Who pays? An analysis of the cost of consumer credit in Belgium, regulation and implications

M. de Sola
A. Francart
Ch. Piette
M.D. Zachary

Introduction

While consumer credit generally only accounts for a relatively small fraction of Belgian households' total debt – which mainly consists of mortgages – it can play an important role in easing budget constraints when it comes to some big-ticket spending items. But this type of "instant" credit can easily lead to an excessive debt burden for the most vulnerable households, that in turn can be exacerbated by excessively high borrowing costs. To alleviate that risk, one of the aims of consumer credit regulation, in Belgium as elsewhere in Europe, is to limit the cost of borrowing for households. The legislation therefore lays down a definition of the annual percentage rate of charge (APR) and a ceiling on those rates.

The latest change in these ceilings in Belgium dates from June 2021, when the maximum APR for credit lines and overdrafts was lowered by one percentage point. The maximum rates for other loans were not changed. Against this background, the purpose of this article is to document the importance of high APRs in the Belgian credit market and to assess how changes in maximum rates might affect borrowers and lenders.

Although there is currently no detailed information on the interest rates and charges applied to individual loans granted in Belgium, several series of variables collected by the National Bank may shed some light on the consumer loan market and enable us to study the implications of any change in the maximum APRs charged on consumer loans for the financial sector and for households. Data from the Central Individual Credit Register, data obtained from prudential reporting, and the average interest rates charged on loans reported to the NBB by Belgian banks are among the sources used. This article also analyses the results of the Household Finance and Consumption Survey (HFCS) conducted on a representative sample of Belgian households. These various sources are supplemented by survey data received from the Federal Public Service Economy (FPS Economy) to ascertain the prevalence of loans at relatively high interest rates, both among Belgian households and in the financial sector. The assumption is that some types of households, expenditure categories and lenders are more likely to relate to highly-priced loans and, therefore, be affected by any revision of the maximum APRs. Under certain circumstances, a lower maximum APR could also have implications in terms of the supply of loans.

The text is structured as follows. Section 1 sets out the current regulations in Belgium and describes the situation in the three neighbouring countries. Section 2 offers an overview of the consumer credit market in Belgium, in particular assessing the prevalence of the loan categories generally associated with high interest rates.

Sections 3 and 4 examine the distribution of the loans according to their cost, from the respective points of view of borrowers and lenders. Finally, section 5 includes some considerations relating to other aspects of consumer credit derived from the literature. The conclusion summarises the main findings of the analysis.

1. Legislation on APRs charged on consumer credit

1.1 Limit on the cost of consumer credit

In the European Union, national laws on consumer credit have to comply with the Consumer Credit Directive, applicable since 11 June 2008[1], which aims to ensure transparent and efficient credit markets while also protecting consumers. The Directive stipulates that the APR must be mentioned when a loan agreement is concluded. The APR indicates the cost of the loan by a standardised method which permits comparison between offers of credit obtained from lenders who may perhaps be located in different Member States. Thus defined, the cost (for the customer) must include all the charges relating to the credit provided, namely the market interest rate, operating costs, a risk premium (for expected or unexpected losses) and the credit provider's margin.

The main element of the APR is the interest rate, i.e. the percentage paid on the outstanding amount. That rate is generally lower in the case of a loan for the purchase of a specific item, since the purpose of the credit is known (the asset may be pledged if necessary); that is not the case for a credit line (opened without any time limit), nor for a personal loan, since the bank does not know the reason for the loan and therefore has fewer safeguards.

1.2 The situation in Belgium

1.2.1 Maximum rates

In Belgium, the APR on a consumer loan is limited by law. So, lenders cannot charge more than the legal maximum rates. Those maximum rates depend on two factors: the amount of the loan and the type of loan

1 Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC.

Table 1

Maximum APRs on consumer credit granted in Belgium

(November 2021, in %)

Amount borrowed	Loans and hire purchase	Credit facilities and all other types of loan	
		with card[1]	without card[1]
Up to € 1 250	17.5 (from 01.12.2019)	13.5 (from 01.06.2021)	9.5 (from 01.06.2021)
Between € 1 251 and € 5 000	12.5 (from 01.06.2016)	11.5 (from 01.06.2021)	8.5 (from 01.06.2021)
Over € 5 000	10.0 (from 01.12.2015)	10.5 (from 01.06.2021)	8.5 (from 01.06.2021)

Source: FPS Economy.
1 Card with electronic functions.

agreement. Changes in the legal maximum APRs only concern new agreements and those at variable interest rates. The maximum rates may change every six months according to the methodology described below. In November 2021, the rates in force could not exceed the limits set out in table 1.

