

# EUROPEAN Forum

Mortgage Market

Autumn 2008



## Golden opportunity

With property markets in turmoil,  
is it time to introduce 'gold standards'?

### Risky business

Why embracing mortgage insurance should be part of the CRD review

### Opening doors

The initiatives helping first-time buyers onto the property ladder

# Welcome

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Welcome to the first issue of Genworth Financial's *European Forum*.

This new biannual publication is one channel through which we would like to bring you information, debate important issues and share best practice. In the previous annual *Bulletin*, we focused on trends in the UK. With this new publication, we are now able

to bring you issues from a European and a global angle, as the world finance map changes.

Recent months have seen unprecedented turbulence in the financial markets, putting additional stress on the housing market in many European countries. Against this backdrop, we examine a number of key issues facing the industry.

Firstly, in our feature on page 3, we explore how best to reinvigorate the markets for securitising residential mortgages. Is a gold standard the way forward, and could it work as a pan-European approach?

We also turn our attention to the proposed amendments to the Capital Requirements Directive (CRD). As you may be aware, Genworth has submitted recommendations to the Joint Forum – the banking, securities and insurance supervisors group – ahead of the CRD review, and our feature on page 8 focuses on the advantages we see of mortgage insurance over other forms of credit risk transfer.

In each issue of the *European Forum* we will be providing a European macroeconomic overview, together with local housing market statistics. We will also be featuring a snapshot of one facet of the European housing market – and for our launch issue we are turning the spotlight on affordable housing and how government initiatives can support first-time buyers. You'll find the report on page 12.

Finally, to find out more about Genworth Financial activities in the wider arena, turn to our round-up on page 18.

I hope you find it an interesting and stimulating read.

**Tammy Richardson**

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# Rescue mission

Amid talk of 'gold standards' for the mortgage industry, maybe it is time to go back to the basics – transparent underwriting and responsible lending practices. **Nick Kirby** reports



Property markets in a large proportion of the developed world are suffering a serious malaise. Not only have we witnessed falling residential property prices and high levels of repossessions, but banks, mortgage companies and developers that enjoyed the boom times are also now suffering – in some cases, terminally.

It is going to take a concerted effort to rally an industry that has endured such a torrid time, albeit arguably partly self-inflicted. With leading US companies going to the wall – not least some of the biggest banks – the government had to step in with the Emergency Stabilization Act. And in the UK, after the Northern Rock debacle, history seemed to be repeating itself. In mid-September, with the prospect of a run on HBOS, the country's largest mortgage lender, the government supported a rescue package in the form of a takeover by Lloyds TSB, as well as the part-nationalisation of Bradford & Bingley.

By mid-October, the UK government announced a rescue package which resulted in the part-nationalisation of several banks.

It was, perhaps, inevitable that there would be other major UK casualties. As Chancellor of the Exchequer, Alistair Darling, told the BBC: "We were onto their [HBOS's] problem for several weeks. It didn't just suddenly happen."

Andrew Cormack, European Commercial Director at Genworth Financial, explains: "Since the turn of the millennium, mortgage-backed securities have played an integral part in the financing of the UK mortgage industry. When the global markets went into turmoil and flaws became evident in the property markets, this funding stream all but dried up as investors became very concerned about the quality of the underwriting of the loans they were invested in."

Towards the end of 2007 and throughout the early parts of 2008, we began to witness a

knock-on effect. Unable to raise funds through securitisation and concerned about borrowers' ability to repay, mortgage lenders began to withdraw the higher LTV mortgage offerings. Falling property values and difficulties in re-financing when their 'teaser rate' came to an end – meaning that many had to revert to the standard variable rate (SVR), which could equate to a considerably higher monthly outlay – put further pressure on borrowers.

This pressure is evident from figures from the Council of Mortgage Lenders (CML), which show that there were 18,900 repossessions in the six months to June 2008, up from 12,800 in the same period the previous year.

### Meeting the challenges

The UK government has acknowledged the need to rectify the current parlous situation. In its *Housing Finance Review*, published alongside the Budget in March 2008, HM Treasury identified two key challenges for the UK mortgage market: the transparency and liquidity of mortgage-backed securities markets; and accessibility of long-term fixed rate mortgages. And in April of this year, Alistair Darling instructed Sir James Crosby, Deputy Chairman of the Financial Services Authority and former CEO of HBOS, to undertake a review into initiatives that might improve the functioning of secondary and primary markets in UK mortgage-backed securities.

Crosby's Interim Report, released in July 2008, indicated the need not only for possible legislation, but also industry- and market-led initiatives, including the possibility of a 'gold standard' to be applied to mortgage-backed securities. Genworth was pleased to be able to contribute to this consultation process.

