



BELGIAN PANDBRIEVEN

Presentation of the Legal Framework

October 2012

Introduction & Framework Description

- A regulatory framework to allow covered bonds issuance by Belgian credit institutions has been established in 2012:
 - Covered Bonds Law, amending the Credit Institutions Supervision Law of 1993
 - Mobilisation Law
- This new legal framework is inspired by the German *Pfandbrief* Act
- Furthermore, following Royal Decrees/regulations are being processed:
 - Royal Decrees
 - on the issuance of covered bonds by Belgian credit institutions: approval by the King awaited
 - a specific Royal Decree on the role of the Cover pool administrator: drafting started
 - Regulations:
 - On the issuance of covered bonds (further eligibility criteria, valuation of cover assets, etc)
 - On the role of the Cover pool monitor

■ Main Characteristics of Belgian Pandbrieven

- **On-balance sheet structure:** the pandbrieven are issued directly by the licensed credit institution. No SPV.
- **Dual recourse:** the pandbrieven holders have recourse against both:
 - The relevant special estate
 - The general estate
- **Bankruptcy remoteness:** inclusion in the special estate has the same effect as true sale in case of insolvency proceedings:
 - Proceedings are limited to the general estate; the special estate(s) is not part of the bankruptcy estate
 - Proceedings do not cause the acceleration of the Belgian pandbrieven
- The pandbrieven issuer must maintain a **Cover Assets Register** to delimit the special estate

■ Main Characteristics of Belgian Pandbrieven

■ Additional **safeguard mechanisms** against:

■ **Commingling** risk:

- Collections received from the Cover assets are by law part of the special estate
- Such collections held by the issuer for the account of the special estate are moreover protected via the 'revindication' right: the ownership rights of the special estate as regards cash that cannot be identified in the general estate will be transferred to unencumbered assets in the general estate.
- After issuer bankruptcy: collections received from Cover assets are excluded from the general estate

■ **Set-off and claw-back** risk:

- Cover pool assets are protected against set-off and claw-back rules thanks to the provisions of the Mobilisation Law enacted at the same time as the Cover Bonds Law
 - Legal and contractual set-off prohibited after transfer (including registration in the cover assets register) of receivables
 - Claw-back rules limited to fraud

Pandbrieven Issuer Supervision

- A Belgian credit institution that wants to issue pandbrieven requires dual authorisation from the **NBB**:
 - A **general authorisation** as pandbrieven issuer. The credit institution must prove it has the organisational capacity (risk framework, IT systems, audit...) to issue pandbrieven but it must also provide information on its financial position, strategy, etc.
 - A **specific authorisation** for a particular pandbrieven issue or pandbrieven programme. The credit institution must provide information on the impact of the issuance on its liquidity position, the quality of cover assets and prove that the programme/issue complies with the legal requirements.
 - Before the NBB decides on the licenses, the NBB requires a report from:
 - The statutory auditor on the organisational capacity of the issuer
 - The cover pool monitor on the compliance of the program with legal/regulatory requirements
- The **NBB** will establish a list of:
 - Credit institutions authorised to issue pandbrieven
 - Authorised programmes/issues per licensed credit institution
- The **statutory auditor** of the issuer is required to report to the NBB:
 - Before issuance, give an opinion on the organisational capacity of the issuer to issue pandbrieven
 - After issuance, update its opinion on the organisational capacity of the issuer regularly

Pandbrieven Issuer Supervision

■ The **Cover pool monitor**

- Is appointed by the issuer...
 - ... subject to prior approval from the NBB
 - Can not be the statutory auditor of the issuer
 - Main responsibilities BEFORE issuance:
 - Takes the necessary steps to ensure that the credit institution that will issue pandbrieven meets the legal and regulatory requirements
 - Carries out other tasks and verifications that the NBB may request
 - Reports its findings to the NBB
 - Main responsibilities AFTER issuance:
 - Verifies, at least once a year, that the issuer complies with the legal and regulatory requirements (same verification as the one before issuance) and reports its findings to the NBB
 - Verifies at least once a month that the:
 - Cover & Liquidity tests (see slide 8) are met
 - Verifies at least once a month that the requirements in relation to the Register (see slide 10) are met
- => Exception reporting to the NBB and issuing credit institution

■ Special Estate - Composition

- Minimum 85% of the value of the Cover pool must be composed exclusively of one of the three following types of assets:
 - Residential mortgage loans (or senior RMBS)
 - Commercial mortgage loans (or senior CMBS)
 - Public sector loans (or senior public sector ABS)
- In addition, the Cover pool may be composed of:
 - Assets from another category above
 - Receivables on credit institutions
 - Hedging instruments

■ Special Estate – Cover & Liquidity Tests

1 85% test:

- Minimum 85% of the value of the Cover pool assets must be represented by one of the 3 categories (see previous slide)

2 105% test:

- The value of Cover assets must represent at least 105% of the nominal amount of the pandbrieven which are outstanding

3 Amortization test:

- The sum of revenues stemming from the Cover assets must be equal to or greater than the amount of interest, principal and costs related to the outstanding pandbrieven and their management

4 Liquidity test:

- The cover assets must generate sufficient liquidity or contain sufficient liquid assets to meet all unconditional payments over a 6 month horizon

5 Additional stress tests of interest rate and currency hedges

The issuer, its auditor and the cover pool monitor must regularly report to the NBB on compliance with the regulations and whether the above tests have been met

■ Special Estate – Valuation of Cover Assets

- Residential & Commercial Mortgages:
 - The lower of:
 - The outstanding loan amount
 - 80% (Res) / 60% (Com) of the sales value of the real estate
 - The value of the mortgage
 - Mortgage mandates may be taken into account for residential mortgages loans if a mortgage registration has been taken for of at least 60% of the total value
- Public exposure:
 - Equal to book value (nominal amount outstanding), except when the counterparties are not part of the EU in which case the value will be zero. There is however an exception to this zero valuation rule for non-EU counterparty exposure:
 - a) in case the non-EU counterparties qualify for credit quality step 1, or
 - b) in case the non-EU counterparties qualify for credit quality step 2 and do not exceed 20% of the nominal amount of Belgian pandbrieven issued

■ Special Estate – Valuation of Cover Assets

- Exposure to credit institutions:
 - Book value for 105% test only if
 - Counterparty qualifies for credit quality step 1 under the CRD directive
 - Counterparty qualifies for credit quality step 2 under the CRD directive and maturity does not exceed 100 days at the time of registration in the Cover pool
 - No value for 85% test
- Hedging instruments: no value
- Value of 30+ days delinquent loans decreased by 50%
- Defaulted loans (i.e. 90+ days delinquent loans) have no value

■ Special Estate – The Register

- Credit institutions must maintain a register of Cover assets and pandbrieven with respect to a special estate
- The special estate includes
 - The assets registered as Cover assets
 - The collateral received in respect of hedging instruments registered as Cover assets
 - Security interest, guarantees and insurances granted in relation to Cover assets
 - Recoveries received in respect of Cover assets or above mentioned accessories
 - NBB reserves linked to the special estate
- The Register will include information about
 - The characteristics of the issued pandbrieven
 - The characteristics of the Cover assets

Special Estate – Cover Pool Administrator

- The NBB may appoint a Cover pool administrator to manage the special estate in certain circumstances:
 - Adoption of a reorganisation measure against the issuer that may negatively affect the pandbrieven holders
 - Initiation of bankruptcy proceedings against the issuer
 - Removal of the issuer from the list of Belgian pandbrieven issuers
 - Where the situation of the issuer is such that the NBB deems that it may seriously adversely affect the interest of the pandbrieven holders
- Upon designation, the Cover pool administrator is legally entrusted with the necessary powers to manage the special estate
- The Cover pool administrator manages the special estate to the exclusion of the issuer, in the interest of pandbrieven holders



