



Fair Value Lending - FAQ

Regulating against a Property Bubble

What is the policy?

'Fair Value Lending' would enforce Irish Banks to be only allowed provide mortgages against a property valuation that is a sustainable multiple of average incomes in Ireland.

How would the “sustainable multiple” be calculated?

The “sustainable multiple” or 'Fair Value' would be calculated by the Central Bank of Ireland through analysing the historical average incomes in Ireland versus historical average house prices in Ireland. Through conducting this process on a yearly or quarterly basis, as well as analysing economies that have stable property markets like Germany, the Central Bank could then arrive at a Fair Value for where house prices should be as a multiple of Ireland's average incomes.

Do you have an example of how it would work in practice?

If for example, after conducting their analysis the Central Bank determine that the established figure for a Fair Value for property should be four times average incomes in Ireland, that would mean that banks in Ireland would not be allowed to lend any money above that price for a particular house.

In such a scenario, if somebody was trying to go to a bank and borrow money to buy a house with a market value of €500,000 at a time when that market price represented five times the value of average incomes in Ireland, the Fair Value of that house would be €400,000.

In other words, because the Fair Value of house prices had been established by the Central Bank of Ireland as four time's average incomes, this would mean that the market price of the house was

overvalued by €100,000 and banks would not be allowed lend against that portion of the market value.

Why should historical average incomes be linked to the price of property?

The essential ingredients of a property bubble are demand, speculation, and the belief that recent history is an irrelevant forecast of the future. Without one or all of these factors being present, the banks have no capacity to cook a bubble. Linking historical average incomes and property prices to mortgage lending maintains demand but removes the two other necessary factors.

Will this policy make it more difficult for people to get a mortgage for a house?

No. The Fair Value Lending proposal would operate in tandem with current regulations for lending already in place by the Central Bank. In the long term, it would mean that people's expectations of property price increases would be benchmarked against average incomes in Ireland rather than speculative unknowns. This will ensure that property prices grow at a sustainable rate making houses affordable for first time buyers and young families.

Why do we need more regulation for banks when people are struggling to get mortgages in the first place?

The Banks will tell you that there is huge demand for mortgage lending in Ireland right now and that they are very conservative in their lending policies. The Reform Alliance believes its proposal of 'Fair Value' lending will act as permanent stopgap measure to future recklessness.

In the same way that the EU Fiscal Treaty forced governments to permanently keep their books in order even at a time when governments were operating fiscally conservative policies, this proposal would make sure the Irish people never again have to suffer a property boom and bust cycle.

Will your proposal damage the construction sector and economic recovery?

No. Developers and property owners have a vested interest in property prices rising at an accelerated pace, but no such interest exists for the builder or tradesman employed in the sector.

Fair Value lending will create a sustainable property market with a work force that supports real genuine demand in the economy, rather than speculation. In the lifetime of someone employed in construction or a small business reliant on the sector, a property bubble is a much greater job killer than it is a creator.

Have you met with Minister for Finance or Central Bank to discuss your proposal?

We have submitted our proposal to both offices and we hope to seek a meeting with the governor of the Central Bank as well as the Chief Executives of all the mortgage lenders in Ireland to hopefully give a proper hearing to our proposal.

Is legislation required?

No. The Central Bank could initiate this regulation themselves or the Minister for Finance could force them to do so. It is open to the Oireachtas to bring in legislation to mandate the Central Bank to bring in regulations that implemented the policy proposal or legislation to impose the proposal on the banks directly.

We know the banks do not seem to like our proposal, so legislation may be necessary and if so we intend to submit a private members bill amending the Central Bank Acts.