As Tammy Richardson, Managing Director of UK Mortgage Insurance, Genworth

Financial, explains: "We firmly believe that one key contributing factor to the problems we have seen is the questionable quality of the underwriting involved in the mortgage market at the point of origination. There has been a definite lack of prudence and consistency."

Cormack adds: "Banks have been driven by competition. In order to attract new customers and have existing customers refinance, there has been an element of lending that has not been particularly prudent. There has been pressure to make decisions quickly, so there has been speed in the key underwriting and, perhaps, short cuts have been taken. I'm not suggesting this is reckless lending, but it is lending that might not have happened with more diligence."

This is not systemic, but as banks are forced to retain their risk on their balance sheets, not knowing 'who' or 'how much' is affecting market perception – and ultimately impacting stock prices in the banking sector. Externally acquired credit risk mitigants in the form of MI could potentially reduce the suspicion.

### Setting the standard

If there is to be a 'gold standard' for mortgage lending and therefore, by default, one that links through to residential mortgage-backed securities, a number of factors need to be considered. Traditional mortgage underwriting was based heavily on the value of the collateral and the assumption that it could not go down. HLTV mortgage lending adds steps that are more often associated with unsecured lending procedures: the ability to repay and the willingness to repay.

Richardson explains: "You need to look carefully at the borrower, the type of loan and its term and the collateral, namely the property on which it is being taken out. There is a misconception that a high LTV loan is a

sub-prime loan – this is not necessarily true. For example, take a first-time buyer, who is earning a good salary with a stable job and sound credit history and can easily afford to make the repayments on a 90% mortgage, but who

doesn't have the deposit. Then take someone who has low income and other debts, but is just refinancing and has 20 to 25% equity. Would you turn down the former because he or she is asking for a 95% LTV?"

## The view from Germany

By **David Pipe, Commercial Leader, Developing Markets**

So far, the German market has been largely unaffected by the credit crunch and isn't experiencing the kind of volatility being witnessed in the UK and Spanish markets. As a result, the German market continues to perform well, and house prices have remained relatively stable. The number of repossessions has stayed constant, and there remains the same availability of mortgage credit from German lenders.

Loans in German RMBS pools and Covered Bond pools are performing better than counterparts in both the UK and Spain. Therefore, there is not the same lack of confidence that is being seen in other markets. That said, the German market is still affected by the generally 'dry' market conditions.

Furthermore, there has not been a run up in property prices over the last few years, so there is no bubble to burst. What's more, there is virtually no sub-prime market in Germany – in fact it is practically a 100% prime market. There are some banks that have suffered, but this has only been because they have invested in securities backed by sub-prime mortgages in the United States, or because in some instances they have

experienced funding problems.

One worry among homeowners is a potential increase in interest rates. Although most mortgages in Germany are fixed-rate products – generally fixed for the first 10 years of the period of the loan, with the availability of up to 30 years fixed – there is concern about the rates that will be available when the time comes to refinance.

Realistically, I do not believe that the establishment of a 'gold standard' is vital to Germany, as it is not experiencing the level of volatility occurring elsewhere. However, when we compare Germany with global best-practice in the markets we serve around the world, two areas that stand out as needing improvement are valuations and loss mitigation.

When compared with a global best-practice peer group, German banks tend not to conduct as thorough valuations as are the norm in many countries – for example, most properties are not inspected as part of the valuation process. This is a symptom of an under-developed mortgage market, where, in the absence of robust valuations, LTVs of over 70% are rare. As a consequence, access to earlier home ownership is restricted.

Reducing LTV limits on mortgages to a maximum of 70-80% and increasing interest rates has only served to stall the mortgage market more. It is on prudent higher LTV mortgages that mortgage insurance (MI) comes into play, and both Richardson and Cormack agree that it should play an integral part in

the formation of any future standards for the reinvigoration of the mortgage market.

As Cormack points out: "This goes to what we would call responsible lending. We only need look at Canada to see how consistency of approach and proper underwriting can help support the market. In Canada, there is a

## The view from Spain

By **Antonio Carballo**, Managing Director, Spain and Portugal

In the last 12 months, the Spanish property market has been experiencing a correction following a long period of growth. It is difficult to say how Spain compares to the UK, due to the differences in general regulatory behaviour and in mortgage-related regulation.

So, while asset price depreciation has been stronger in the UK so far, we would expect prices in the Spanish market to drop further and for a longer period. There are no significant repossessions as yet, but we expect those to gradually increase in 2009. One thing is for certain: things are likely to get worse before they get better.

There are general concerns in the property market. Homeowners are worried about interest rate levels and unemployment, while banks and mortgage providers are concerned about the availability of funding, capital and the increase of overall delinquencies. Furthermore, the massive supply of housing stock made price decreases inevitable. However, the upside for first time buyers will not be felt unless there is access to credit.

