCD.

First, both countries welcome the EP amendment establishing minimum harmonisation on all aspects except APR. Second, regarding the scope, they support the following exclusions:

- Credit unions in the UK, Ireland and Poland should be excluded as they are small and socially beneficial organisations.
- Pawnbrokers should be excluded as consumers are not compelled to repay any sums that are advanced.
- Credit agreements that are certified by a court or are the outcome of a settlement reached in court should be excluded.
- Bank overdrafts should be partially excluded.
- Consumers already in default should not be excluded from the scope of the Directive, as they may need credit in their vulnerable situation.

British and German representatives to the Council sent a letter that details their common position and requests Commissioner Byrne to consider these points in re-drafting the Consumer Credit Directive.

Consumer credit reform in the UK

New UK consumer credit regulations draw criticism

The new consumer credit regulations in the UK will take effect at the end of October. According to the DTI (Ruth Henrywood, Assistant Director), the UK could not continue to wait for agreement on the CCD, as at present it is hard to predict how long that will take and the evolution and features of the UK market call for regulatory action now. In the DTI's view, the drivers for reform in the UK are:

- problems with consumer information,
- illegal activities by money lenders, and
- over-indebtedness.[1]

The reform aims at tackling these issues.

Yet a recent report from Datamonitor criticises the reform and warns that the regulations proposed by the UK government for the introduction of a clearer regulatory regime of the credit market could have negative effects on both lenders and consumers. It argues that lenders will face very high compliance costs, which could negatively affect smaller lenders and put them out of business. Further, dishonest providers would be able to enter the market more easily. Consumers will also face higher information costs.

Interest rate ceiling vetoed by UK government

The UK government is in the process of reforming its consumer credit market and the issue of whether or not to introduce an interest rate ceiling is related to the reform. On the basis of a study conducted by the DTI, the UK government has decided against introducing such a cap. The reasons given are linked to the belief that the latter can represent an obstacle for low-income borrowers, as well as lead them to choose less appropriate products

[1] See the DTI's White Paper, retrievable from www.dti.gov.uk/ccp/topics1/pdf1/creditwp.pdf.

or even seek credit from illegal lenders. The study shows that interest rate ceilings in Germany, France and the US influence lenders' behaviour. Generally, lenders in those countries do not provide credit for small loans that are repayable in the short term. Consequently, some of the low-income consumers are excluded from the market or take out longer-term loans that are less appropriate for their needs.

The DTI's position against the introduction of interest rate ceilings was confirmed by Ms Henrywood in the seminar on "Consumer Credit and Credit Counselling" at the Madelene College of the University of Cambridge. She did not, however, exclude the possibility of introducing a ceiling at a later stage.

G-10 Governors approve Basel II

In July, the Central Bank governors and heads of bank supervisory authorities in the G-10 countries gave their support to the new Basel II capital adequacy framework. The new framework strengthens capital requirements for banking organisations, by establishing principles that the latter have to respect and follow when assessing the adequacy of their capital. Moreover, in their assessments supervisors can make sure that banks have sufficient capital to sustain their risks. The new Basel II also reinforces market discipline by improving transparency in banks' financial reporting.

The G-10 governors and supervisors aim at continuing discussions with industry representatives and other authorities, as national adoption and approval processes advance. The new framework has to be implemented by the end of 2006. Nevertheless, the more complex approaches to risk management can be implemented one year later. A more distant deadline gives banks and supervisors more time to conduct impact analyses and parallel capital calculations.

MARKET ISSUES

The UK financial market

Mortgage lending falls

Since November 2003 the Bank of England has increased the interest rate five times, with the aim of slowing down the rate of consumer borrowing and the fast-paced growth of the UK property market. The effects of these actions are starting to show. Mortgage lending in the UK was approximately €1.5 billion less in May than in April. The main reason for the drop in gross lending is the decrease in credit for housing purchases. According to Michael Coogan, CML Director-General, it appears that the UK housing market has begun to cool, owing to reduced consumer affordability and rising interest rates. Halifax, the UK's biggest mortgage lender, confirmed a fall of house prices in August by 0.6% – the first fall since August 2002. The fall in housing prices is a clear sign that the growth of UK house prices is slowing down. Yet house prices are still 21.3% higher than they were a year ago.