THE BELGIAN MORTGAGE MARKET

September 2012



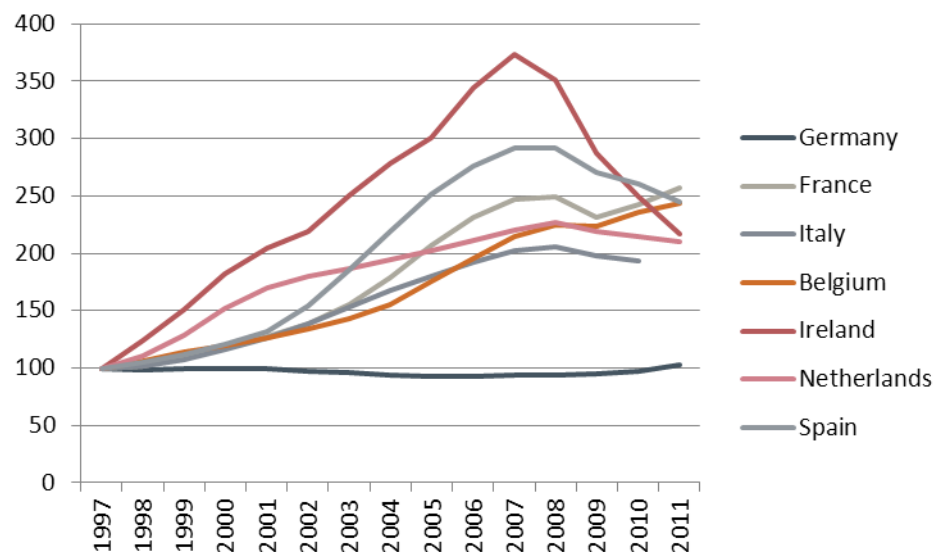
Prices and Mortgage Loans

Prices and Mortgage Loans

Strong growth of house prices

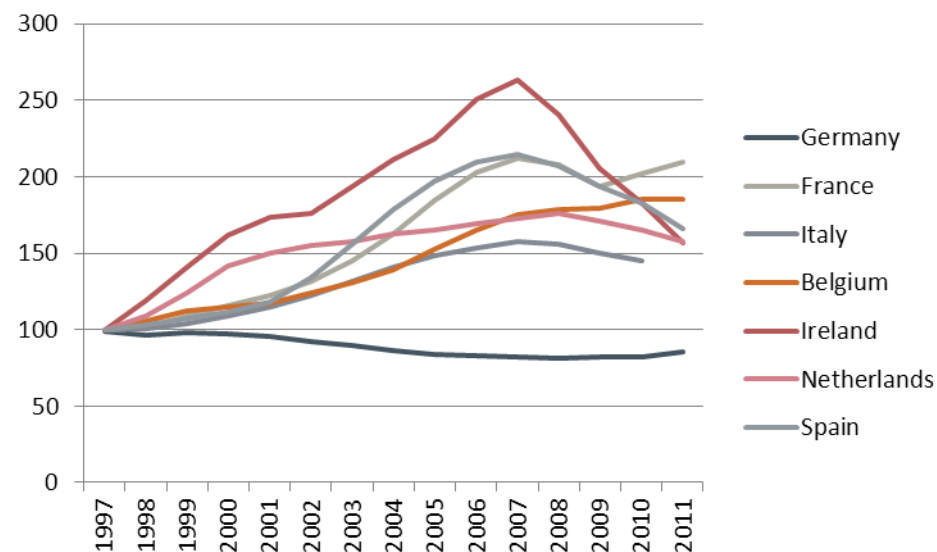
- Nominal House Prices continued to increase
- Real House Prices are relatively stable lately

Nominal House Prices, 1997=100



Source: OECD Economic Outlook Annex Tables

Real House Prices*, 1997=100

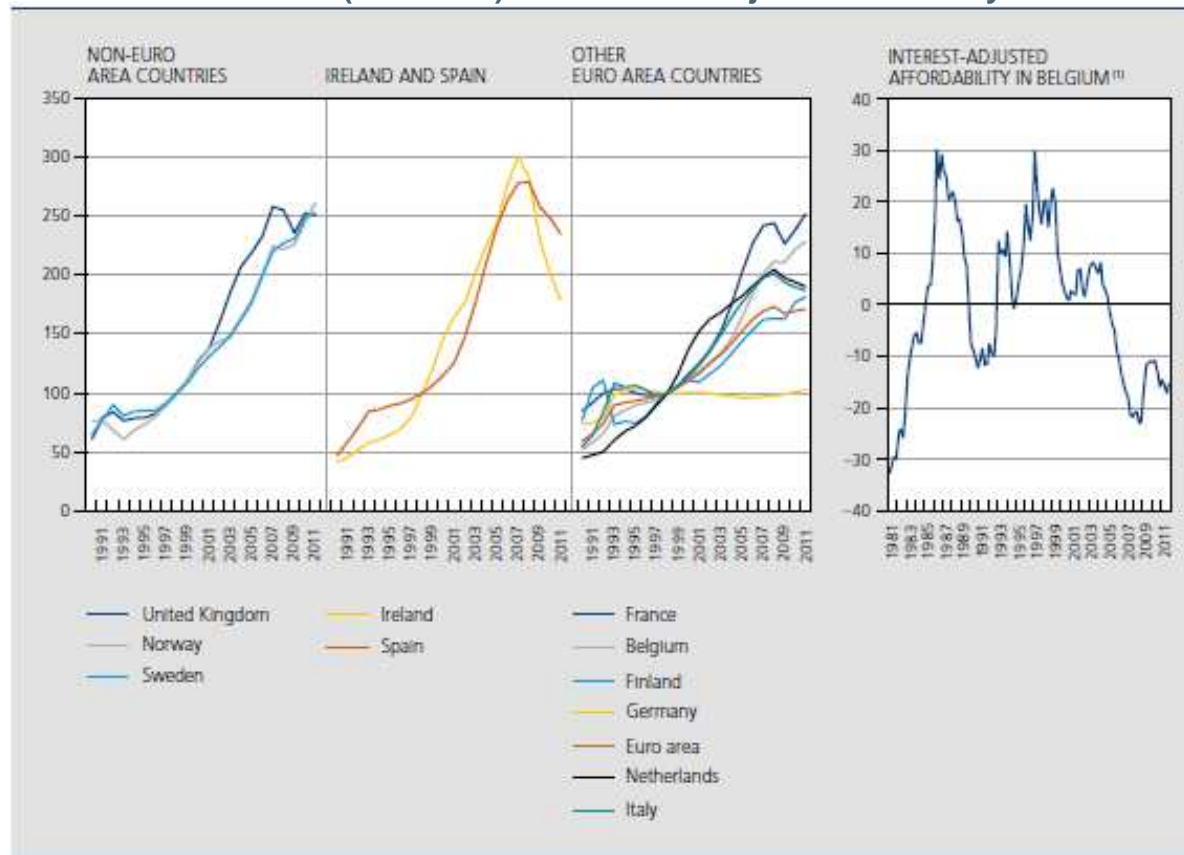


* Nominal house prices deflated by the private consumption deflator

Prices and Mortgage Loans

Belgian market 15% overvalued compared to average since 1981

House Price Indices (1998=100) and Interest-Adjusted Affordability

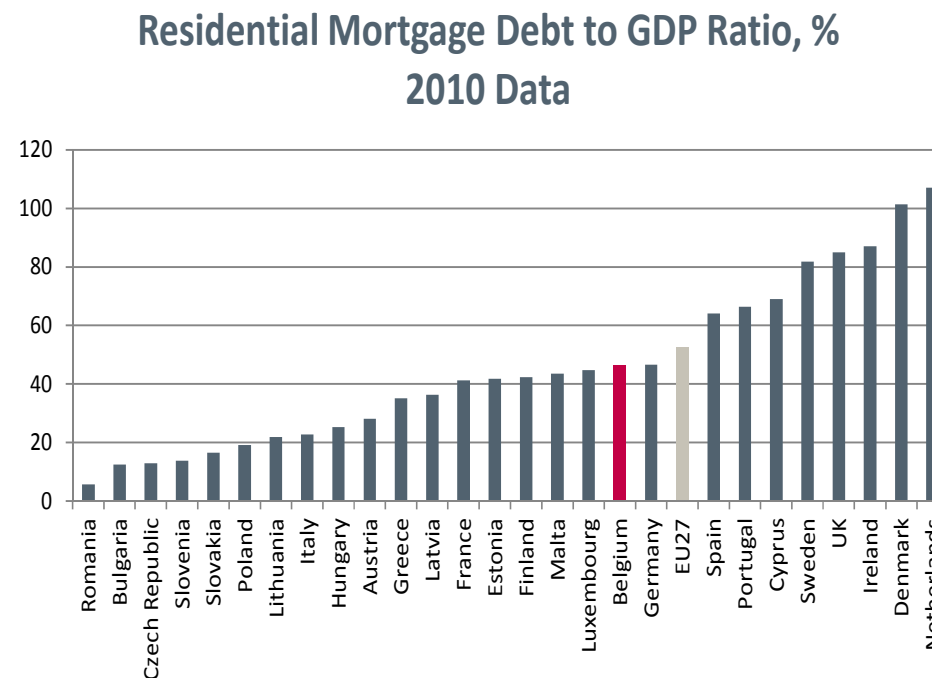
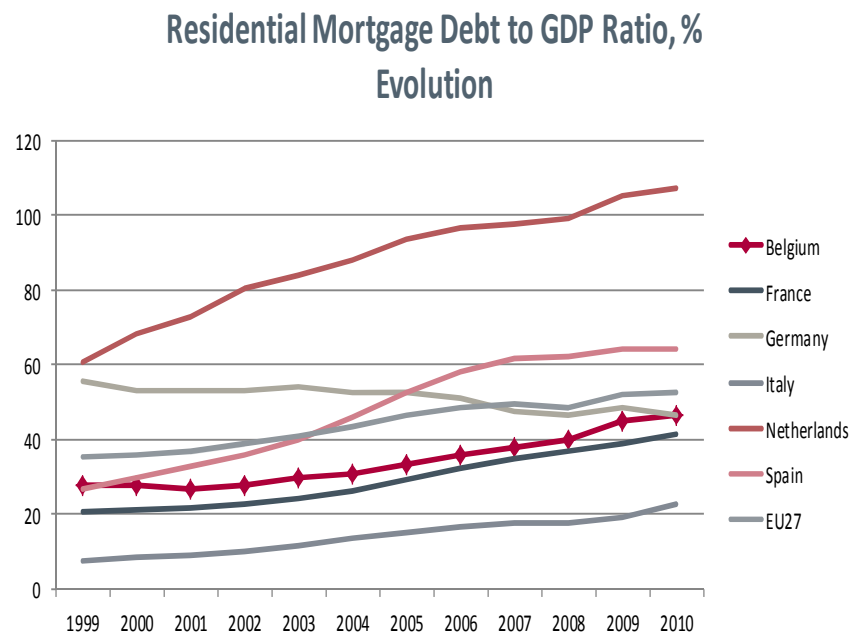


Sources: OECD, NBB.

(1) Ratio between the disposable income of households and the average mortgage loan debt service, which itself depends on house prices and interest rates; percentage deviation from the average of the period since the first quarter of 1981. A negative sign indicates overvaluation of property prices.