Investors need to have their confidence

restored in the market as far as securitisation of loans is concerned. There is a lack of trust, which is why there is no market today. The real question is how to achieve that?

MI has an important role to play in the rejuvenation of the property market in Spain. It will help both mitigate capital, which is positive for lenders, and improve access to homeownership, which is positive for consumers. The second pair of eyes MI provides to mortgage lending will, if widely used, ensure a prudent and sustainable growth in the housing market. That is good for the health of our economy and for the well-being of our population. Spanish banks have generally taken a prudent stance to retail mortgage lending, yet the performance of more recent 'vintages' will be a test for many of them. Moreover, the extensive acceptance of personal guarantees for HLTV lending is more pronounced in Spain than any other market in Europe. When these less-formalised instruments are put to the test by systemic stress, significant problems through ineffective protection can be expected.

statutory requirement for MI on all loans of 80% LTV or more. The risk is transferred from the bank to the insurer and it means there is a second pair of eyes on the eligibility of the applicant and loan quality. Investors looking at RMBS can see that this diligence has been undertaken."

Indeed, the proof of the pudding is there to see. The mortgage market in Canada has not witnessed the traumas suffered by both the US and UK markets. Both Richardson and Cormack believe that having a maximum LTV of 95% but applying MI at 80% and above would provide a solid working model in the UK.

#### Reality check

While the government, the regulatory bodies and the industry work on proposals to reinvigorate an ailing market, things in the UK may get worse before they get better.

"Tweaking stamp duty levels, or introducing facilities to allow the swapping of mortgage securities for Treasury Bills, are short-term measures," says Cormack. "We are promoting policy that looks at the longer-term stability of the housing funding market. International precedence shows that government endorsement of prudent underwriting criteria and the use of MI have a major role to play in realising this goal.

"Today, there is a large amount of refinancing to come in the UK property market. As the introductory mortgage rate comes to an end on many mortgages and people have to convert to the SVR, there is going to be payment shock. This is why you simply can't abandon high LTV mortgages. People who bought in at 95% – or sometimes even more – are going to get caught out as a result. You have to move beyond a basic affordability test by looking at employment stability, proof of



income, exhaustive credit history and then back that up with MI."

Along with talk of 'gold standards', there has been discussion about making such standards pan-European. But is this practical? As Cormack explains: "It will be very tough, as there are different financing tools in different markets, so things will need to be done more on a national basis. What's more, European countries have been affected to differing degrees. However, I do see a role for Brussels advocating best practice lending criteria to guide EU countries."

The other challenge is to get banks to adhere to a standard code of conduct. When the property and mortgage markets are back in good health, what is to stop the banks overheating the market by dropping standards and introducing overly competitive rates?

Cormack says: "You need to have standards. Investors are not comfortable with the asset pools out there; they are not sure of the loan quality and are not willing to take risks. In the future, those investors will be able to look at which organisations adhere to a set of agreed standards, and make informed decisions." 🌟

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NICK KIRBY edits several financial publications, including *Smart Investor* and *Skandia* magazine.

# Mitigating credit risk

A package of amendments to the Capital Requirements Directive (CRD) has been suggested by the European Commission, designed to limit exposure to credit risk and tighten up industry regulation. **Jo Atkin** reports, with contributions from Daniel Garcia, Genworth Financial

Genworth Financial has taken the opportunity to submit recommendations to the Basel II Joint Forum, as part of the CRD review. The changes being proposed to the CRD are in part a response from the European Commission to the credit market turmoil and the corresponding roadmap of actions set out by the EU's finance ministers in October 2007, while other changes reflect work that had already been underway within the Commission for some time. The potential changes to the CRD address a raft of issues, including limiting potential large exposures to a percentage of the own funds of a bank and the lack of regulation of hybrid capital instruments and their divergent treatment across countries.

## Genworth's submission focused on three particular areas:

- The importance of credit risk transfer (CRT), particularly the advantages of using a third party,

such as a mortgage insurer.

- The need for more responsible lending practices – lenders should have more appropriate levels of capital for high LTV residential mortgage loans.
- Finally, Genworth also commented on changes proposed by the Commission to the CRD.

This article discusses the first point in the submission to the Commission, and looks at the benefits of mortgage insurance (MI) and how it is distinguished from other credit risk mitigants.

## Assessing credit risk

One of the main aims of Basel II is to make capital more risk sensitive, therefore banks must be able to judge risks. As far as mortgages go, Basel II has introduced requirements such as regular monitoring of the value of the property and recognition – for credit risk mitigation purposes – of instruments such as MI.



