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ECRI NEWS

Understanding Credit Markets for Europe

A RENEWED INTEREST IN THE FUTURE OF RETAIL FINANCIAL SERVICES

A message from Sylvain Bouyon, CEPS Research Fellow, Head of the European Credit Research Institute

The European Commission is expected to publish its long-awaited Green Paper on retail financial services by the end of the year. On the menu, cross-border provision of financial services, digitalisation of the financial sector and enhanced competition. As emphasised by Karel Lannoo on page 2, cross-border provision of financial services in the EU remains marginal. The strength of incumbents and localregulators seems to be an important factor deterring newcomers from entering the market, along with price pressure and innovation. Current efforts to reinforce the single market in financial services already face tremendous challenges and these should be tackled through a better implementation of existing European rules rather than through the development of new harmonising measures.

Against the background of renewed interest in the future of retail financial services, ECRI will organise a series of conferences in the coming months in order to discuss some key issues affecting this particular sector. On 26 January 2016, a conference on "Over-indebtedness of European Households: Myths and Realities" will be organised with the aim of understanding the drivers and effects of over-indebtedness and evaluating innovative tools to tackle and/or prevent this phenomenon.

In cooperation with VISA Europe, on February 10th, another ECRI conference will address the latest issues in relation to the recently revised and adopted Directive on Payment Services (PSD2). A third conference to take place in April will feature the launch of a new book, Milestones in European Housing Finance, co-edited by Jens Lunde and Christine Whitehead and published by Wiley-Blackwell This important event is timed to coincide with the transposition deadline of the Mortgage Credit Directive (Article 42) and will contribute to a better understanding of the high diversity of mortgage business models across the EU-28.

In the meantime, ECRI continues to build its expertise on the topic of financial technologies (FinTech), which are expected to markedly shape the financial sector in the coming decade and thereby raise diverse regulatory and policy issues. On page 5, Monica Monaco and Ugo Bechis focus their attention on payments, which are likely to be the segment most impacted by Fintech. The authors question the concept of "strong customer authentication" as defined by the PSD2, and analyse its implications for cyber-security. The authentication of consumers in payment and e-commerce will also several different areas of the European Commission's work including Third-Party Payments Providers (TPPPs), liabilities and security breach responsibilities and the objectives of the Digital Single Market Strategy (DSM) Communication published in May 2015.

While new technologies should have a lower impact on housing finance, other recent trends unrelated to technologies might exert a strong influence on the future development of mortgage markets. On page 4, Darinka Czischke sheds light on the wide-ranging changes in social housing and affordable housing sectors of many EU member states. In a context of persistent budgetary austerity, public-sector funding for social housing and affordable housing is tending to decrease across Europe. New funding models, with an growing role of private-sector investments, are therefore needed and might require regulatory adjustments.

Two recent ECRI commentaries ("Recent trends in home ownership" and "Home ownership, labour markets and the economic crisis") have highlighted the latest trends in home ownership across the EU-28. The analysis of time series on home ownership since 2007 reveals three striking phenomena: the continuation of highly diverse home-ownership rates across countries, significant contractions in the UK and Ireland, and marked contractions in ownership among poorer households in the EU15. In parallel, recent macroeconomic data published by Eurostat suggest that the variables of mobility and home ownership have had a significant impact on the dynamics of unemployment rates across the EU28. A policy model with further emphasis on renting might emerge in that context.

Finally, ECRI continues to cover all issues related to consumer credit. On page 3, Nick Jones, Head of Communications at International Personal Finance, presents the results of a recent IPF survey of its customers' view across a range of financial topics: their primary economic concerns, confidence in the future, retirement planning, trust in the financial sector, etc. One of the main findings of the report is that the cost of living remains by far the biggest concern for households in Eastern Europe.

On a final note, regarding macroeconomic data, ECRI has recently published the new edition of its highly authoritative, comprehensive and frequently cited set of statistics on consumer credit in Europe. It is worth noting that the 2015 Statistical Package includes for the very first time several "emerging" economies (India and Russia).

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IN THIS NEWSLETTER

ECRI Newsletter Articles

FORMING A RETAIL FINANCE UNION OR WAITING FOR GODOT?

By Karel Lannoo, Chief Executive Officer, CEPS

The cross-border provision of financial services in the EU is minimal. On average, it represents about 1% of the services provided across the 28 member states. All the efforts undertaken over the last years to allow consumers to reap the benefits of the single market have also yielded very little results in financial services. As with other utilities, the strength of incumbents and local regulators seems to be an important deterrent keeping aspiring newcomers at bay, and with it price pressures and innovation. Hence, what can the European Commission achieve with its Green Paper on retail financial services?