Prices and Mortgage Loans

Residential Mortgage Debt: Rising, but still Modest



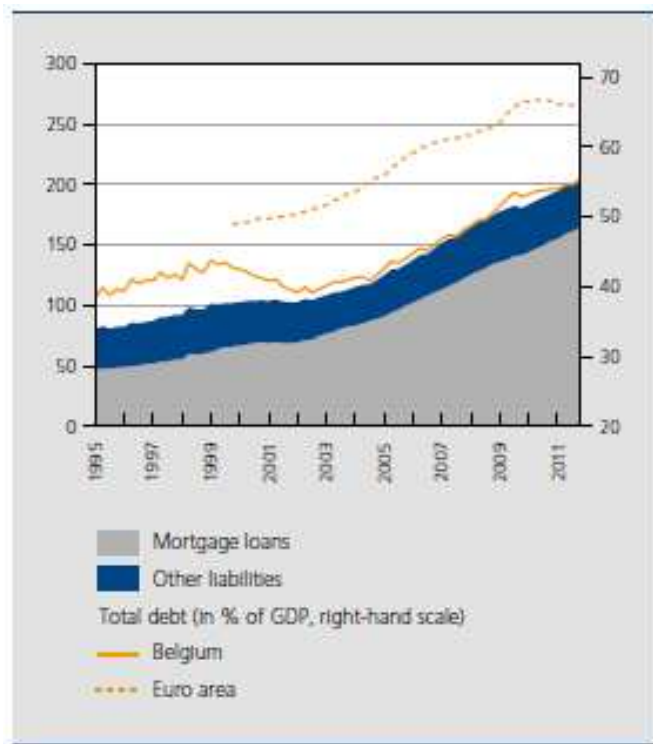
Source: EMF - Hypostat 2010 – A review of Europe's Mortgage and Housing Markets

- Residential mtg debt has increased over the past decade,...
- but remains modest compared to peers

Prices and Mortgage Loans

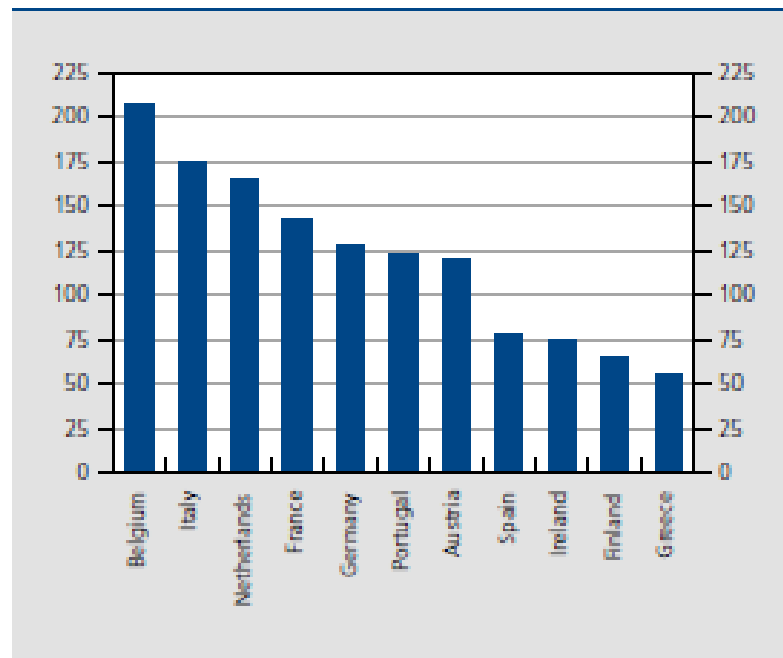
Low Indebtness and Very Strong Net Financial Asset Position

Debt of Belgian Households
(in € billion, unless otherwise stated)



Source: ECB, NBB.

Net Financial Asset Position of Households
(in % of GDP)

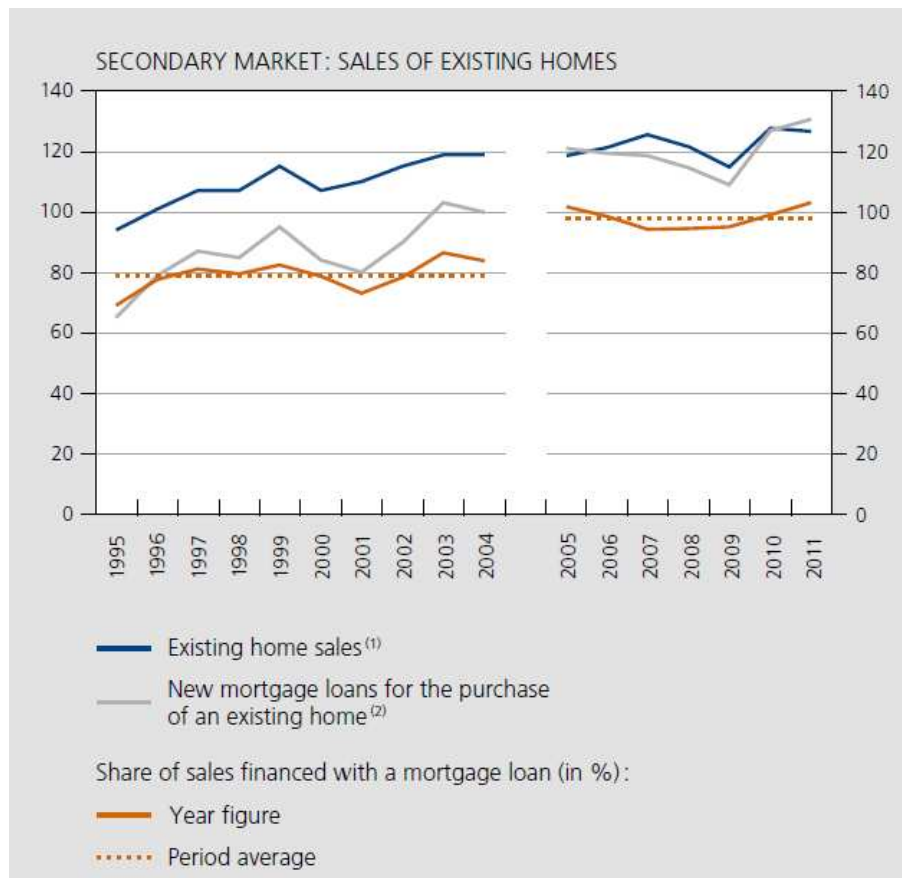


Source: EC, NBB.

- Total debt of household remains low compared to Eurozone average
- Belgian households have high net financial asset position

Prices and Mortgage Loans

Number of Mortgage Loans: Structural Increase in 2005



Source: National Bank of Belgium

- Tax changes led to a structural break
 - Living Bonus
 - Tax Amnesty
- Structural increase in the share of sales financed with a mortgage loan



Tax-Policy Boosts to the Housing Market

Living Bonus

Explains Structural Break in 2005

- In 2005, the federal government introduced a new living bonus.
 - Under the old system mortgage interest payments were deductible and capital redemptions could lead to a tax reduction
 - From 2005, interest payments, capital redemptions and debt insurance payments were **all** deductible
 - Up to €2.120* per person per year
 - Plus €710* in the first ten years of the mortgage
 - The new system led to an increase in debt financing for real estate purchases

* These amounts are indexed every year (Amounts for 2012)

Tax Amnesty

Money Reinvested in Real Estate

- In 2004, the federal government announced a tax amnesty for money hidden abroad.
 - Money could be regulated by paying a fee of 9%
 - The fee was lowered to 6% if the money was reinvested in the purchase, construction or renovation of real estate*
 - The flow of money reinvested in Belgian real estate led to a surge in house prices in 2004-2005.

* Certain other investments also led to a reduced fee.

Green Loans (1)

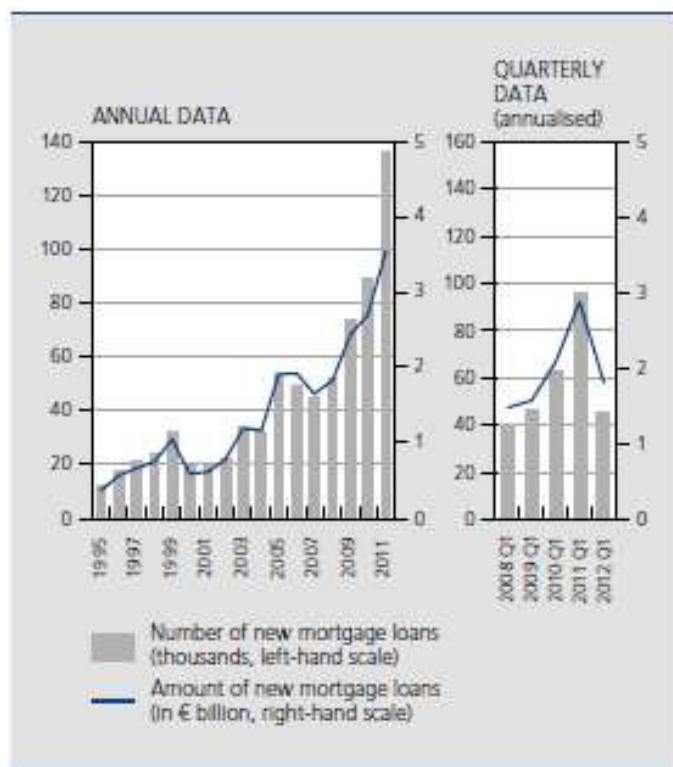
Three Year Boom in Mortgages

- Favourable tax-regime for « green loans »
 - Loan for the sole purpose of financing pre-defined energy-saving investments
 - Programme ran from 1 January 2009 to 31 December 2011
 - Benefits:
 - Interest rate reduction of 1.5%
 - Tax deduction of 40% of the remaining interest rate costs
 - Loan amount between €1.250 and €15.000 per person, house and year
 - Loans were mostly made under form of a mortgage
 - Main examples of energy saving projects:
 - Replacing/maintenance of heating system
 - Solar panels
 - Double glass windows
 - Isolation of roof, floor or walls
 - Thermostatic valves
 - Energy audits

■ Green Loans (2)

Three Year Boom in Mortgages

Mortgage Loans for Renovation



Source : NBB.