There are two ways of assessing capital. The first, the standardised approach (RSA), is an ad hoc method where risk weightings are set depending on the type of asset the bank has invested in. For mortgage loans, there are LTV thresholds; these vary between countries and determine the risk weighting parameters, and, therefore, capital requirements.

The second, internal rating based approach (IRB), is a method that depends on internal lenders' estimations of risk variables as probability of default (PD) and loss given default (LGD). Here capital will be more risk sensitive than the RSA method.

Property value will have a big impact in the IRB method. Gary Miller, Director of International Legal and Regulatory Affairs at Genworth, explains: "Genworth has focused on making sure the banking regulators, including those in countries not familiar with MI, understand its significance and importance as credit risk mitigant. Genworth operates in

European countries where the CRD has been already transposed and therefore regulators are aware of the different ways of mitigating credit risk including MI. Our experience allows us to share best practices from different territories.

"We are advocating that the regulators give MI as full recognition as possible, so the banking system can get the benefit of MI for credit risk management purposes. In addition, the housing finance system can benefit from using MI and more broadly serve that underserved sector of the housing-ready population."

#### **Other types of credit risk transfer (CRT)**

Some of the other forms of CRT, such as credit derivatives, are complex. For example, Miller says that credit default swaps (CDS) are "entirely legitimate instruments and the market has grown rapidly. They are complex but have not been tested in a stress environment – until now." Credit derivatives tend to be viewed for trading and are shorter term. MI takes more of an investor approach by investing in the lenders' risk longer term. The other example of a CRT vehicle would be financial guarantors, which typically issue guarantees on a security, not on the mortgage itself.

#### **The strengths of MI**

A key aspect of MI is that it is very highly capitalised with a strong capital base, well above investment grade. "As a highly-rated mortgage insurer we take a big chunk of risk," says Miller. "When housing systems go under stress you need a strong capital base to pay your claims and come out at the other end."

Mortgage insurers are comprehensively regulated and file quarterly financial statements showing their risk profile. Risk is spread through reinsurance and other types of risk-sharing agreements.



### Rigorous underwriting

A number of countries are experiencing significant mortgage stress, with rises in arrears and possessions. For example, in the UK, repossessions were up 48% in the first half of this year compared with the same period in 2007, according to the Council of Mortgage Lenders. Miller says: "We have a proven claims mechanism. Mortgage insurers have paid billions in claims with a high level of reliability."

Genworth has a rigorous underwriting process and expects to pay losses as it is in a first loss position. It has a strong incentive to assess risk accurately and looks closely at the underwriting criteria on the loans it agrees to insure. In effect, it acts like a second pair of eyes and is not afraid to decline to underwrite loans that do not meet lending criteria.

### Accessibility issues

In recent years, a number of factors have led to a boost in the mortgage market, including

low interest rates, a growing pool of buyers, increase of income (high GDP growth rates), and house price appreciation. These factors have resulted in an increase in the average LTV with a perception that the loan was well backed (asset/property prices increasing).

However, the last 6-12 months have seen prices starting to fall, most notably in the UK, Spain and Ireland. This trend, combined with rising interest rates and the tightening of lending criteria across Europe, is making accessibility even more difficult.

As banks assess riskier lines of lending they either discourage, prohibit or limit lending, or if they are willing to accept the risk they are required to hold significantly more capital. One consequence is that banks ration credit and as a result, while people who have better credit profiles can get a housing loan on good terms, first-time homebuyers often can't.

Miller explains: "There are those who don't have the level of down payment required by the bank, but do have a job, good career prospects and a decent current debt-to-income. However, the banking system tends not to serve them well because high LTV loans are risky."

In many countries, the historic cut-off point for loans considered high LTV is around 70% to 80%, and Miller points out that anything above that makes it "hard, impossible or significantly more expensive to get lending". At this threshold a borrower needs to find a down payment of 20% to 30% plus associated expenses (legal fees, taxes, etc) and to achieve this a borrowing couple would need to save for at least six to eight years.

### Reconciling conflicting goals


"Many people have had to go outside the mainstream banking system or get a guarantee from relatives or even take out a personal

loan with a higher interest rate," he says. "By having a financial system that rations credit in that way and avoids the riskier assets, you are discouraging it from serving certain broader economic, policy and social goals, such as getting people into sound housing. But from the political perspective, governments want people to have more access to homeownership."

This creates tension between those two conflicting goals, says Miller. "On the one hand you have housing advocates and politicians who want the banks to serve this segment and make loans on favourable terms, while on the other hand regulators see that as exposing the banking system to more risk."

