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Central Bank of Ireland
New Wapping Street
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25th March 2022

Re; CP146 Mortgage Measures Framework Review

Dear Governor,

The Society of Chartered Surveyors Ireland (SCSI) is a professional body representing approximately 5000 members who are typically employed across the built environment in the construction, land, and property markets through private practice, in central and local government, in state agencies, in academic institutions, in business organisations and in non-governmental organisations.

We are writing to you in relation to the Central Bank's current review of the mortgage measures framework. Our members are well positioned across the entire property lifecycle to provide accurate feedback as they work closely with owners of residential property, prospective purchasers, renters, contractors, developers, and investors. As such, our submission harnesses their experience and expertise to provide an overview of the national property market and proposes considerations for the Central Bank as part of this review.

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The introduction of the macroprudential framework in 2015 was a measure intended to safeguard financial stability and prevent house purchasers from borrowing beyond their means which the SCSI supports in principle. The need for better regulations and a prudent lending approach to protect households against high levels of indebtedness is critically important and continues to be acknowledged by SCSI as an important lever to reduce systemic risk to banks and reduce financial risks to the economy.

Since 2015, national property prices have risen by approximately 60% according to the Central Statistics Office (CSO) National Property Price Index. The MPR's are achieving their stated aim of preventing an excessive build-up of credit within the house purchase sector, but they are also having an impact across the development market. Significant political pressure in recent years called for relaxations of the regulations often describing the rules as 'crowding out some buyers from the market'. Whilst there may be some truth to this, the indirect impact of the MPR's on the residential rental market may also be exacerbating the elevated levels of rent inflation which is reported by business groups as impacting on the economy and cost of living.

There are many other factors at play when considering house price inflation such as rising populations, wage growth etc. Population demographics can play a role in escalating house price inflation, for example, a growing proportion of the population within the 25-35 age bracket can increase demand for property purchasing and therefore increase values. The main solution however to provide an acceptable level of supply / demand equilibrium is to increase the delivery of new housing in areas of demand to tackle rising accommodation costs. In recent years, this has become more and more difficult for the development sector to continue to increase the supply in an environment of hyperinflation of building materials and labour. It is positive to see the Central Banks forecasts for new home completions rising to 35,000 new units in 2024, however, inflationary challenges and supply chain issues in some areas still persist and potentially may scupper these forecasts.

Housing and mortgage markets rebounded in 2021 having been impacted by the onset of COVID-19 in 2020 with the total value of mortgage drawdowns being €10.5 bn, the highest value recorded since 2008[1]. Government produced ambitious targets for the sector over the coming years as outlined in the 'Housing for All' Plan. Having adequate levels of financial liquidity in the marketplace is vital to help achieve these targets and ensure sufficient funding is available to meet the mortgage requirements of private households, and beyond. Looking at the private residential market, the average annual Housing for All output target for private rental and private ownership homes over the next ten years is 18,950 units. Taking a scenario where second-hand stock continues[2] to turnover approximately 47,000 private dwellings[3] and for the Housing for All to deliver annual output targets over the next decade, the likely liquidity required for this market would be around €18.35[4] bn per year. This is based on nationwide median dwelling selling prices of €250,000 for second-hand dwellings and €350,000[5] for new dwellings (mix of both housing and apartments based on current output levels).

	Estimated Output (units)	Sales Price	
Existing Dwellings			
Estimated annual stock turnover	47,000		
Average sales price per unit		€250k	
			€11.75bn
New dwellings			
Housing for All target (averaged over 10 years)	18,950		
Average sales price per unit		€350k*	
			€6.6bn
Total Liquidity required for private residential market**			c.€18.35bn

*New dwelling figure is VAT inclusive**Numbers may not add up exactly due to rounding

[1] BPFI Housing Market Monitor Q4 2021
[2] Note: It has been documented that residential property transaction levels are currently below what is considered as norm for property turnover rates, however, for the purpose of this exercise this calculation is based on current market turnover rates.
[3] In the year to December, 46,419 dwelling purchases by households at market prices were filed with Revenue. Source: CSO, Residential Property Price Index December 2021
[4] Calculation does not account for inflationary impacts on average dwelling prices over time and is based on averages
[5] Data sourced for Property Price Register based on 2021 transactions. New dwelling price is VAT inclusive

The overall residential market requires a combination of state and institutional investment, financial funding and cash within the marketplace, and a sustained mortgage market which can accommodate the increased delivery of supply required to meet demand.