Car financing decreases by 15%

The successive increases in interest rates by the Bank of England seem to have had a significant impact on car financing in the UK, which decreased by 15% between July 2003 and July 2004 according to the Finance and Leasing Association.

Secured loans increase

The level of borrowing experienced a continued rise with the ratio of personal borrowing to income, doubling between 1995 and 2003. Figures show that the average level of outstanding consumer credit per household has increased from £2,088 in 1995 to £6,464 in 2003.[2] In line with the general increase in borrowing, secured loans have shown a significant rise. Datamonitor notes that the latter

[2] See the DTI's 2004 report, *Tackling Over-Indebtedness – Action Plan 2004*, Department of Trade and Industry, London.

increased by 42% in one year alone (2003-04), mainly because of consumer's increasing difficulties in repaying unsecured debts.

Experian makes credit score accessible for consumers

In June the UK-based credit reference agency Experian launched the first service in the UK that allows consumers to have access to their credit score. This online service enables consumers to calculate their individual credit score and thus better understand their level of indebtedness, the possibility of obtaining more credit and see how lenders may view their individual credit history when they apply for credit. Consumers are also protected as they can react to eventual mistakes in the credit-scoring system.

Recent mergers and acquisitions

Last month saw a number of mergers and acquisitions, at both the European and international levels.

Russia attracts financial institutions

The Russian banking market seems to be increasingly attractive for European banks. The credit outlook for Russian banks is upbeat.

The encouraging prospects of the Russian consumer credit market can be explained by reference to three key factors: a) Russia has a population of about 146 million; b) consumption is rising quickly; and c) household debt is still low. Moreover, the distribution of credit in the Russian market is organised through sales outlets and chains, giving customers easy access to credit offers.

Between 2001 and 2004, the Russian market grew by an average rate of 65% and the outlook for the next ten years is optimistic.

While its 'risky' average bank rating is B, one of the lowest in the world, during the last three years there has been an upward trend in rating. Although the increase in rating will probably slow or level off, it is unlikely to be reversed. Thus it is important that Russia persists in its banking reforms, since its banks are facing increasing competitive and regulatory pressures.[3]

Consumer credit market: BNP Paribas acquires Russian Standard Group

The French banking institution, **BNP Paribas Group**, signed an acquisition agreement in July through its subsidiary **Cetelem** with the leading player in the Russian consumer credit market, Russian Standard Group.

The acquisition amounts to a 50% stake of Russian Standard Group's financial holdings, which include control of more than 90% of the Russian Standard Bank (RSB). This operation will also give Cetelem significant growth potential.

The acquisition of RSB will reinforce Cetelem´s position as a major financial institution in Russia, a country in which the consumer credit market offers significant growth potential.

Other mergers and acquisitions in Russia

At the end of September several European banks showed significant interest in entering the Russian market.

HypoVereinsBank (HVB), Germany's second largest banking group and Nordea, the largest banking group in the Nordic region, have jointly agreed to increase their holdings in the International Moskow Bank (IMB), the eighth largest bank in Russia.

Hansabank announced its intention to acquire Kvest Bank in Moscow. Hansabank has already established its leasing business in Russia and the acquisition of Kvest Bank would allow Hansabank to increase its presence by

[3] For further information, see the results of Standard & Poor's survey, *Russia must Persevere with Banking Reform despite Shaky Start*, 9 Sept. 2004.

entering the corporate banking market, a sector in which Kvest Bank is specialised.

Grupo Santander acquires Dutch car financing company

Grupo Santander has signed an agreement to acquire the vehicle finance company of the Dutch retail Bancassurance Group. Following this acquisition, Santander Consumer will expand its consumer finance business to 11 countries in Europe.