MI is a widely used mechanism to reconcile those conflicts. Miller explains: "It does that by encouraging the banking system to safely and prudently serve a sector that the regulators recognise as being riskier and therefore require additional capital as a buffer. If the banks have the backing of a strongly capitalised insurance, such as MI, the regulators are more comfortable with that."

"The political and housing advocacy side see it as achieving two goals. Firstly, getting the private sector financial system to serve the housing need rather than have to do it through expensive social housing programmes. Secondly, because MI performs a standard insurance function of diversifying loss across large groups, it lowers the cost of carrying that risk for the system at large."

In summary, MI allows lenders to take more risk, reducing credit rationing, easing and improving access to homeownership, and reducing uncertainties over the business cycle. 

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JO ATKIN is the editor of the specialist publication, *Mortgage Finance Gazette*.

## Success stories

Compared with the neighbouring United States, Canada has seen virtually no rise in claims and delinquencies. MI is compulsory in the Canadian banking system on all loans over 80% LTV and there are two mortgage insurers: Genworth and the Canada Housing Mortgage Corporation, which is a government agency.

Gary Miller explains: "The system works well in Canada to encourage the banks to service homebuyers who only have a small down payment. It also serves well to create innovative new products, including 40-year loans and products for professionals, such as doctors coming out of medical school with debts but good prospects. Also, the compulsory element has made it easier for mortgage insurers to draw a line on products that are too risky. It's kept the banks out of the sub-prime type of asset."

MI has been extremely successful in a number of countries, including the US, Canada, Australia, New Zealand, Germany, Italy, Spain, UK, Ireland, Mexico and the Nordic countries. These countries are comfortable and familiar with MI, and recognise it as a reliable credit risk mitigant. Other countries are keen on adopting MI. These include India, Brazil and Korea.

Miller also points out that the World Bank, in consulting with developing countries, is an advocate of incorporating MI into housing finance systems.

# Opening the door for buyers

The role of mortgage insurance in extending the reach of government-backed affordable housing schemes

The current slowdown in the European housing market is proving a challenging climate for first-time buyers and low-income workers hoping to get a foothold on the property ladder. The increased cost of funding as a result of the global credit crisis has had the effect of increasing interest rates to borrowers irrespective of European Central Bank (ECB) rates which rose from 2% to 3.25% in the period from December 2005 to November 2008.

In the last decade, affordability pressures on first-time buyers were solved with increased LTVs, lengthened loan periods and the introduction of innovative products that were inherently more risky. However, the increasing severity of the credit crunch over the past 12 months has seen lenders revert back to lower LTVs and tighten credit criteria substantially.

As a consequence, many first-time buyers and low-paid workers are being forced to engage in unsecured borrowing, seek financial assistance from parents and other family members, or even club together with friends to fund their deposit. This increases the vulnerability of groups of buyers, the lending institutions and the general economy.

## Government initiatives

One solution being considered by an increasing number of countries – both European and worldwide – is the introduction of affordable housing schemes. These government/private partnerships can offer an innovative option for borrowers for whom a mortgage is out of reach.

Affordable housing and shared-ownership options have been in existence in Ireland for over a decade, as part of the government's commitment to home ownership. One of three local authority initiatives, the Affordable Housing Scheme was introduced in 1999. This involves the provision of new houses on land provided or acquired by the local authority in or near centres where increasing house prices have created an affordability gap. These homes are offered for sale to eligible purchasers at a significant discount from the market value of comparable houses in the area – approximately 10-40%.

Over the past 18 months, Ireland has seen a marked decline in house prices and a slump in construction activity. Notwithstanding the recent price decline, inflation over the preceding decade, coupled with the increase in European Central Bank (ECB) base rates, has put first-time buyers under significant



pressure. According to the latest data from the Irish Central Bank, between December 2005 and August 2008, Irish first-time buyers saw average mortgage rates rise from 3.55% to 5.80%. While Ireland has experienced a significant economic downturn of late, the Irish government is nonetheless committed to providing affordable housing. Indeed, it is expected that new proposals will be announced in the near future to help low-income and first-time buyers become homeowners.

Ireland is not alone in its support for this section of society. In the UK, there are a number of products available for first-time buyers that involve either shared ownership or shared equity from local housing associations. And the Spanish government has recently announced plans to ease the income requirements for its social housing, in an attempt to reactivate the stricken Spanish property market.

### Conclusion

By using mortgage insurance (MI) to mitigate risk, lenders are more open to providing high LTV (loan-to-value) mortgages to borrowers for affordable housing. In this way it also assists key public sector workers to enter the housing market. Genworth is providing mortgage insurance to a number of lenders under current affordable housing schemes.