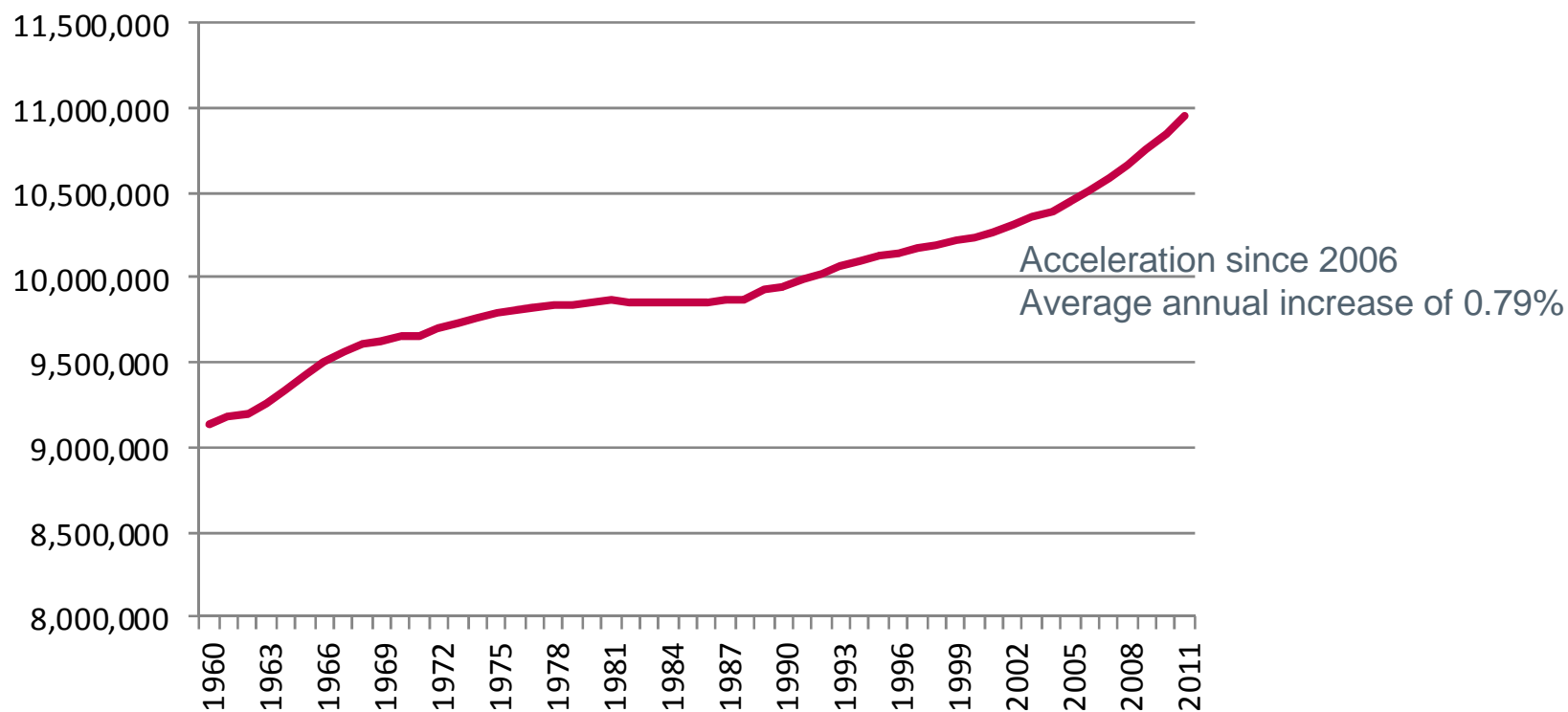
- The number of new loans for renovation purposes surged from an annual average of 36.000 in the period 2000-2008 to an annual average of 100.000 in the years 2009-2011.
- The large number of loans in these three years resulted in new production totalling €8.7 billion.
- Data for Q1 2012 show that the expiring of the fiscal incentives has led to a significant decline in the number and amounts of new mortgage loans for renovation.



Demographics

Demographics

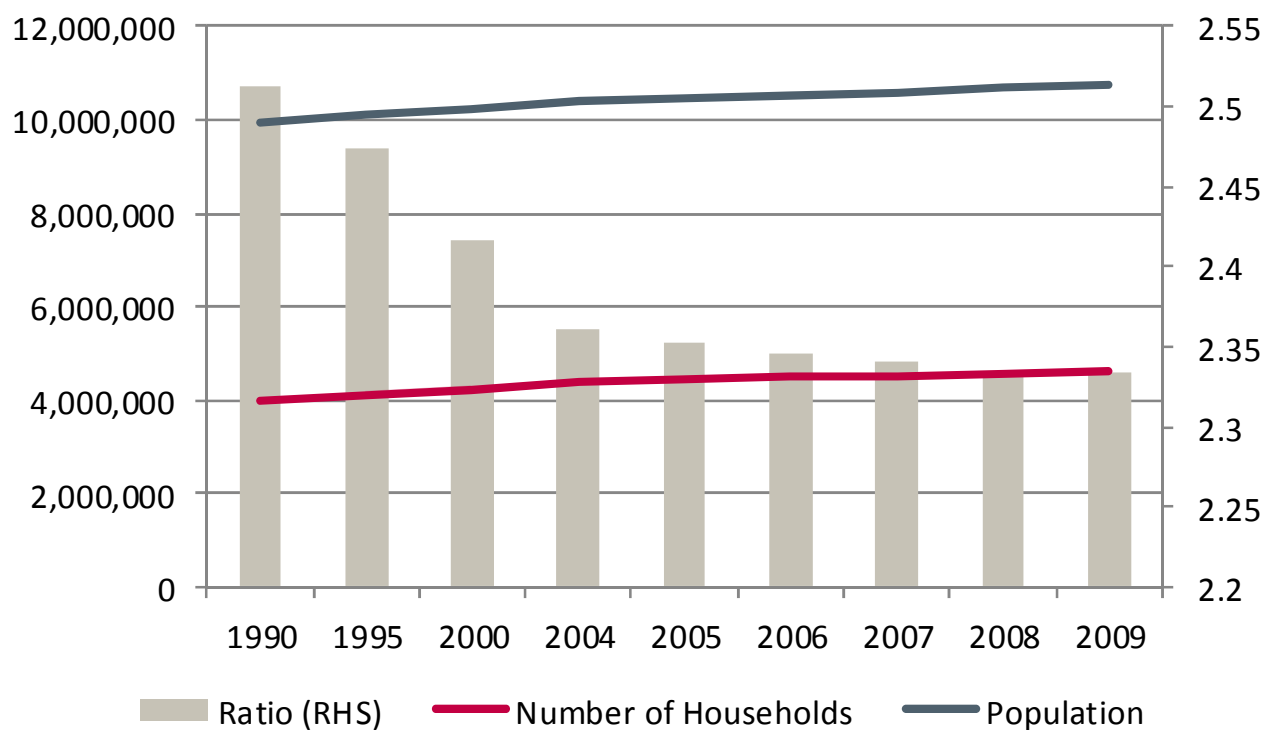
Population increased by nearly 10% over the past 20 years