As with the Banking and Capital Markets Unions, a Retail Finance Union is needed to create both depth and scale for financial markets and to give consumers a wider choice. This would not require an additional wave of harmonising measures. On the contrary. The premise should be that as a result of the single rulebook and Banking Union, prudential standards have become so harmonised that member states' objections to the cross-border provision of financial services must be directly challenged by the EU authorities. Rules have become so identical in the EU28, that any means to prevent cross-border provision should be generally deemed as invalid.

To ensure the acceptance of cross-border financial services, it would be useful to follow the logic of the Banking Union. Next to the prudential supervision 'peak' of the ECB, greater cooperation needs to be established among conduct-of-business supervisors in the EU under a second 'peak', across the different functional supervisors EBA, ESMA and EIOPA. Now that the big post-crisis regulatory wave is almost over, the ESAs should have more time for their other responsibilities, namely the "tasks related to consumer protection and financial activities" (Art. 9 of the ESA Regulation). Its 'Committees on financial innovation' (Art. 9.4 ESAs) should be re-invigorated and used as a tool to exchange information on market developments.

The US example can serve as a useful model. The Securities and Exchange Commission is a powerful body defending the interests of investors, also on the retail side. It suffices to look at its mission statement 'The Investor's Advocate' and its enforcement actions. Furthermore, as called for in the Dodd-Frank Act, a powerful consumer body was created, the Consumers Financial Protection Bureau, to educate consumers, enforce laws and study market developments. Five years after its creation, the Bureau already employs over 1,500 persons, well above the total ECB banking supervision staff.

In an environment of widespread and growing doubts about the European project, an initiative that shows consumers that the EU matters can be immensely helpful to counter such attitudes. This does not necessarily require the formulation of new laws or constructing new institutions, but simply using existing structures and enforcing laws already on the books.

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UPCOMING ECRI CONFERENCES

26 JANUARY 2016
10:30-17:00
CEPS, Brussels

Over-indebtedness of European households: Myths and realities

10 FEBRUARY 2016
11:00-13:00
CEPS, Brussels

Strong Customer Authentication within the context of the PSD2

19 APRIL 2016
11:00-15:30
CEPS, Brussels

Housing Finance models across the EU28

For further information about ECRI conferences, please contact Vilde Renman (vilde.renman@ceps.eu)

ECRI STATISTICAL PACKAGE 2015 OUT NOW

For the first time, detailed data on several "emerging economies"

WHAT IS THE ECRI STATISTICAL PACKAGE?

Since 2003, the European Credit Research Institute (ECRI) has published a highly authoritative, widely cited and complete set of statistics on consumer credit in Europe. This valuable research tool allows users to make meaningful comparisons between all 28 EU member states as well as with a number of selected non-EU countries, including the US and Canada.

WHAT IS COVERED?

Two Statistical Packages are on offer. The more comprehensive product "Lending to Households (1995-2014)" contains valuable data on consumer credit, housing loans, other loans, total household loans, loans to non-financial corporations as well as total credit to the non-financial business and household sector. The 'standard' "Consumer Credit in Europe (1995-2014)" exclusively covers consumer credit data.

The 2 Packages in Fact & Figures:

• 40 Countries: EU 28, Turkey, Rep. of Macedonia, Iceland, Norway, Switzerland, Liechtenstein, Australia, Canada, Japan, the United States, India and Russia.

• 20 years data series: 1995-2014

• National accounts: GDP, final consumption expenditure and gross disposable income of households, inflation and exchange rates.

• 150 (67) tables: present time series data in nominal and real terms, and per capita, as well as breakdowns by lender, type, currency and maturity are also available for selected countries.

• 27 (13) figures: highlight credit trends in a way that allows user to make meaningful comparisons of the retail credit markets across countries.

FACTSCHEETS

The European Credit Research Institute (ECRI) provides indepth analysis and insight into the structure, evolution and regulation of retail financial services markets in Europe. Through its research activities, publications and conferences, ECRI keeps its members and the wider public up-to-date on a variety of topics, such as retail financial services, credit reporting and consumer protection at the European level.

