» **Print**

Banks cash in on French housing boom

11:28am GMT

By Lionel Laurent

PARIS (Reuters) - The traditional French aversion to risk and debt is being turned on its head as rock-bottom interest rates and tax breaks push investors into real estate, boosting banks' mortgage lending and their client revenue.

The worry is not that a subprime-style fiasco is in the making, but rather that these trends are unlikely to last.

French housing loan issuance doubled in the 12 months to November 2010, according to the Banque de France, to 145 billion euros (£125 billion) -- eclipsing mortgage stagnation in crisis-scarred Spain and a 7.9 percent decline in Germany.

House prices in France also outpaced Spain and Germany with an 8.6 percent rise in the third quarter of 2010, according to the Royal Institution of Chartered Surveyors, driven by a cocktail of ultra-low interest rates and government incentives to spur homebuying.

Such growth is not a ticking time bomb for domestic lenders like BNP Paribas and Credit Agricole, analysts say. French household balance sheets are solid, lending standards are tight and according to Deutsche Bank France has one of the lowest mortgage-to-GDP rates in Europe at 35 percent.

"Housing loans in France are of a significantly higher quality overall than in a lot of other countries," said Christophe Nijdam, analyst with Alphavalue. He said France lacked the kind of helter-skelter securitisation that had encouraged U.S. lenders to take big risks in the past.

"When you have to keep the credit risk on your balance sheet, it keeps you responsible," he said.

Mortgage growth also means more revenue for French banks' retail units, which for much of 2010 have proven to be a reliable growth engine amid uncertain capital markets. Margins on housing loans are wafer-thin but French banks use them to cross-sell a variety of products and lift client revenue.

In the first nine months of 2010, revenue rose by 3 to 6 percent at BNP Paribas, Societe Generale and Credit Agricole's domestic retail units, offsetting declines in corporate and investment banking.

2011 HEADWINDS

The bigger risk for banks is simply that the party won't last through to the end of 2011. Long-term borrowing rates are on the rise and French President Nicolas Sarkozy's administration may also target capital gains on real estate with an expected tax overhaul.

"The key question is sustainability," Mediobanca analyst Antonio Guglielmi said. "As long as we are in the current rate environment it looks quite healthy in terms of growth."

But borrowing rates face upward pressure. With long-term rates on the rise and incoming Basel III bank regulations set to increase banks' cost of capital on mortgages, housing loan rates could rise by 1.25 percentage points in the second half of 2011, to nearly 4.6 percent, says Alphavalue's Nijdam.

The result is likely to be a slight slowdown rather than a big drop in mortgage volumes, analysts say, but already the property market is preparing itself for a wave of uncertainty.

"It's too soon to tell what's going to happen this year ... There are too many unknowns, whether over tax reform or the macroeconomy," said Pierre Bazaille, head of the Notarial Institute for Property Law. He said notaries had already been "swamped" in December with last-minute transactions.

For Bazaille, the growth in prices has been uneven and hugely tilted towards Paris and outlying suburbs, implying a correction of price falls seen during the recession.

The threat of a slowdown might tempt banks to drop their standards and keep churning out mortgages despite rising borrowing costs, said Alphavalue's Nijdam, not just because of the revenue boost but because it allows them to amass political capital by showing they are financing the economy.

The idea of a slackening of risk controls is not realistic, bankers in Paris say. But either way 2011 is likely to see a return to more normal lending patterns for France, as investors seek other places to put their money than roofs over their heads.

(Editing by Jon Loades-Carter)