REALKREDITRÅDET
ASSOCIATION OF DANISH MORTGAGE BANKS

By e-mail

CEBS

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"Second part of CEBS's technical advice to the European commission on liquidity risk management"

CEBS has on 17 June 2008 published the consultation paper: *"Second part of CEBS's Technical advice to the European commission on liquidity Risk management"*. The Association of Danish Mortgage Banks[1] welcomes the initiatives communicated in the paper, but has the following suggestions to clarify the paper.

It is stated in **recommendation no. 17** that the institutions actively should monitor their funding sources to identify potential concentrations, and they should have a well-diversified funding base.

The Danish Mortgage Banks are specialized mortgage banks with no right to receive deposits. Furthermore, the mortgage banks can only fund loans by the issuance of various types of covered bonds.

Recommendation no. 17 should reflect that it is to be understood under due consideration of the nature and national legal framework of the institution; i.e. both commercial banks and specialised mortgage banks. We expect that the intention with recommendation no. 17 is not to hinder the activities of the specialised mortgage banks.

Our comments also apply for **recommendation no. 15** (adequate contingency plans) and **recommendation no. 16** (liquidity buffer).

The bondholders cannot accelerate the bonds and demand premature payment from the mortgage banks. There are also no deposits to be withdrawn; i.e. the mortgage banks cannot be confronted by a run in the traditional way.

Furthermore, there's no funding liquidity risk in the "lifetime" of a Danish mortgage credit loan:

- When the loan is disbursed, the borrower receives the proceeds from the sale of the covered bonds,
- There is - due to the very strict Danish balance principle - nearly no mismatch between the payments from the borrower and the payments to the bondholders,
- A high proportion of the loans are funded by covered bonds that mature at the same time as the loans, and
- if the borrower redeems the loan, the corresponding bonds are redeemed.

Finally, the Danish covered bonds are highly liquid.

[1] Realkreditrådet is the trade organization of the Danish mortgage banks. At the end of 2007, the member mortgage banks had a total lending of approx. DKK 2,080 bn. corresponding to approx. EUR 280bn

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The mortgage banks need for a well diversified funding base, a contingency plan and a liquidity buffer is therefore less than for commercial banks.

The liquidity risk of the Danish mortgage banks is very limited, to possible missing payments from borrowers over the life of the loan. That liquidity risk is by nature arising as a result of either settlement or credit risk, not funding liquidity risk.

It is therefore important to stress that possible requirements for the mortgage banks should not be assessed for example in relation to the mortgage banks' liabilities, but rather in relation to the very limited liquidity differences the mortgage banks actually might meet on the cash flows over the life of the loans and issued bonds.

Best regards,

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