ECRI is an independent, non-profit research institute whose interdisciplinary team of researchers and academic cooperation partners has developed a specialised body of knowledge on retail financial markets. It was founded in 1999 by a consortium of European banking and financial institutions. ECRI's operations and staff are managed by the Centre for European Policy Studies (CEPS) in Brussels.

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INTERNATIONAL PERSONAL FINANCE

Living costs seen as biggest concern in Eastern Europe

By Nick Jones, Head of Communications, IPF

International Personal Finance ('IPF' or the 'Group') is an international consumer credit business with roots in Northern England going back over 130 years. In our international markets we trade under the Provident brand as well as a number of digital brands, including Credit 24 and 'hapiloans'.

Every 12 months, IPF undertakes a major piece of consumer research that seeks to gain a greater understanding of our customers' views across a range of financial topics, including how satisfied they are with their standard of living, their primary concerns, economic confidence, views on retirement planning, as well as their trust in the financial sector. The primary motivation for this report, however, is to give our customers a voice in the ongoing debate among key decision-makers and influencers on financial inclusion.

What did we find?

We found that living costs remain by far the biggest concern for people in East European countries. Forty percent of respondents in the survey cited living costs as the most concerning factor. Perhaps not surprisingly, rent and mortgages are seen as the biggest drivers of increased living costs. This was especially true for people in Hungary and Romania.

Looking at economic confidence, we were surprised that there was a significant difference in how people viewed their own household outlook against that of their national economy. People were more optimistic about their own household performance than that of their national economies. Increased personal income was the main driver of this. Help from the state was ranked very lowly, with only 1% thinking it would contribute towards an improved financial position.

Exploring access to credit services, the survey found that just over half of European respondents have no cash savings and the same number said that they themselves had been asked for financial help. Almost half of the respondents are more cautious in their spending than last year, with holidays seeing the greatest reduction in spending. It was disappointing, although not entirely unexpected, to see two-thirds of Europeans not saving for their retirement,predominately due to a lack of disposable income.

As a business that issued over one billion pounds in

2014, affordability is something that we take seriously. We were therefore pleased to see the ability to repay loans as the main factor when taking out credit. Across all of our markets, our customers think carefully before borrowing, and, on the whole, do not act on impulse. With a lack of savings, unexpected expenses were the main reason for taking our credit, followed by debt consolidation and home improvements. The majority of people only use credit in an emergency and never borrow more than they can afford to repay. It was also notable that our customers view the annual percentage rate, ease of applying and reputation of the provider as the most important factors when deciding to borrow money.

In conclusion, while there are differences from country to country, East Europeans are above all concerned about their living costs, yet believe their financial well-being will improve in 2016. As a business that lends responsibly we are pleased that our customers think carefully before taking on debt and consider from whom they borrow money.

If you would like to receive our 2016 report, or have important financial questions that you need help in answering, then please get in touch. By working together we aim to make this report mutually beneficial – for all our external stakeholders as well as for the IPF Group.

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THE CHANGING LANDSCAPE OF AFFORDABLE HOUSING FUNDING MODELS IN EUROPE

By Darinka Czischke, Professor, Delft University of Technology

Both the social housing and affordable housing sectors are undergoing wide-ranging change in many EU member states. In England and the Netherlands, for example, while social housing is becoming a residual tenure for those on very low incomes, affordable housing is seen as an instrument to help middle-income groups rent housing at below-market price. In France, affordable housing is aimed at assisting low-income households to buy their first home. In other cases, government programmes aimed at supporting this type of housing have been weakened or even abolished due to austerity measures. A case in point is Poland, where 2009 saw the demise of the National Housing Fund (established in 1995), which until then had supported the delivery of affordable housing to employees and workers. Overall, there is a trend across Europe towards the reduction of public sector funding for social housing, which means that funding models require a re-think.

At least two macro trends can explain these developments: on the one hand, macro-economic constraints (notably those stemming from the global economic and financial crisis), and on the other, domestic events such as the recent reform of the social housing regulatory framework in the Netherlands. As a result, in countries like England and the Netherlands we see that a new market segment for the provision of 'affordable housing' is opening up to housing providers, both not-for-profit and for-profit.

In the Netherlands, the new 2015 Housing Act restricts the activities of social housing corporations in the moderately priced private rental sector, with the aim to create a more level playing field and attract private sector investments. A key question is whether or not for-profit housing providers are willing to enter this market. So far, there is inconclusive evidence that this is the case. Recent private sector investments in this segment have been largely driven by a lack of attractive investment opportunities in the owner-occupied housing sector.