Source: Eurostat

Demographics

The Number of Households is growing faster than Population

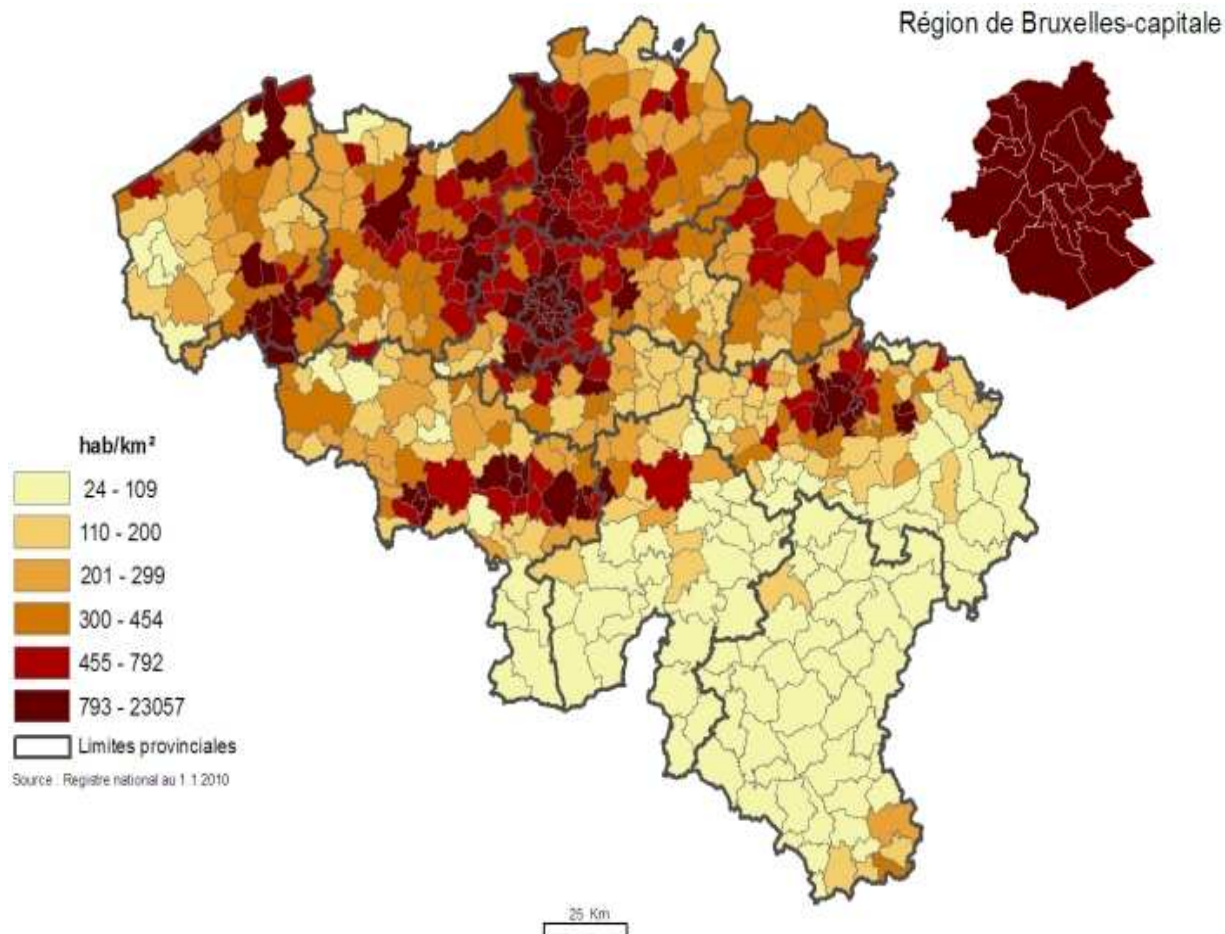


Source: Belgostat and Eurostat

Demographics

Densely populated

- Especially Brussels and Flanders are densely populated
- Between 2002 and 2005 the average size of lands sold for construction shrunk by one-third (S&P)

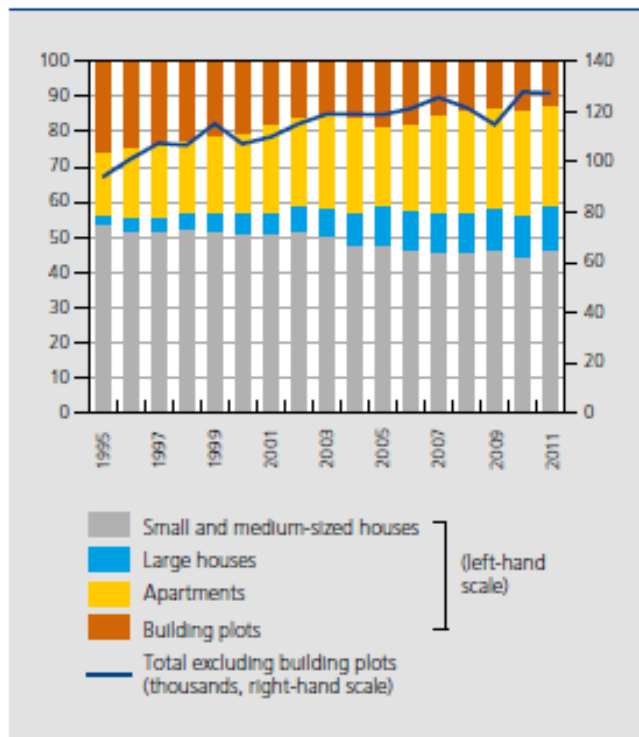


Source: Belgostat

Demographics

Building Plots are Becoming Scarce

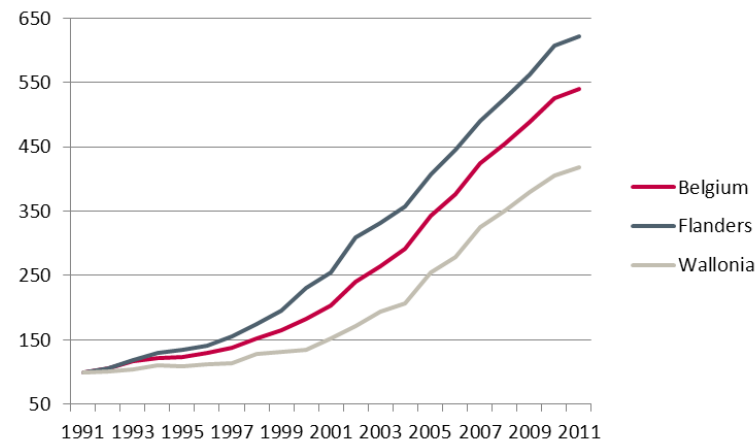
Breakdown of the total number of residential real estate transactions



Source: National Bank of Belgium

- S&P: “Housing supply is structurally constrained in the long term by a scarcity of land and a dense population.”
- Land transactions fell by two-thirds between 1992 and March 2012 in Flanders

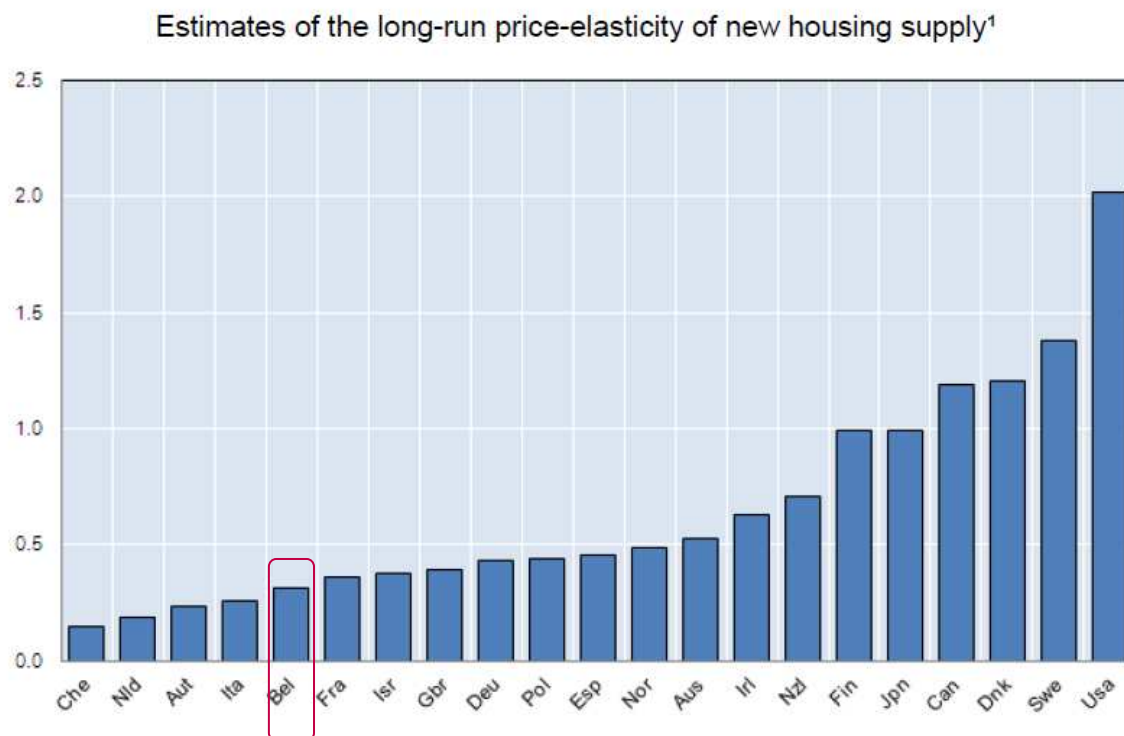
Building Plot Price Index, 1991=100



Source: Stadim

Demographics

Price Responsiveness of housing supply is low



1. Estimates of the long-run price elasticity of new housing supply where new supply is measured by residential investments (i.e. the coefficient on lagged prices in the long-run investment equation as reported in Table 1, of Caldera Sanchez and Johansson 2010). Estimation is based on a system of two equations which model the demand and supply of housing in an error correction framework. All elasticities are significant at least at the 10% level. In the case of Spain, restricting the sample to the period 1995-2007, which would reflect recent developments in housing markets (such as the large stock of unsold houses resulting from the construction boom starting in 2000 and peaking in 2007-09), only slightly increases the estimate of the elasticity of housing supply from 0.45 to 0.58. Estimation period is early 1980s to early/mid-2000s. See Caldera Sanchez and Johansson (2010) for details.