In addition, Genworth believes that with further support from governments, credit risk mitigation products such as MI would encourage far greater participation in private sector affordable housing schemes in European markets, freeing up government funds. Also, MI has an important role to play in mitigating the risk governments suffer in market downturns, which would impact on the ability of the scheme to continue to self-fund.☀

# Macroeconomic overview

A summary of key economic indicators across the European Union and the Eurozone

In light of the grave problems in the financial sector, and very tight credit conditions, economic activity will remain under serious pressure. GDP growth looks set to more than halve to 1.1% in 2008, down from 2.6% in 2007.

Slowing economic activity, fragile consumer spending and intensifying competition points to CPI growth falling after Q3. Added to this, consumer and business confidence are approaching a combined seven-year low; this is undermining prospects for investment, employment and consumer spending. The current weakening of the labour market is expected to become more marked and indeed more widespread.

Lending growth rates, too, are down. The reasons for this are two-fold: caution on the part of consumers, and banks restricting volumes due to liquidity restraints. The crisis in the financial sector has resulted in a number of banks being sold or restructured; others have sought additional capital.

Lending for consumption interest rates have remained broadly unchanged, while the rise in rates for loans with initial rate fixation of less than one year has been offset by other maturities.

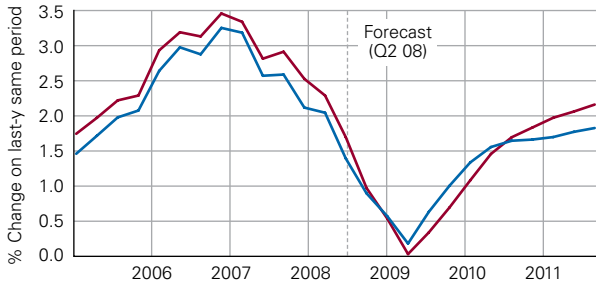
## The Eurozone

15 European Union member states currently use the single European currency: Austria, Belgium, Cyprus, Germany, Finland, France, Greece, Republic of Ireland, Italy, Luxembourg, Malta, The Netherlands, Portugal, Slovenia and Spain.

## Non-participating EU member states:

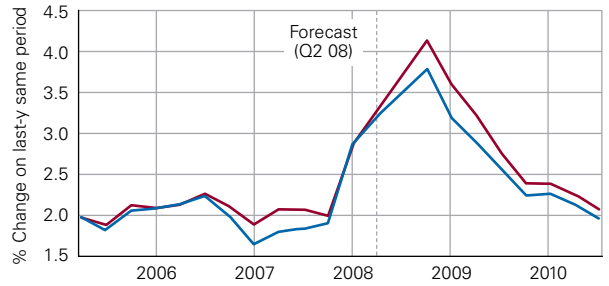
Bulgaria, Czech Republic, Denmark, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Sweden and the United Kingdom.

### GDP Growth Rate



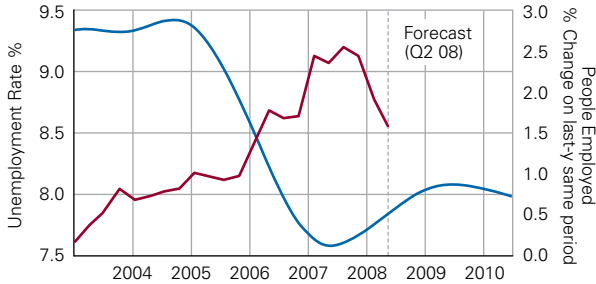
— Eurozone  
— European Union – 27  
Source: Global Insight (@ 11/11/2008)

### CPI Growth Rate



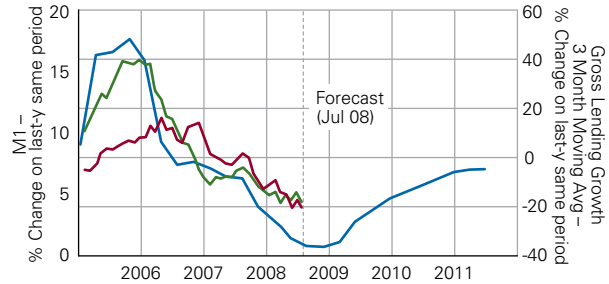
— Eurozone  
— European Union – 27  
Source: Global Insight (@ 08/10/2008)

### Unemployment



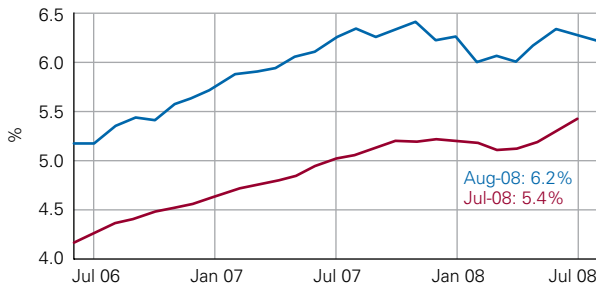
— Eurozone, Unemployment Rate  
— Eurozone, People Employed (R)  
Source: Global Insight (@ 08/10/2008)