Now that the housing market is recovering, there are indications of for-profit sector retrenchment from the rental sector. Taking the example of England again, the 'affordable rental housing' product launched in 2011 by the coalition government allows housing associations to charge up to 80% of market rents. However, despite being labelled 'affordable', sharp variations between regional housing markets mean that this is not necessarily the case everywhere. In a city like London, for instance, 80% of the market price is still not affordable for the majority of the capital's inhabitants.

In addition, there is a growing trend in many European countries to tackle housing affordability through alternative forms of provision, such as so-called collaborative housing initiatives. These include a wide variety of approaches to the provision of mixed-income and mixed-tenure housing. While not (yet) in large numbers, the strategies applied in these initiatives represent examples of innovation, notably in the field of non-speculative funding models for affordable housing. In this regard, interesting opportunities for socially responsible lending open up. We are currently conducting research on funding models for social and affordable housing for the European Investment Bank (EIB) at the Department of Management in the Built Environment at the Faculty of Architecture and the Built Environment (TU Delft). The study looks at affordable housing policies and funding models through six country case studies. We expect to publish a report on our findings next spring.

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HOW TO AUTHENTICATE A PAYMENT IN E-COMMERCE: STRONG CUSTOMER AUTHENTICATION REQUIREMENTS, THE EBA RTS AND CYBER SECURITY

By Monica Monaco, Founder and Managing Director, TrustEu Affairs and with contributions from Ugo Bechis, e-Payments & SEPA Advisor, UBI Banca

As clearly outlined in the European Parliament study "Building blocks of Ubiquitous Digital Single Market"[1], cybersecurity is an upcoming regulatory challenge.

The authentication of subjects in a payments and e-commerce context is at the core of this discussion and affects the European Commission's work in many different ways, raising questions about Third Party Payment Providers (TPPPs), liabilities and security breach responsibilities, and the very objectives of the Digital Single Market Strategy (DSM) Communication, which was published by the European Commission on 6May 2015 and includes actions on cybersecurity.

It is well known that e-criminals devise sophisticated methods to intercept customer credentials and to modify transactions even protected by general passwords, be these fixed or dynamic passwords.

Such risks would likely increase in the second Payment Services Directive (PSD2) scenario where an extra layer is factored in with the presence of a new entity, the TPPPs, if the security along all links of the chain is not duly assured.

For this very reason, PSD2, voted upon in the European Parliament on 8 October 2015, defines "strong customer authentication" as an authentication based on the use of two or more elements categorised as "knowledge"(something only the user knows), "possession" (something only the user possesses) and "inherence" (something the user is) that are independent, in that the breach of one does not compromise the reliability of the others. It is designed in such a way as to protect the confidentiality of the authentication data (Article 4.30 PSD2).

Such a definition, open to various interpretations until the European Banking Authority (EBA) drafts the related Regulatory Technical Standards –expected between 2016 and 2017 – may or may not refer in reality to existing authentication methods and opens the door to new authentication methods to be exploited and defined.

Two issues appear to be sensitive in the light of recent authentication practices in the market:

a) the very 'independence' of the two elements, which is overcome by the 'tokenisation' solutions where one token represents such two elements, being their 'technical proxy' and

b) the 'possession' concept, not necessarily controlled by the user, where the instrument authentication data are in a digital wallet hosted in a 'cloud' environment out of his/her control.

According to recital 107 and Article 98 of the PSD2, the EBA will prepare draft Regulatory Technical Standards(RTS)onsecurityaspectsofpaymentservices,in particular with regard to strong customer authentication, which the Commission would then adopt.

These RTS would specify both the requirements of and the exemptions from strong customer authentication, and more precisely the requirements for common and secure open standards of communication for the purposes of identification, authentication, notification, and information, as well as for the implementation of security measures, between account servicing payment service providers, payment initiation service providers, account information service providers, payers, payees and other payment service providers.

The level of depth of those RTS will be relevant, i.e. how they will logically address all the issues outlined above and the degrees of freedom they will leave to the level of technical specifications.

Furthermore, the EBA exemption criteria could be based on the level of risk involved in the service provided, the amount, the recurrence of the transaction, or both, as well as on the payment channel used for the execution of the transaction.

The Network Information Security Directive (NIS), now in its final discussion phase, will also affect the security of the 'channels', with reference to the status and responsibilities of the 'internet enablers', e.g. the 'big data' subjects, often operating from a third country, beyond EU jurisdiction.