Residential Delivery – Viability

Average house prices are now just over 3.3% less than what they were at the peak of the property boom in 2007.[6]

Over this period, the cost of delivering new housing product to the market has become much more expensive as documented in the SCSI's *Real Cost of New Housing* and new *Real Cost of New Apartment Delivery* reports where the cost to deliver a 3-bedroom semi-detached home in the Greater Dublin Area increased by 12% from 2016-2020 and a low-rise apartment delivery cost rose by almost 11% between 2017 and 2020. Construction costs inflation is expected to be much higher into 2022 and beyond.

SCSI has previously reported on how COVID-19 further exacerbated the gap between the supply of dwellings and demand, as demand for property continues to exceed supply. New housing supply has remained relatively stagnant over the last number of years, having been affected by pandemic related consequences including lockdown periods, supply chain disruptions and a shortage of materials and labour. This coupled with inflationary increases are causing concern within the sector for project viability in the medium term.

SCSI regularly monitors tender price inflation. The SCSI Tender Price Inflation Report[7], which tracks commercial construction project inflation (labour and materials), is showing a median increase of 7% in the first 6 months of 2021. An update of this report is due in March/April 2022. Anecdotally, chartered surveyors are reporting

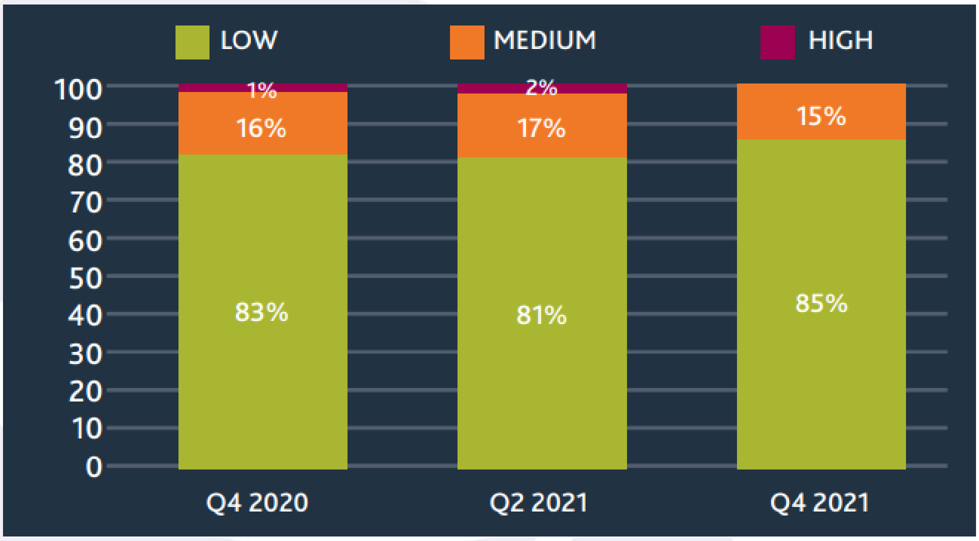
[6] CSO, Residential Property Price Index January 2022
[7] SCSI Tender Price Index Report October 2021

considerable increases in materials generally, with the largest increases in material prices relating to timber, copper, diesel, cement and concrete products. This has also been reported in other industry reports published in 2022. More recently the geopolitical context raises further uncertainties in the sector in terms of potential international supply chain disruptions and further price increases to commodities such as fuel.

SCSI has concerns that continued price pressures and lack of supply of certain materials, may have a negative effect on housing supply over the course of 2022 and into 2023, as developers may decide to delay/hold projects due to viability concerns.

As it stands, levels of stock continue to remain relatively flat for SCSI residential agency surveyors which reflects the overall low market supply that is being reported by SCSI residential agency members, commentators, and buyers alike. In surveys to members over the course of 2020-2021, over 80% of respondents have consistently stated that they have low levels of stock available on their portfolio for sale.

Table: SCSI Residential Agency Members' reporting on levels of stock available for sale



Affordability for prospective purchasers

In the context of increasing residential prices and within the current loan-to-income and loan-to-value mortgage measures framework[8], there is a cohort of potential purchasers who are effectively unable to meet the requirements to access a mortgage and purchase a property. At least 100 million low and middle-income people in the United Nations Economic Commission for Europe (UNECE) region are housing cost overburdened; they spend more than 40 per cent of their disposable income on housing.

In an SCSI study undertaken in 2020, the affordability gap (i.e., the gap between total mortgage plus deposit available from the average delivery price of a residential property) for average income earning first time buyers looking to purchase a newly developed 3-bed semi-detached house in the Greater Dublin Area was €25,000. This is based on 2020 delivery costs, as published in the SCSI's *'Real Cost of New House Delivery*' report where average delivery costs were €371k which is likely to be much more expensive now due to further increases in material and labour costs. The report highlights critical viability challenges with the supply of units to the market for individual purchasers at affordable levels.