1.2.2 Setting of maximum APRs

The method of calculation currently used in Belgium to set the maximum APRs was introduced on 1 February 2007.

Each year, at the end of March and the end of September, a review is conducted to check whether the maximum APRs need adjusting, following a change of at least 0.75 p.p. in the reference indices. The reference index used depends on the type of loan:

- for credit lines and overdrafts, it is the monthly average of the three-month Euribor interbank interest rate;
- for other forms of loan, depending on the amount borrowed the benchmark is reference index A, B or C applicable to mortgage loans, namely the interest rate on 12-month treasury certificates, 2-year Belgian government bonds or 3-year Belgian government bonds.

Finally, the new maximum APRs come into force on the first day of the second month following their publication in the *Moniteur belge*. As the revision is carried out in March and September, the changes will typically apply from the following month of June or December, respectively.

A change in the legal maximum APRs only affects new agreements and current agreements at variable interest rates, for example credit facilities offered with cards issued by banks, major retailers and mail order companies.

For current agreements at variable rates, if the new maximum rates are lowered any rates that exceed the maximum must be reduced accordingly. If the maximum rates are increased, lower rates can be raised to the level of the new maximum so long as consumers are warned of this change in advance and informed of the new APR.

The change in the maximum rates also influences debit interest rates on sight accounts, which are charged in the event of the account being temporarily overdrawn. Such overdrawing, treated as short-term credit, is in fact regulated as if it were an open-ended credit facility without a card, for an amount up to € 1 250.

The latest change in maximum APRs dates from June 2021: the maximum rate of charge for credit lines and overdrafts was lowered by one percentage point for all loan amounts, as, in March 2021, the three-month Euribor was 0.75 of a percentage point lower than that observed at the time of the previous revision (September 2012). The maximum APR for other loans remained unchanged, as their respective reference indices were more stable.

1.3 Comparison with neighbouring countries

Belgium's three main neighbouring countries have also set a limit on the interest rates charged on consumer credit. Specific rules were introduced there at the beginning of the 20th century, or even earlier in Germany, and have been adjusted several times since then.

In France, this subject is governed by the Consumer Code, which defines an exorbitant loan as any credit granted at an annual percentage rate more than one-third higher than the average real interest rate charged during the preceding quarter by credit institutions and finance companies for transactions of the same type entailing similar risks. That average rate is calculated by the Banque de France every three months and varies according to the type and amount of the loan. In addition, credit providers are obliged to offer consumers an instalment loan and not a renewable loan (such as a credit card), if the amount requested exceeds € 1 000. However, the French law does not cover the charges on small bank overdrafts for which banks can impose a minimum flat-rate charge,

the amount being determined arbitrarily (generally around € 5 but possibly up to € 22 [1]). This supplement is not included in the APR, but if it is taken into account it may increase the APR considerably, to well over the exorbitant level as defined above.

In Germany, restrictions on interest rates are applied indirectly via case-law rather than by a regulatory authority setting maximum limits. An agreement subject to an interest rate deemed unethical can therefore be invalidated. Thus, the Supreme Court has ruled that interest rates twice as high as the relevant market rate calculated by the central bank (or 12 % above such a market rate) are *contra bonos mores* (*sittenwidrig* – immoral).

In the Netherlands, the maximum rate is set at the statutory rate of 2 % plus 12 % (*Wet op het consumentenkrediet*), taking it to 14 %. Owing to the pandemic, that supplement was temporarily cut to 8 % on new loans between 15 July 2020 and 1 March 2021 [2]. A change in the law is currently under consideration in order to make that reduction permanent. People unable to obtain credit can turn to municipal credit institutions which offer social consumer loans. Despite these schemes, some consumers excluded from traditional channels turn to online loans from companies based in other European Union countries.

1 As at 8 January 2021.

2 To our knowledge, the Dutch government has not yet evaluated the temporary reduction in the maximum rate, nor has it assessed the impact, if any, on the provision of consumer credit.