Iceland's largest banking group to acquire Danish bank FIH

Kaupthing Bank, Iceland's largest banking group, will finalise the acquisition of the Danish bank FIH. The Danish Financial Supervisory Authority has approved the transaction. This acquisition allows Kaupthing Bank to enlarge its share of the Danish corporate market. The operation will be completed by the end of October.

BBVA expanding in Texas

BBVA, the second largest Spanish bank, has agreed to buy Laredo National Bancshares, a top financial service provider in Texas. Since BBVA owns also BBVA Bancomer, one of the largest banks in Mexico, this acquisition allows BBVA to increase its presence in the Hispanic market.

Barclays to acquire leading US credit card issuer and South African retail bank

Barclays, the UK's fourth largest bank, announced the acquisition of Juniper Financial Corporation, a leading credit card issuer in the US in August. At the end of September, it started negotiations for the acquisition of a majority stake in Absa Group Ltd., South Africa's largest retail bank.

Barclays is currently enlarging its business and through the acquisition of Juniper it could enter the US credit card market, which is one of the largest markets in the world. Through the acquisition of Absa, a deal that would represent Barclay's largest foreign transaction to date, it would significantly increase its presence in South Africa.

CC-Bank hardens credit conditions

CC-Bank, a German bank specialised in consumer credit, wants to reduce its risk costs by strengthening the conditions required to obtain credit. Besides individual assessment, other statistically relevant criteria such as age, profession and family conditions will also be taken into account for the determination of a client's credit score. This strategy should allow CC-bank to maintain its level of risk costs below €147 million in 2004.

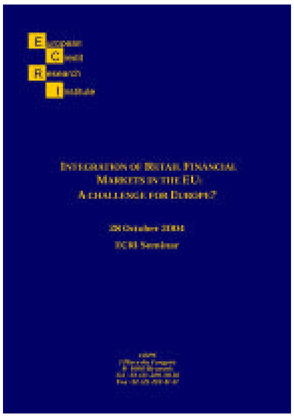
The direct approval of credit will stagnate but the increase in retail finance (by 50%) and car finance (by 10%) will allow CC-Holding to continue growing, its strength remaining the business of consumption finance.

CC-Bank has been owned by Grupo Santander since 1987 and has acquired AKB-Bank and part of Santander Direktbank in Frankfurt.

ECRI NEWS

ECRI Seminar in October
Integration of EU retail financial markets: A challenge for Europe?

The integration of EU retail financial markets and the future Consumer Credit Directive is the focus of a high-level seminar organised by ECRI on 28 October. The forum will bring together policy- and law-makers along with representatives from consumer and industry groups.



Integrating retail financial markets is still a challenge for the EU. The positive outcome of the FSAP has not been reflected in the field of retail financial services today. Action is needed but questions remain about how to define a realistic policy strategy.

ECRI offers an effective forum for discussion on the real possibilities of achieving market integration in retail finance. The three main sessions will cover:

1) Evaluation of the market and business experience

The aim of this session is to assess the current market situation, as well as to gain an understanding of business experience. **Nick R. Page**, Partner, Corporate Finance, Pricewaterhouse Coopers, will give an overview of the current market, evaluating the level of integration, highlighting the benefits and obstacles encountered.

Later, representatives of the financial markets will present their experience. Owing to the difficulties of entering foreign markets through cross-border activity, it is widely acknowledged that it can only be done through mergers and acquisitions or joint ventures. In this context, **Pierantonio Rumignani,** Managing Director, Santander Consumer Finance, and **Eric Spielrein**, Senior Vice-President and Corporate Secretary, RCI Banque (Groupe Renault), will discuss the strategies used to overcome obstacles in cross-border expansion.

2) The regulatory perspective

It is not clear whether EU legislative intervention to facilitate cross-border delivery will materially influence market outcomes.