The below table illustrates further examples of the affordability gap using several cohorts of prospective – first-time buyers, second-time buyers and both couples and individuals across several urban or commuter locations based on property prices for all dwelling types (new and second-hand stock).

[8] Loan to income measures the mortgage allowance available based on a cap of 3.5 times one's income, and loan-to-value requires an upfront deposit calculated as a percentage of the overall value of the property and based on buyer profile.

Affordability Scenarios for Prospective Purchasers

	Salary[9]	Mortgage 3.5* cap	Property Price[10]	Deposit reqd.*	Total Funding (mortgage & deposit)	Affordability (approximate)	Government incentive
Cork (County)							
First time buyer (couple)	83k	290k	344k	34k	324k	19k	Could avail of Help to Buy relief up to €30,000
First time buyer (1 person)	41k	145k	344k	34k	179k	164k	Could avail of Help to Buy relief up to €30,000
Second time buyer (couple)	83k	290k	245k	49k	339k	94k	
Wicklow (County)							
First time buyer (couple)	83k	290k	490k	49k	339k	151k	Could avail of Help to Buy relief up to €30,000
First time buyer (1 person)	41k	145k	490k	49k	194k	296k	Could avail of Help to Buy relief up to €30,000
Second time buyer (couple)	83k	290k	356k	71k	361k	6k	
Galway (County)							
First time buyer (couple)	80k	278k	345k	35k	313k	32k	Could avail of Help to Buy relief up to €30,000

[9] Salary data sourced from CSO's *Earnings analysis using administrative data sources 2020* – median annual earnings by county

[10] Property data sourced from Property Price Register 2021 transactions and calculated using median values Prices for new dwellings have been calculated to be inclusive of 13.5% VAT.

First time buyer (1 person)	40k	139k	345k	35k	174k	171k	Could avail of Help to Buy relief up to €30,000
Second time buyer (couple)	80k	278k	237k	47k	326k	89k	
Dublin (County)							
First time buyer (couple)	89k	310k	437k	44k	354k	83k	Could avail of Help to Buy relief up to €30,000
First time buyer (1 person)	44k	155k	437k	44k	199k	238k	Could avail of Help to Buy relief up to €30,000
Second time buyer (couple)	89k	310k	380k	76k	386k	6k	

** Note numbers in the above table have been rounded to the nearest thousand so figures may not add up exactly*

In three quarters of the scenarios, prospective purchasers are unable to afford average property in their location as the maximum mortgage allowance falls below the average property price. To note, these scenarios only illustrate overall median values for the counties included, there will of course be variances to these values in different areas within a county. Similarly, these examples illustrate the average incomes of earners in Ireland, there will be variances as 50% of earners' incomes fall below this average income level. Many of this cohort may be renters who may otherwise have the aim to become a purchaser but find themselves unable to save for a deposit while paying monthly rents which in the current market may exceed the level of repayment that a mortgage would require.

Housing affordability is often a challenge for groups of the population facing vulnerabilities. These include young people, senior citizens, large families with children, and people who suffer from limited access to healthcare, fuel poverty, and price inflation of essential goods and services[11]. Housing affordability remains a major challenge also for middle income earners, especially in many large cities where rents are increasing.

The current context of the property market is an important contextual framework to consider the impact of the macroprudential rules on the market and where they are impacting on purchasers. Mortgaged buyers can often be disadvantaged when competing against non-mortgaged buyers for property for reasons such as additional bidding/purchase restraints placed on mortgage buyers. The property market is not a single market, but rather a series of micro-markets and a ‘one size fits all’ approach to lending rules may not sufficiently serve the market.

Inadequate funding for vacant and derelict property

To meet the urgent demand for housing, and in line with Ireland’s sustainability agenda including controlling emissions, the country has a significant level of vacant properties which could be renovated or retrofitted for residential use. SCSI believes that a proactive approach should be taken to renovate existing vacant properties to bring a new supply of housing to the market. In our discussions with SCSI residential property surveyors, many have noted increased difficulties for purchaser's accessing a mortgage for renovating properties. From an industry perspective, SCSI has advocated to Government that all such works are guided by appropriate standards and address any existing barriers to ensure that developments can be delivered in a timely manner and to a high standard. From a lending perspective, SCSI believes that purchasers seeking to bring a vacant property back into use should be supported in doing so through the macroprudential framework or related financial tools.

Part of the challenge for purchasers buying properties for renovation is in relation to the upfront costs many face when seeking a mortgage from banks. Our members

[11] United Nations Economic Commission for Europe, Housing 2030

inform us that bank lending policy require purchasers to fund a considerable proportion of the renovation costs until such time that the property is almost complete, and the final valuation can be issued which allows for the loan-to-value computation to be finalised. Many buyers do not have the additional cashflow to fund renovation costs on top of the property purchase cost and SCSI believes that more could and should be done to support borrowers in this regard and also support government policy to renovate vacant and derelict units.