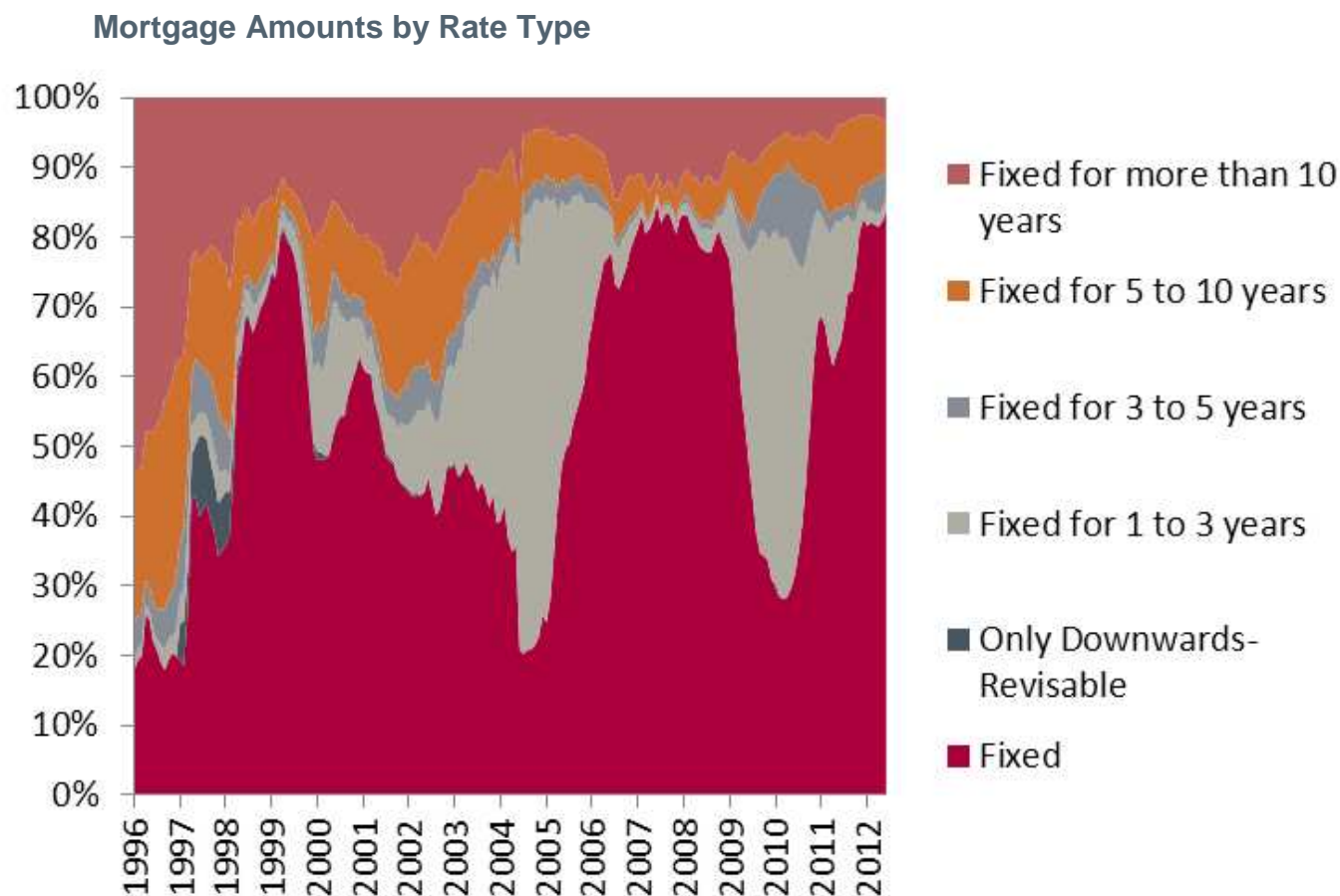
Source: OECD



Mortgage Characteristics

Mortgage Characteristics

Mostly a Fixed Rate Mortgage Market



Source: UPC-BVK

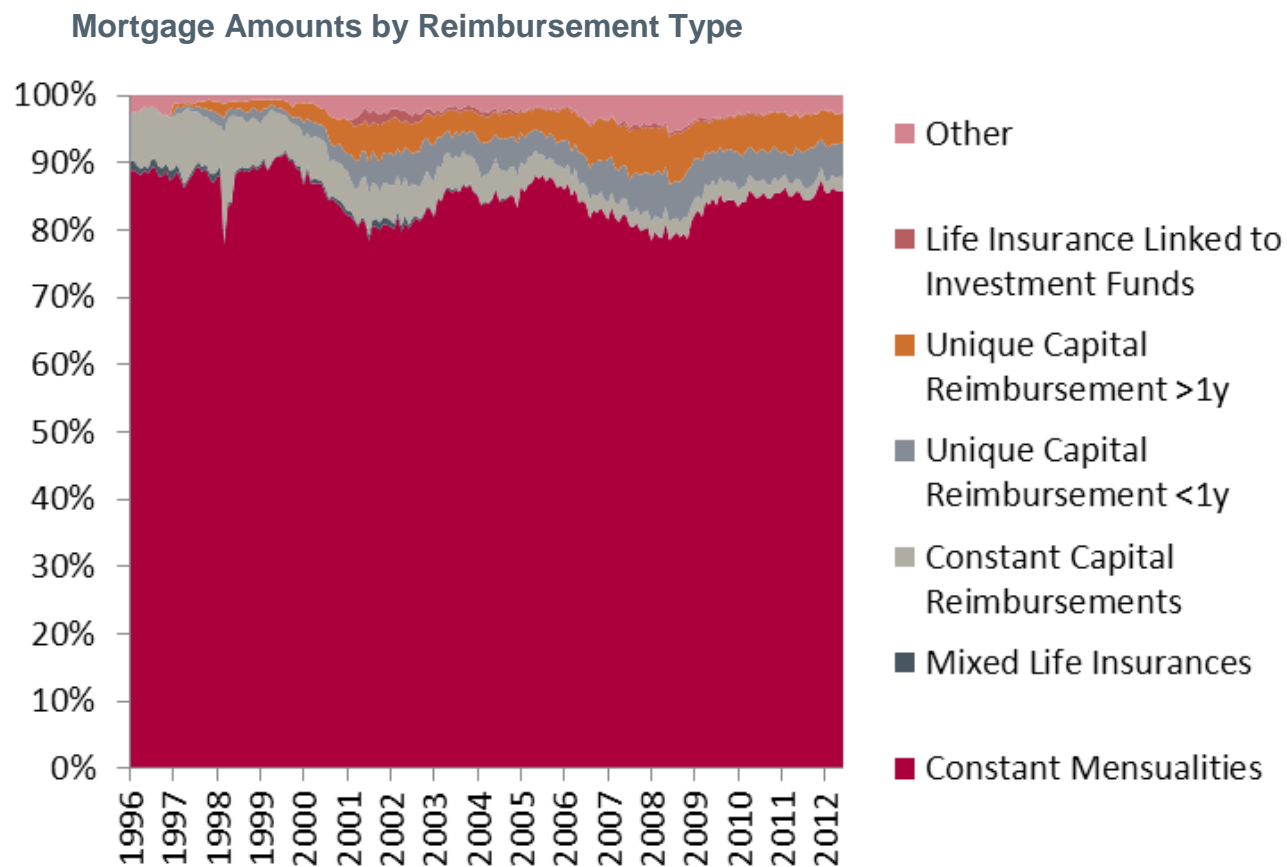
Mortgage Characteristics

Variable-Interest Rate Mortgages are Well Regulated

- The law imposes restrictions on revisable mortgage rates
- After the first year, the interest rate may increase by maximum 1% compared to the original interest rate
- After the second year, the interest rate may increase by maximum 2% compared to the original interest rate
- The interest rate may increase to maximum double to original interest rate
- The reference interest rates are the Belgian 12 month T-bill and longer-term OLO yields. The minimum reset frequency is 1 year.
- Margin fixed at origination.
- The regulation of variable-interest rate mortgages protects the debtor against large interest rate shocks.