For the time being we know from the PSD2 that the implications of not applying strong customer authentication are very serious, both in terms of liabilities (Article 74 of the PSD2) and well as in the case of recourse. As Article 92 of the PSD2 sets out, where the liability of a payment service provider is attributable to another payment service provider or to an intermediary, that payment service provider or intermediary shall compensate the first payment service provider for any losses incurred or sums paid, including in cases where any of the payment service providers fail to use strong customer authentication.

We also know (Article 97 of the PSD2) that member states shall ensure that a payment service provider applies strong customer authentication where the payer

1.accesses its payment account online;

2.initiates an electronic payment transaction;

3.carries out any action through a remote channel that may imply a risk of payment fraud or other abuse.

As far as the initiation of payments is concerned, the article specifies that member states shall ensure that, for electronic remote payment transactions, payment service providers apply strong customer authentication that includes elements that dynamically link the trans-

1 Building blocks of Ubiquitous Digital Single Market", Study for the IMCO Committee, EuropeanParliament, February 2015.

action to a specific amount and a specific payee.

The article further specifies that such rules shall also apply when payments are initiated through a payment initiation service provider (PISP) or when the information is requested through an account information service provider(AISP) – AISPs and PISPs being TPPPs types.

Furthermore, member states shall ensure that the account servicing payment service provider allows the payment initiation service provider and the account information service provider to rely on the authentication procedures provided by the account servicing payment service provider to the payment service user.

How member states ensure all this, and whether they interpret such obligations differently, also in consideration of whether TPPs are present in one member state or another, is still to be determined.

How would the European Banking Authority deal with this very difficult task?

Would for example the "requirements for common and secure open standards of communication" hint at any technical standard body that shall then develop these standards? How will those open standards of communication fit into or be compatible with the W3C[2] Web Payments Working Group as regards standard requirements for signature, cryptography and open Application Protocols Interfaces (APIs)? And would the user identification security standards be those defined by ETSI– which is already developing standards for e-Identity (e-ID) applicable to Telcos– or the ISO standards more specific for payment initiation credentials, or any other?

Many experts, as well as some of the European member states during the PSD2 Trilogues, have raised the possibility of aligning the PSD2 payment authentication with the eIDAS requirement.

The eIDAS Regulation 910/2014 sets general EU-wide standards for electronic identification and trust services for electronic transactions and requires qualified electronic signature creation devices, while introducing e-signatures for consumers and e-seals for legal entities.

If such methods were to be used when authenticating a payment, electronic signatures would theoretically ensure the identity of the signing customer andnon-modification of the transaction content as e-signed payments initiation data cannot be modified, either in the TPPs or in the banking domains.

Could the EBA align PSD requirements and terminology with eIDAS? Will the EBA RTS point to a set of standards to be further developed outside of the EBA remit? And how will such EBA RTS satisfy the needs of the convergence of e-Commerce and mobile payment practices where the commerce transaction tends to be consolidated with the e-payment?

One solution could be to address all these dependencies – not so much in terms of principle, as has been the case so far, but in aligning their actual content details and their delivery schedule, to allow a consistent and efficient implementation by the market players.

In the meantime, cybersecurity remains a challenge to the further development of e-commerce in Europe, the US and elsewhere. Let us say, however, that the intense debate on these matters can be taken as a hopeful sign.

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2 W3C is an International standards body for Web Technology.

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ECRI PUBLICATIONS

Key findings from the ECRI Statistical Package: Sixth year of contraction in European private credit markets, despite a stabilisation on the housing market

Robin Sainsot, 3 September 2015

http://www.ceps.eu/system/files/Key%20findings%20 2015%20final_1.pdf

Home ownership, labour markets and the economic crisis

Sylvain Bouyon, CEPS/ECRI Commentary No. 14, 15 June 2015

http://www.ceps.eu/system/files/ECRI%20Commentary%20No%2014%20SB%20Home%20ownership%20and%20labour%20markets%20FINAL--.pdf

Recent trends in EU home ownership

Sylvain Bouyon, CEPS/ECRI Commentary No. 15, 16 June 2015

http://www.ceps.eu/system/files/ECRI%20Commentary%20No%2015%20SB%20Recent%20Trends%20in%20Home%20Ownership%20in%20the%20EU-28%20final_0.pdf

Report on the conference "Consumer protection in financial services, the challenges of innovation and capital markets union" (12 May 2015)

http://ecri.eu/new/system/files/48ECRINewsletter2.pdf