First clarification is needed as to whether potential trade is being stifled by legal or regulatory barriers or whether cross-border trade is taking place in a manner that is detrimental to consumers (or both).

Which retail financial services require legislative intervention in the EU in order to support cross-border delivery also needs to be established.

Consumer trust and confidence is a pre-requisite for the cross-border delivery of financial services. Any legal intervention must contribute to developing such trust.

A realistic policy needs to be developed to define the utility of achieving a single retail financial market. The cost-efficiency of introducing legislative measures for this purpose must be evaluated.

Hence, the regulatory framework for the achievement of an integrated EU retail financial market needs to be discussed with the market players. This session brings together representatives from institutions, industry and consumer groups to debate the guidelines of a positive regulatory policy. **Alexander Schaub,** Director-General, Internal Market, EU Commission,[4] will present the Commission's past, current and future approach for the achievement of a single retail financial services market. **Rosa Maria Gelpi,** Vice-President, Cetelem Group and Chairman of the EBIC CCD Working Group, will discuss the difficulties encountered by the industry in the development of cross-border retail finance in the EU. She will refer to the regulatory issues with regard to consumer protection. Finally, **Donal Walsche,** Secretary-General of Euro Coop, will refer to the role of consumer protection legislation as a key issue for market integration.

3) The proposed CCD – National views in the EU Council

Discussions on the draft CCD will soon be underway again in the Council. After the amendments are agreed by the European

[4] If Mr Schuab is unable to attend, another senior Commission official will give the presentation.

Parliament, it is for the Council to decide on the final draft.

The British and German representatives on the CCD to the EU Council (respectively Hergen Haye, DTI, and Peter Horne, Ministry of Justice) will present their views on the draft CCD. They will also comment on the Commission's response to the amendments introduced by the EP to the original text.

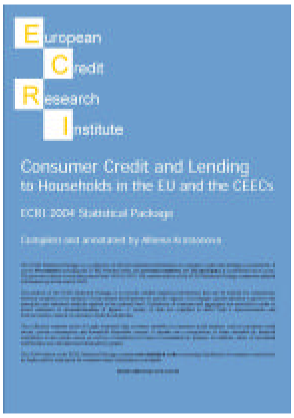
The views of the German and British representatives are especially significant as the market of these two member states accounts for around 60% of the total EU market.

Their discussion will be complemented by the participation of **Stephan Huber**, assistant to MEP Joachim Würmeling (Rapporteur of the CCD), who is actively committed to the parliamentary amendments, and **Karel Lannoo**, CEO of CEPS and ECRI.

For further information see: www.ecri.be

New ECRI Statistical Package 2004

An updated version of the ECRI Statistical Package will soon be available. The Statistical Package is an annual collection of relevant statistical data on consumer credit and lending to households.



The Statistical Package brings together data covering 30 countries, including:

- EMU-12 – Austria, Belgium, France, Finland, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain;
- EU member states that are not members of the EMU – Cyprus, Czech Republic, Denmark, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, the Slovak Republic, Slovenia, Sweden, and the United Kingdom;
- EU accession countries – Bulgaria and Romania;
- EU candidate country – Turkey; and
- G-7 countries – Japan and the US.

The current edition of the ECRI Statistical Package comprises updated information up to the end of 2003. Data in the previous edition covered the period 1990-2002.

The purpose of the ECRI Statistical Package is to provide information that can be used for comparisons between countries or for analysis of loan-market developments in specific regions. In this context, special attention is given to the principles and statistical methods applied at the national level. Definitions of the concepts and aggregates are provided, along with a glossary of abbreviations and symbols, in order to avoid any confusion or misunderstanding of the figures. A variety of data are compiled to allow both a macroeconomic and microeconomic outlook of consumer credit developments in the countries selected.

The collection contains series of rough (nominal) data on major variables in consumer credit analysis, such as consumer credit stocks, private consumption and disposable household income. It spreads out a composition of loans extended by financial institutions to the private sector as well as a breakdown of loans to households by purpose. In addition, ratios of household indebtedness are calculated and illustrated.