Mortgage Characteristics

Share of Interest-Only Loans Remains Low



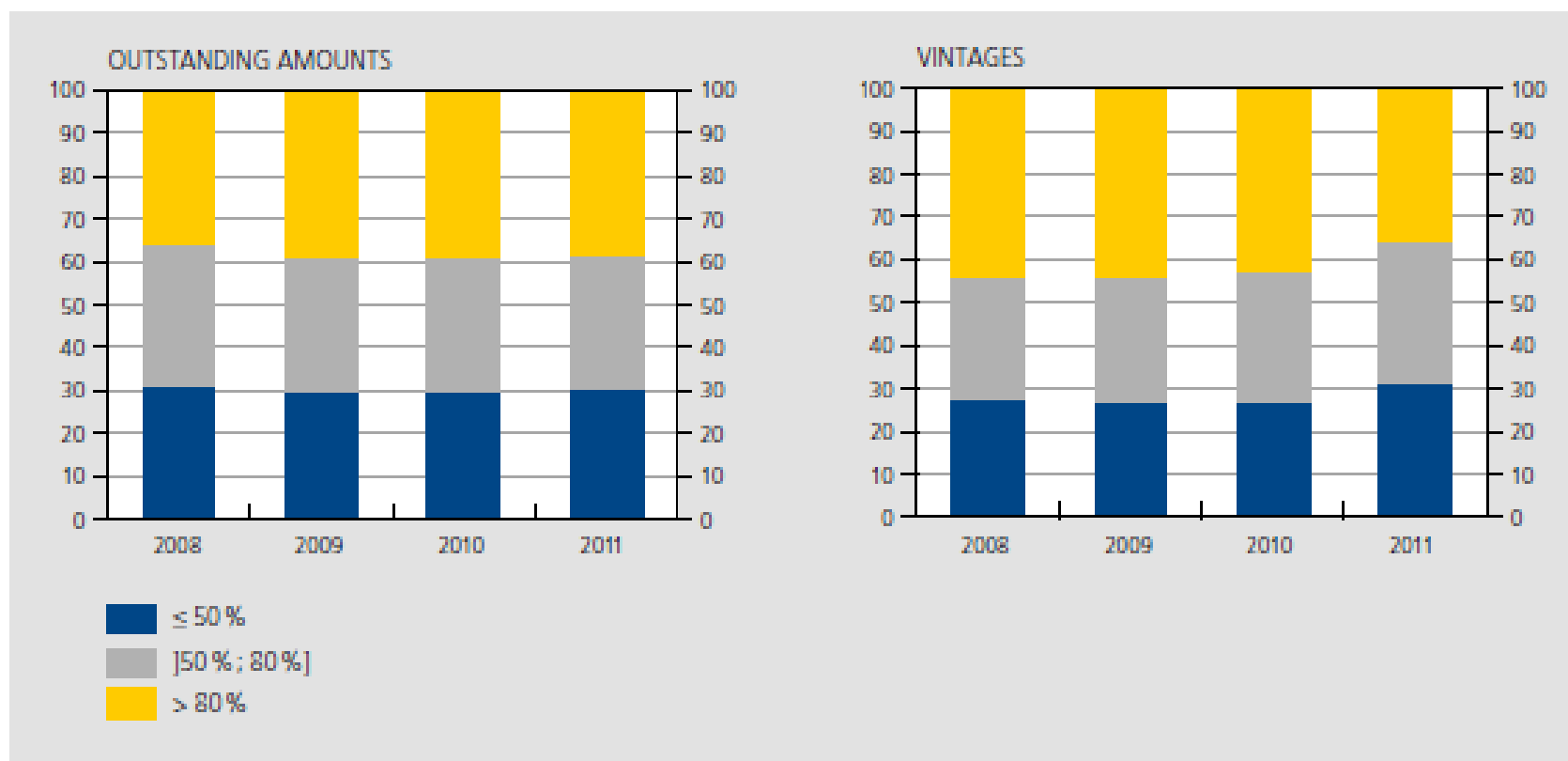
Source: UPC-BVK

Mortgage Characteristics

Trend towards More Conservative LTVs

Loan-to-Value Ratios at Origination

(in % of total loans at the end of the year or total loans granted during a particular vintage)



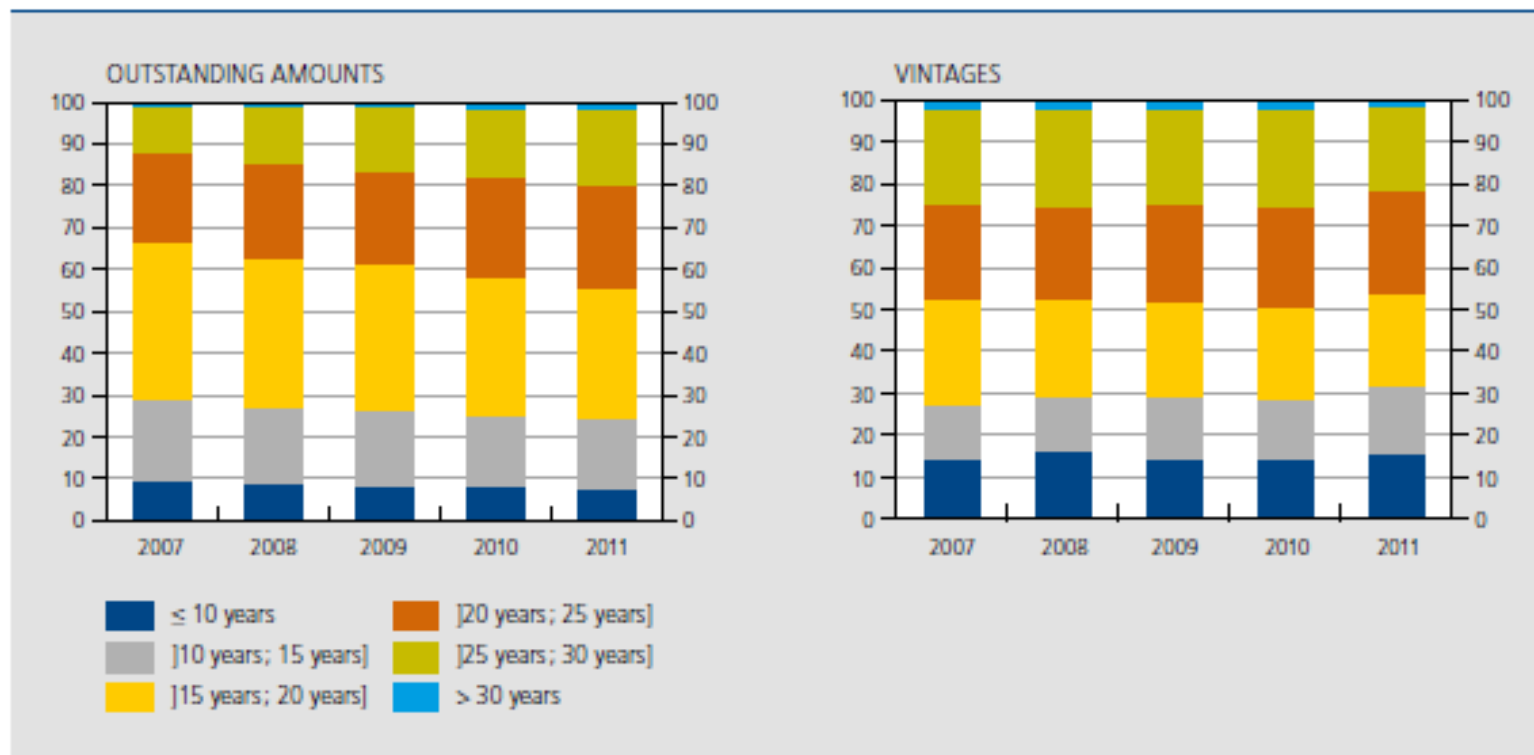
Source: NBB.

Mortgage Characteristics

Share of Loans with Original Maturity >20y has increased strongly

Maturities at Origination

(in % of total loans at the end of the year or total loans granted during a particular vintage)

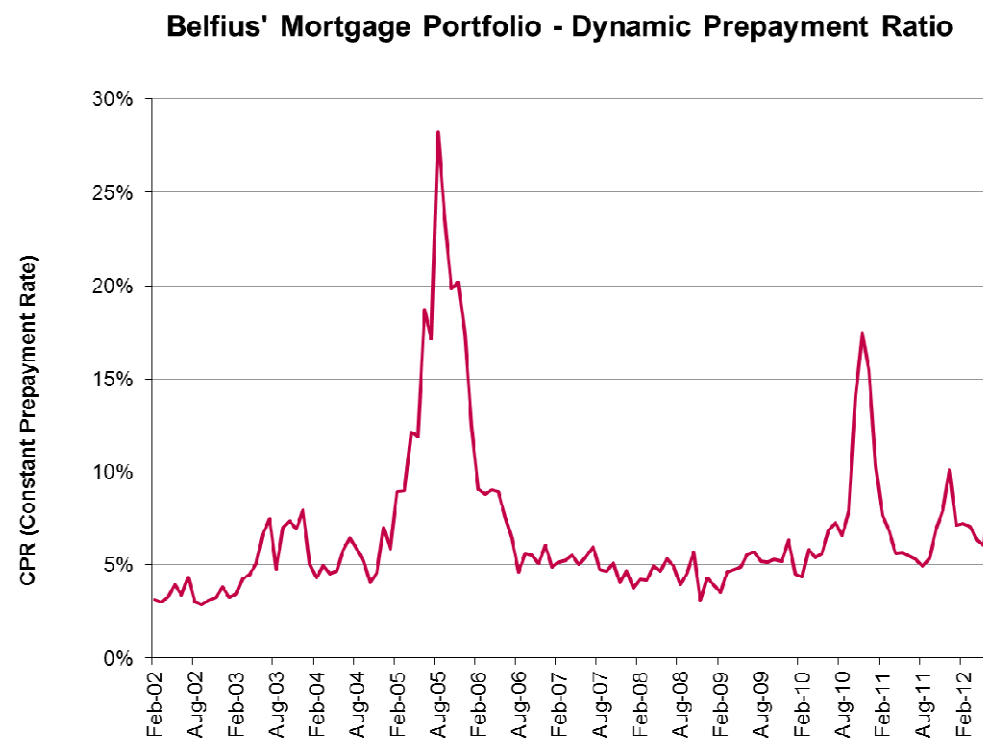


Source: NBB.

- The duration of a mortgage inscription is capped at 30 years.
- Therefore mortgage loans exceeding 30 years are rare.