Table 2

Maximum APRs in Belgium, Germany, France and the Netherlands

	Date of introduction	Reasons for introduction	Current method of setting the limit
Belgium	Introduced in 1990	Protecting consumers Preventing excessive rates Preventing excessive volatility in variable rates	According to the movement in the benchmark rate (per 75 basis point change)
Germany	Introduced in the 19th century (abolished between 1940 and 1969)	Avoiding lending at excessive rates	2 × the average rate or 12 % above the average
France	Introduced in 1935	Preventing abusive practices due to banks' market power Preventing the development of predatory lending to households Balancing the relationship between lenders and borrowers	1.33 × the average percentage rate charged in the previous quarter by credit institutions and finance companies
The Netherlands	Introduced between 1900 and 1939	Controlling illegal financial activities Protecting consumers Curbing risk-taking by some credit providers	Statutory interest rate + 12 %

Source: Faherty M. *et al.* (2017).

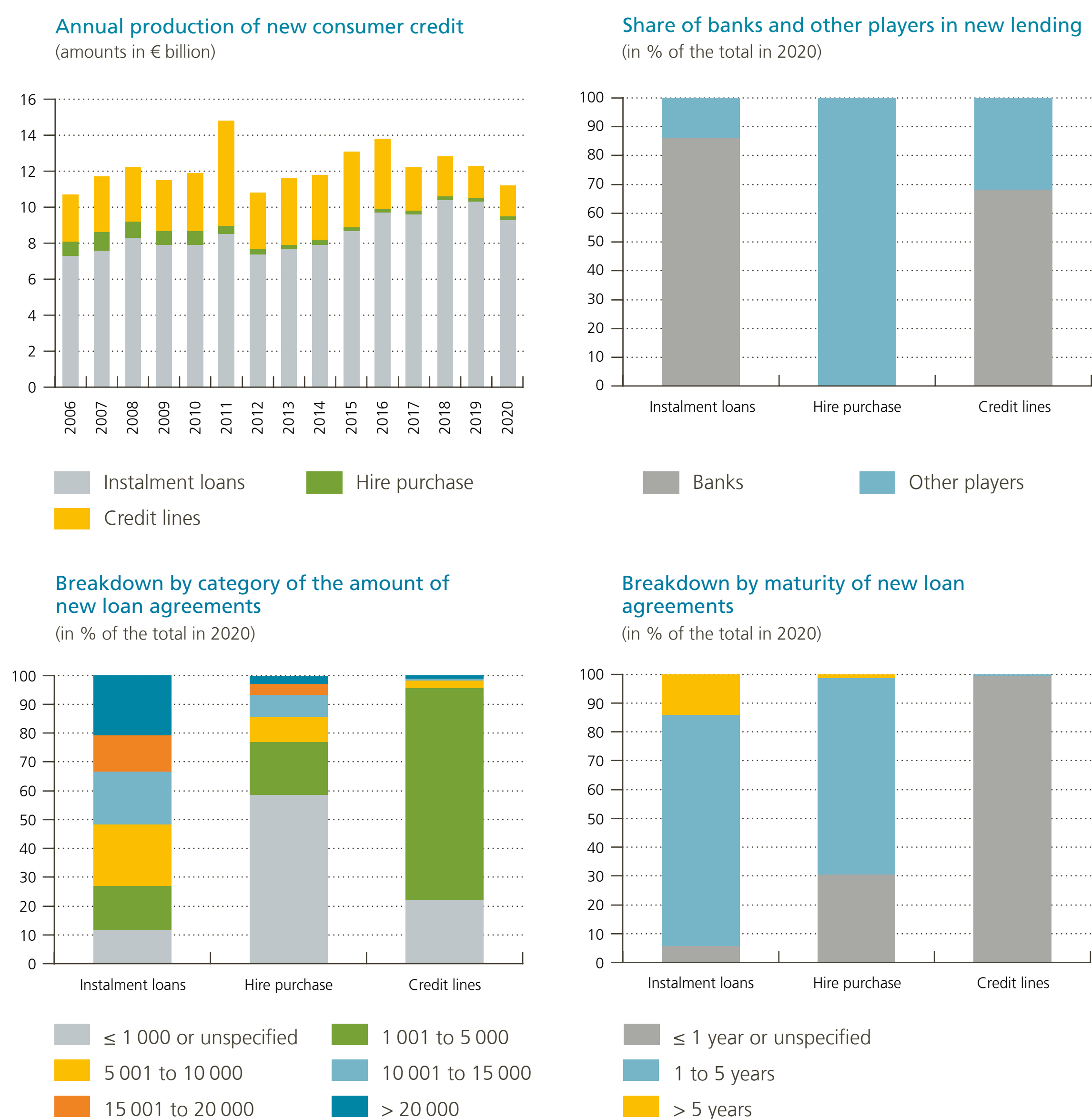
2. The consumer credit market in Belgium