For example, if a house was inhabitable and a purchaser borrows €300k to purchase the house and will require an additional €200k to fund the renovation works, the LTV for the overall borrowing will be reduced back from say 80% to 70% or possibly lower. Borrowers are asked to provide their own financial input to carry out the renovation works and often, this is not a financially feasible option for many. The above example is a regular feature when borrowing from banks even when the final market value of the property expected when the works are complete is more than the 80% LTV. A contingency of 10% for the renovation works is also a criterion applied by banks.

In this letter, SCSI has sought to highlight activity and trends in the residential market as witnessed by our members. Ultimately, the macroprudential rules are intended to safeguard against irresponsible lending. Looking at the current lending tools, the loan-to-value ratio in Ireland (set at 90 per cent for FTB's) is close to prior industry standards and international norms, the loan-to-income ratio (set at 3.5* gross income) has been highlighted by industry and politicians as relatively strict, as house prices have risen, and rental inflation has lowered the savings capacity of households.[12] Inflation is now on the rise as the ESRI predicts inflation will increase by 8% in 2022.

Changes to Macroprudential rules (LTI)

There is a growing need for changes to the macroprudential framework as it was introduced in 2015 and much change has occurred within the housing market since its

[12] https://www.esri.ie/system/files/publications/WP686_0.pdf

introduction. Any changes to the rules, particularly the LTI, will need to be well timed to avoid any negative consequences for the market and economy generally.

Pre Covid, property price inflation was just under 1% nationally, however pent -up demand and lower levels of new housing supply since then, means that property inflation is at double digit growth currently. Had the pandemic not hit, there would have been a stronger argument to relax the rules due to stable house price movements.

The SCSI suggests that a longer-term approach is taken where the Central Bank continues to periodically review opportunities to introduce alternative lending instruments within optimal market conditions to protect both purchasers and the lending framework. Periodic overarching framework reviews facilitate a continued in-depth analysis of the measures at an interim basis, SCSI would suggest that this continues on a medium-term basis (i.e. every 3-5 years) so as not to cause undue market uncertainty.

A move from LTI to Debt Service Ratio (DSR) is potentially another option for consideration by the Central Bank, provided the timing is right. SCSI notes that alternative lending instruments such as DSR have been proposed by various stakeholders as viable alternatives to LTI which may allow increased scope for borrowers to access mortgages of higher value. The level that the macroprudential limits are set and the timing of their introduction are crucial determinants of their impact on housing values[13].

The outlook

SCSI residential agency surveyors forecast that house prices will continue to rise over the coming year. As of December 2021, residential agency surveyors anticipated that national dwelling prices would increase by a further 5% on average over the course of 2022. Low supply and robust demand were cited as some of the main factors underpinning this sentiment.

[13] Research Technical Paper: Credit conditions, macroprudential policy and house prices

Location	Anticipated increase in house prices
National	5%
Dublin	5%
Munster	5%
Leinster (excluding Dublin)	5%
Connacht/Ulster	7%

Inflation pressure on new construction will continue to exist and most likely be exacerbated with recent Geopolitical events with the war in Ukraine and this is expected to further apply viability challenges on an already challenged sector.

The SCSI Tender Price Index, due to be updated in April 2022, highlights the extent of inflation experienced by the broader construction (commercial) sector. 7% increase in tender prices during a 6-month period is what was reported in our most recent report in October 2021.

Table 1 Tender Price Inflation – 6 months

Location	1h2021
Dublin	6%
Rest of Leinster	7.8%
Munster	6.3%
Connacht/Ulster	7.8%
National Median	7%

The construction sector is making strong attempts to drive down costs by embracing modularisation and digital technology so that efficiencies in the process can be identified and improved. Through the Government's Construction Sector Group and Build Digital programme, the medium- and long-term strategy is to develop a modern construction sector to meet domestic targets and perhaps act as a export opportunity in due course. However, this will take time and until then, a greater focus on other regulatory matters such as the macroprudential rules are needed to avoid a situation whereby new residential development is reduced due to viability concerns.

While the macroprudential rules were appropriate at the time of their implementation to avoid the boom-bust property cycles of the past, as outlined in this letter, a number of factors in the intervening years have resulted in the need for the rules to be reviewed to ensure the viability and affordability of housing for stakeholders across the property market.

We thank you for taking the time to consider this letter. Please do not hesitate to contact me should you require any further information or if the SCSI can be of assistance to you as you progress with your review.

Your sincerely,

Shirley Coulter, CEO

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