Mortgage Characteristics

Prepayments can be sizeable

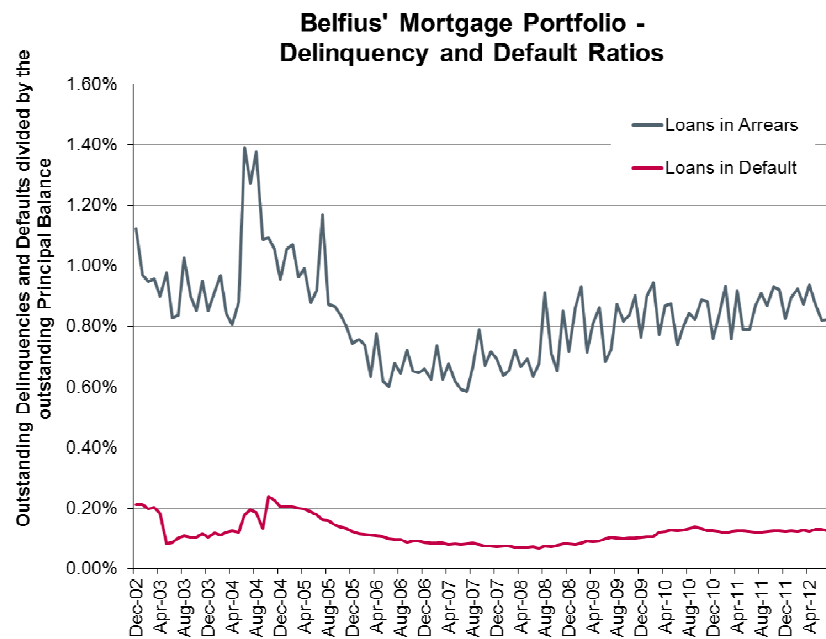


Source: Belfius Bank Originated Belgian Residential Mortgage Portfolio

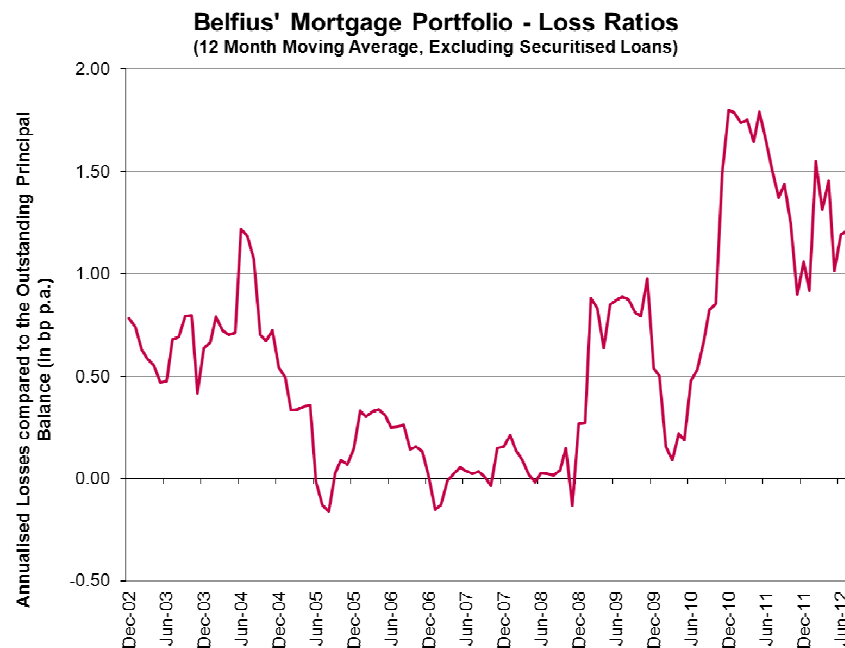
- The law limits the prepayment penalty to 3 months of interest payments on the prepaid amount.

Mortgage Characteristics

Arrears, Defaults and Performance Indicators



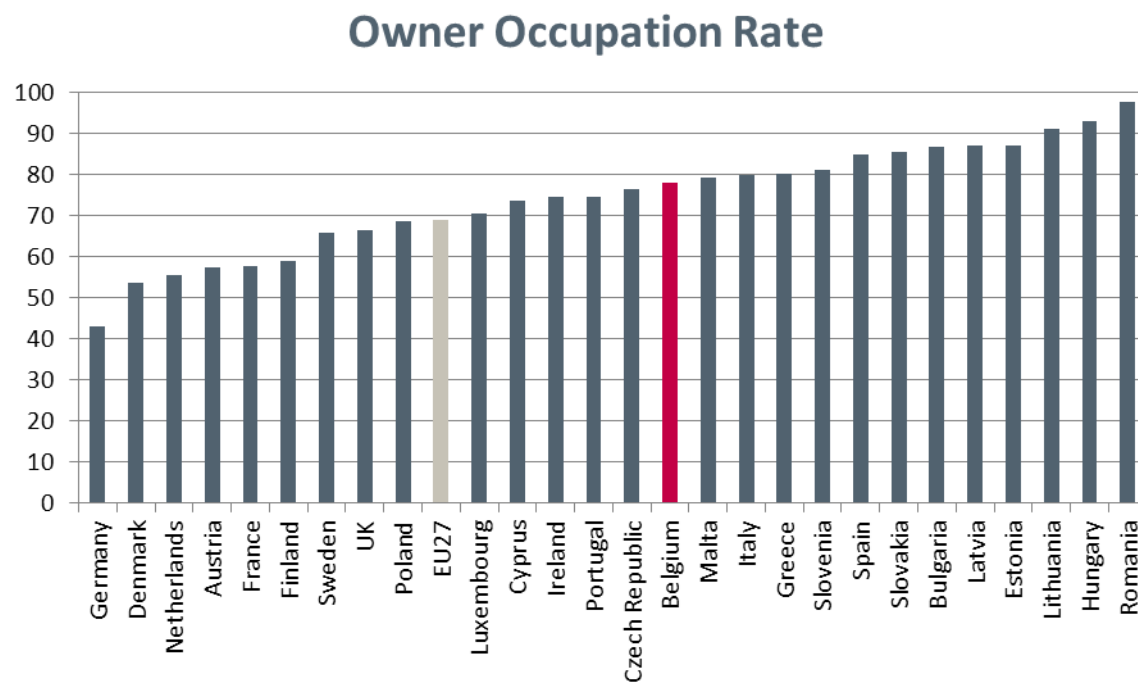
Source: Belfius Bank Originated Belgian Residential Mortgage Portfolio



Source: Belfius Bank Originated Belgian Residential Mortgage Portfolio

Mortgage Characteristics

Due to its tax system, Belgium has a relatively high OOR



Source: EMF - Hypostat 2010 – A review of Europe's Mortgage and Housing Markets

Mortgage Characteristics

Registration Taxes

- Belgium has a system of high registration taxes on the purchase of a real estate property
 - Though this registration taxes are now portable in the Flanders region, the turnover on the Belgian residential real estate market remains quite low compared to other countries.

 - Two levels of registration taxes
 - On purchase: Different in each region
 - Flanders: 10% of sale value (first €15.000 not taxed); portable
 - Brussels: 12.5% of sale value (first €60.000 not taxed); non-portable
 - Wallonia: 12.5% of sale value
 - On mortgage registration: 1% of mortgage amount
- => This explains the existence of the mortgage mandate

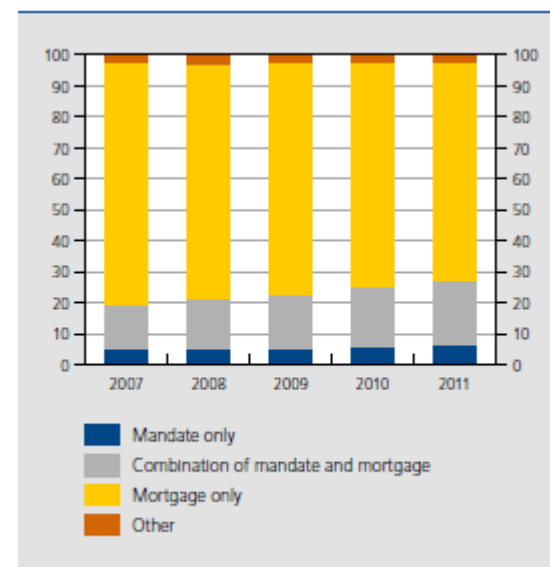
Mortgage Characteristics

Mortgage Mandates

- Mortgages are expensive in Belgium, because mortgage registration fees need to be paid. In order to reduce mortgage registration fees, a mortgage mandate (*hypothecair mandaat – mandat hypothécaire*) is used.
- A mortgage mandate is an agreement between the borrower and a proxy whereby the borrower gives the proxy an irrevocable option to unilaterally (no further involvement of the borrower required) create a mortgage on a predefined property in favour of the lender and this up to a certain predefined amount. This mandate can be exercised at any time.
- It is market practice in Belgium to grant a residential mortgage loan partially covered by a mortgage (frequently up to the maximum tax benefit) and partially by a mandate. This way the borrower avoids part of the mortgage registration fees it needs to pay.

Use of Mandates and Mortgages

(% of total outstanding amounts at the end of the year)



Source: NBB.



Disclaimer

This document is prepared by Belfius Bank NV/SA, Boulevard Pacheco 44, 1000 Brussels, Belgium or by any affiliated company (herein referred as 'Belfius Bank') on behalf of itself or its affiliated companies.

This document is published purely for the purposes of information, it contains no offer for the purchase or sale of financial instruments, does not comprise investment advice and is not confirmation of any transaction.

All opinions, estimates and projections contained in this document are those of Belfius Bank as of the date hereof and are subject to change without notice. The information contained in this document was obtained from a number of different sources. Belfius Bank exercises the greatest care when choosing its sources of information and passing the information. Nevertheless errors or omissions in those sources or processes cannot be excluded a priori. Belfius Bank cannot be held liable for any direct or indirect damage or loss resulting from the use of this document.

The information contained in this document is published for the assistance of the recipient, but is not to be relied upon as authoritative or taken in substitution for the exercise of judgement by any recipient.

In the United Kingdom, this report is intended only for Investment Professionals (as defined in The Financial Services and Markets Act 2000 (Financial Promotion) Order 2001) and is not intended to be distributed or passed on, directly or indirectly, to any other class of persons (in particular retail client) in the United Kingdom.

This report is distributed in the U.S. solely to "major institutional investors" as defined in Rule 15a-6 (U.S. Securities Exchange Act of 1934). Each U.S. recipient by its acceptance hereof warrants that it is a "major institutional investor", as defined; understands the risks involved in dealing in securities or any financial instrument; and shall not distribute nor provide this report, or any part thereof, to any other person. Any U.S. recipient wishing to effect a transaction in any security or other financial instrument mentioned in this report, should do so by contacting Belfius Bank. Investors outside the US and UK are encouraged to contact their local regulatory authorities to determine whether any restrictions apply to their ability to purchase investments to which this report refers.

This report or any part of it may not be reproduced, distributed or published without the prior written consent of Belfius Bank. All rights reserved.