Mortgage Finance GAZETTE

Flexible lending for Europe

Despite present worries over US sub-prime mortgages, similar market flexibility in Europe would help boost home ownership. Allan Saunderson interviews **Clarence Dixon**, the European managing director of Crown Northcorp

Even if the sub-prime mortgage market in the US is currently throwing profound jitters into financial markets worldwide, Europe – and particularly Germany – would benefit from the boost in home ownership that flexibility via such non-conforming credits could provide, says the top European official for US/UK-based servicing group Crown Northcorp.

Clarence Dixon, a native of California and head of European business development for Crown Northcorp, is one of the few Americans on the continent with experience in sub-prime, or 'non-conforming' home loans. He estimates that about 10 per cent of the German new mortgage market – about €10 billion a year – has the potential for the category: lower downpayments and higher loan-to-value: available for borrowers with below-prime credit records, attracting higher interest rates to offset increased lender risk.

"If you look at the German market with about 40 per cent home ownership, one of the main reasons is that in the past the banks have made the hurdle very, very high," Dixon said: "If you can't come in with 20 per cent or 30 per cent equity, you go and rent. On a €200,000 or €300,000 home, who has €60,000, €70,000, or €80,000 spare in their pockets? Not very many people."

Offering products such as low equity mortgages would not only help large numbers of individual families, but also be the natural exit for major private equity groups that invested in residential portfolios and are now turning to portfolio sales to exit. "If you make the mortgage payments higher than the rent, you just blow yourself out of the marketplace," Dixon says. "If you've got a person paying €400 rent every month, you can't sell them mortgage financing at €600. You're going to have to come in with a product that says well, if your rent is now €400, your mortgage payment is going to be €330 – a product that's low equity and that creates value. Then you have the customer for life. Those are the types of products and clients we want to target in this market."

Sub-prime

Does Dixon think US sub-prime problems will spill over to Europe? "My answer to that question is no," he says. "Number one, you don't have a sub-prime market in Germany – which is the key reason Crown decided to establish here. Number two, most of the turmoil in the US is not caused by loans originated in 2007 or 2006 but in 2002/2003 when people were throwing money into the marketplace trying to pick up everything they could get."

Early this decade Crown in the UK created the Rooftop subsidiary to provide non-conforming mortgages. In Germany last year, it bought the Bochum-based Westphalia Bank from HypoVereinsbank and transformed it into Crown Westfalen to have the banking licence and institutional expertise to service non-performing loans and move into home loan lending.

Dixon says the special servicing unit is running well but the market is shifting. "In NPLs, you don't have the big portfolios coming on to the market any more," he says. "The savings banks are becoming restrictive about selling because of the public view of this. The mortgage banks have more or less cleaned up their houses. The market is going to smaller portfolios: €10 million to €30 million, instead of the €50 million to €100 million."

Third-party administration

The second priority is primary servicing for third-party non-conforming mortgage lenders: "If you get a lender, typically US, UK or Asia-based, they don't want to come over here and set up a bank. It doesn't make sense for two or three years or five years. What we offer is a banking platform to originate loans on their behalf. Funder X will say 'I want to invest €500 million in sub-prime with high LTV or low LTV or low credit rating' – whatever they call non-conforming. They design the product, define the criteria, give it to us and we can originate the loans for them. We distribute them through our banking platform, sell them back to the funder and service them through to maturity. The loans will never stay on the books of Crown Westfalen; we don't take the risk. Once they have a book big enough, the funders will securitise or do a whole loan sale, whatever exit strategy they decide."

Other European countries

After Germany, Dixon sees the Netherlands, Spain, Portugal and Austria as the most interesting jurisdictions for non-conforming mortgages in Europe. France offers huge opportunities but the marketplace and regulatory hurdles generally hinder access by third parties. But Germany is different. "What makes this market so attractive is that you have had 10 to 12 years of property stagnation," Dixon says. "Now the first indicators are showing rises, inch by inch. Where's the risk? There is none."

Dixon says he has had positive response from German banks considering outsourcing their non-conforming business. "Of the, say, 20,000 applications they get in a year, only 7,000 applications fit, and of those only 5,000 are ruled worthy. I tell those banks 'Give me those other 13,000 that you throw away. I am not a competitor. I don't want the relationship with the borrower, I just want the mortgage.' The German high street bank can keep the savings account, keep the deposit account, keep the bonds, the insurance policies and all the cross-selling potential, without throwing the client out the door to, possibly, another lender." **MFG**

Allan Saunderson is managing editor of Property Finance Europe, *where this interview originally appeared*