### Money Supply & Lending



— M1 Monthly Supply  
— Gross Lending for Consumption (R)  
— Gross Lending for Home Purchase (R)  
Sources: European Central Bank, Global Insight (@ 08/10/2008)

### New Business Interest Rates Home Purchase Lending



— UK, Mortgage Rate Tracker  
— Eurozone, IR Lending for Home Purchase  
Sources: European Central Bank, Bank of England

### New Business Interest Rates Lending for Consumption



— Eurozone, IR Gross Lending for Consumption  
— UK, IR Unsecured Lending 10K  
Sources: European Central Bank, Bank of England

Data supported by Global Insight unless stated otherwise.

# Local snapshot

A closer look at key macroeconomic indicators and UK housing market statistics

## The bigger picture

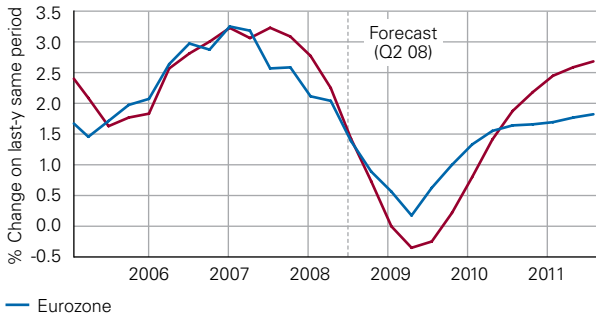
The UK economy was headed for recession even before the global financial crisis deepened. Consumer spending has been hit hard by low growth in disposable income, high inflation, tight lending practices, heightened debt levels, a sharply declining housing market and lower equity prices.

It appears that inflation may well now have peaked, and it should retreat markedly from late 2008 in the face of extended weak economic activity. It is anticipated that there will be a significant uptrend in unemployment in 2008 and it will continue to rise in 2009 as an almost certain recession is followed by only very gradual recovery. Consumer confidence is below the long-term average, suggesting growth in retail sales is expected to remain flat.

## Housing and lending

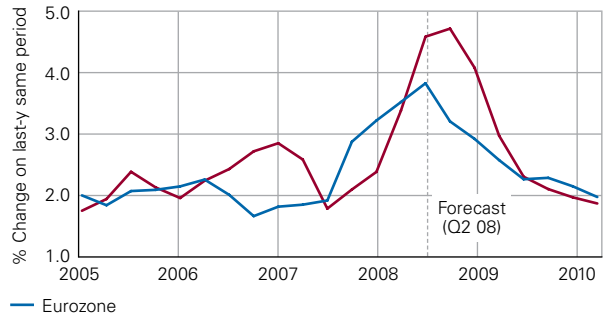
The weakness in the housing market has affected consumer spending. Consumer confidence is reaching new lows, and home sales are at a three-decade low. A drop in mortgage lending has come amid a wider shake-out in the sector's lending capacity.

### GDP Growth Rate



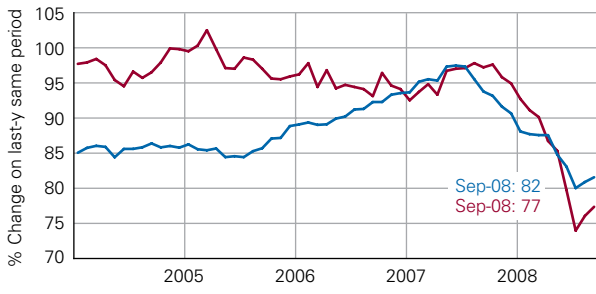
Source: Global Insight (@ 11/11/2008)

### CPI Growth Rate



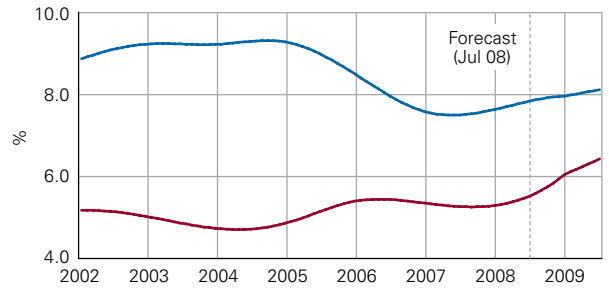
Source: Global Insight (@ 08/10/2008)

### Consumer Confidence



Source: Global Insight (@ 08/10/2008)