The updated edition of the ECRI Statistical Package contains a **new statistical series** concerning distribution of consumer credit stocks by lender and by instrument for countries where information is available.

The package will soon be available at www.ecri.be.

ECRI STATISTICAL PACKAGE 2004

Executive Summary

Figure A. Composition of total loans extended to households by category, 2003

Figure B. Distribution of consumer credit stock in the EU by country, 2003

Introduction

I. Figures

1. Evolution of consumer credit in the EU and the US 1995-2003 (as a percentage of GDP)
2. Lending to households by type of loans (the EMU-12, the EU-15, the EU-10 and the US) in 2003 (as a percentage of GDP)
3. Composition of lending to households in EU countries by type of loans in 2003
4. Composition of lending to households by type of loans (in selected EU member states and accession countries) in 2003
5. Consumer credit as a percentage of private consumption, 2000-2003
6. Consumer credit as a percentage of household disposable income, 2000-2003
7. Consumer credit as a percentage of GDP, 2000-2003
8. Outstanding Consumer credit per capita in 2003

II. Tables

1. a. Lending to the private sector, 2003 (stocks)

1. b. Lending to the private sector, 2003 (as a percentage of GDP)

2. a. Consumer credit, 1990-2003 (stocks)

2. b. Consumer credit, 1995-2003 (as a percentage of GDP)

3. a. Consumer credit by lender, 1995-2003 (stocks)

3. b. Distribution of consumer credit by lender, 1995-2003 (percentage)

4. a. Consumer credit by product, 1995-2003 (stocks)

4. b. Distribution of consumer credit by product, 1995-2003 (percentage)

5. Private consumption, 1995-2003

6. Household disposable income, 1995-2003

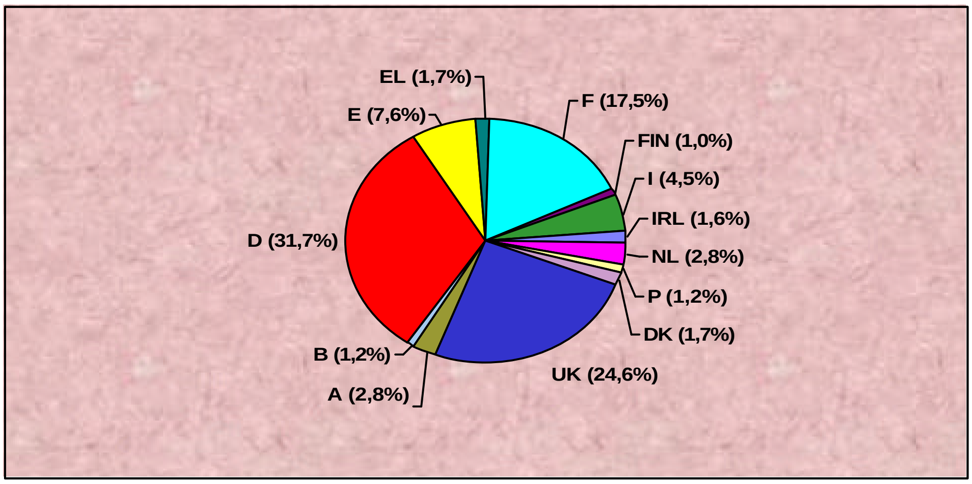
7. GDP at current prices, 1995-2003

III. Explanatory Notes and Definitions

1. General notes
2. Country-specific characteristics

Glossary of Abbreviations and Symbols

Distribution of consumer credit stock in the EU by country in 2003


EL (1,7%)
E (7,6%)
F (17,5%)
FIN (1,0%)
I (4,5%)
IRL (1,6%)
D (31,7%)
NL (2,8%)
P (1,2%)
DK (1,7%)
B (1,2%)
UK (24,6%)
A (2,8%)