### Unemployment



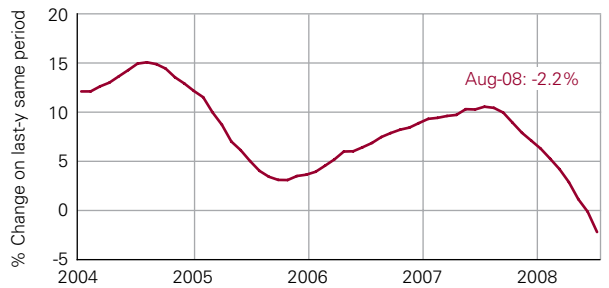
Source: Global Insight (@ 08/10/2008)

### New Lending Flow



Source: Bank of England, CML

### HPI



Source: Financial Times HPI

# Round-up



## Putts for charity

Throughout 2008, Genworth has been using its involvement with the European golf tour to raise money for a number of charities. With the support of leading tour players, including Lee Westwood, Padraig Harrington, Thomas Levet, Robert Karlsson and Ross Fisher, Genworth has been able to raise in excess of €175,000 for the Rainbow Trust, Save the Children and Aldeas Infantiles SOS.

November marked the close of this year's sponsorship at the Volvo Masters in Valderrama, Spain. The event followed Genworth's backing of the BMW PGA Championship (UK) in May and the SAS Masters (Sweden) in August.

### **Tracking financial vulnerability**

Genworth Financial has launched the first ever Financial Vulnerability Index. The Index aims to provide valuable insights to policy-makers and help develop common solutions to some of the issues faced by consumers today. Calculated using comparative data from 10 European countries, it was developed with the European Credit Research Institute (ECRI) and the Personal Finance Research Centre (PFRC) at Bristol University.

The Index was presented on 2 October at the Italian Insurance Association in Rome. Daniela Vandone, who co-ordinated the research for Italy, introduced the Index to an audience of CEOs and GMs of leading insurance companies and consumer associations.

### **New leader for Spain and Portugal**

Genworth Financial is delighted to welcome Antonio Carballo as Managing Director for mortgage insurance in Spain and Portugal. Bringing over 18 years' experience with him, Carballo's previous role was as Managing Director, Co-Head of European Banking, at Moody's Investors Service, prior to which he worked in UK and US banks. His focus at Genworth will be on driving sustainable growth.

### **Milan conference**

In conjunction with Italy's leading financial newspaper, *Il Sole 24 ORE*, Genworth recently sponsored and hosted a conference, 'Retail Mortgages and the Darwinian Selection 2008', at their Milan headquarters. The event featured a range of industry speakers including our own Valeria Picconi, Managing Director for MI Italy, who shared key findings from Genworth's recent research into the Italian first-time buyer market. Notably, that there are three segments, totalling 2.3 million potential first time buyers in the next five years. For more information, please contact [valeria.picconi@genworth.com](mailto:valeria.picconi@genworth.com)

# In perspective



As the credit crunch has unfolded it has exposed serious weaknesses in the global financial system and regulatory framework. The consequences have been dire: unprecedented levels of individual and corporate debt; a lack of liquidity in the wholesale funding markets and the collapse, takeover or government bail-out of world famous financial institutions. Against this turbulent backdrop, our first *European Forum* highlights a number of important market issues:

- Credit risk transfer – in the light of the proposed amendments to the Capital Requirement Directive, we believe that the highly optimistic view over the risk embedded in retail mortgages, based on very positive recent historical experience, may change. The right risk weighting should emerge, together with the enhanced value provided by strong, standard mitigants provided by regulated entities.
- The lack of transparency and quality of underwriting in mortgage-backed securities markets – what standards have been used, who else has ensured that those standards were complied with, and who puts its balance sheet behind it to guarantee that is the case? We advocate the definition of golden standards and the need for enhancements for HLTV mortgages to achieve them.
- The benefits of a more responsible approach to lending – in stark contrast to the US, UK and Spanish markets, the Canadian market, where mortgage insurance is a statutory requirement on all loans exceeding 80% LTV, has remained stable. Genworth continues to believe that universal MI is the way forward, limiting portfolio and systemic risk, and delivering broad benefits to mortgage lenders, borrowers and the overall economy.

In the wake of this market turmoil, the need for responsible lending will remain, and as young people continue to aspire to own their first home, tested, prudent instruments such as MI will play an even bigger role.

A handwritten signature in black ink, appearing to read 'Angel Mas', written over a thin horizontal line.

**Angel Mas**

[President and CEO, Mortgage Insurance Europe, Genworth Financial](#)

We very much value your feedback and would like to hear your views on the articles in this issue. If you have any comments, or if there are any particular topics you'd like us to address in future issues, please go to:  
[genworth.co.uk/feedback/miforum.pdf](http://genworth.co.uk/feedback/miforum.pdf)

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