2.1 Amounts and characteristics of consumer loans granted

According to the data recorded in the Central Individual Credit Register, consumer credit amounting to € 11.1 billion was granted in Belgium during 2020. That is lower than the previous year's figure (loans totalling € 12.4 billion), in the context of the COVID-19 crisis which triggered a fall in household consumption expenditure.

Chart 1

Consumer credit trends and characteristics in Belgium



Source: NBB (Central Individual Credit Register).

The great majority of consumer credit consists of instalment loans, i.e. loans part of which must be repaid at set intervals (generally monthly) at the same time as payment of the interest. These loans, which totalled € 9.3 billion in 2020, are usually granted by banks. Although the economic code does not stipulate any specific purpose for this type of product, lenders usually grant these loans mainly to finance a particular good or service, such as the purchase of a car, renovation of a property, or a holiday booking. They most often concern amounts in excess of € 5 000, and most of them have a maturity of between 1 and 5 years.

Hire purchase sales – being confined to a small number of specialist companies linked to retail businesses – represent only a very small proportion of consumer credit, amounting to € 220 million in 2020. Although some of these agreements are concluded for the purchase of a vehicle, more than half concern sums of less than € 1 000. These are usually medium-term loans with a maturity of between 1 and 5 years. That suggests that the "typical" hire purchase involves relatively small monthly payments but over a long period.

Credit lines form the third category of consumer credit. These consist of spare liquidity made available to individuals, practically always for an indefinite period and in most cases by banks via overdraft facilities. In 2020, credit lines had totalled € 1.7 billion, but that figure is only a guide since it concerns "authorised" borrowing. The Central Credit Register does not provide information on the amounts that individuals actually draw. The vast majority of agreements limit authorised drawings to at most € 5 000[1].

2.2 APRs charged by lenders

According to the data from a six-monthly survey conducted by FPS Economy between 2015 and 2019 among a number of players active in the consumer credit market and relating to four "typical" agreements[2], the rates charged on credit facilities are generally the highest, averaging 9.91 % for credit lines with no card and 12.48 % for credit lines with a card. The latter figure is close to the maximum rate (14.50 %, between 1 December 2012 and 1 June 2021) permitted by the regulations for the "typical" agreement considered by the survey, concerning a maximum overdraft of € 1 250.

Many market players also charge rates close or equal to the legal maximum for instalment loans. Half the lenders polled between 2018 and 2019 by FPS Economy stated that they charged an APR of between 8 % and 10 % for a € 10 000 loan (the maximum being set at 10 % from 1 December 2015). However, other lenders reported much lower average rates, in some cases under 5 %.

The last "typical" agreement considered in the FPS Economy survey concerns a hire purchase for a vehicle, the amount borrowed being € 15 000 repayable in 48 monthly instalments. Here, the APRs are much lower than those charged for a € 10 000 instalment loan, probably on account of the existence of collateral, namely the vehicle acquired by the borrower. Moreover, there is presumably keener competition on the car finance market, with some lenders – namely the vehicle vendors – being motivated to offer low interest rates in order to boost their sales. As in the case of instalment loans, the rates charged for this type of agreement also vary widely, with the average APR per lender ranging between 1 % and 5 %. Although drawn from fewer observations, creditors declaring that they are charging higher rates for this type of contract seem to grant larger loans, on average[3].

The scale of the variations is more apparent in aggregate data which encompass all types of credit, such as the data collected by the MIR (Monetary Financial Institutions' Interest Rate) survey. However, that survey only

1 The breakdown of our data (into the following amounts: up to € 1 000, from € 1000 to € 5 000, and from € 5 000 to € 10 000) does not enable us to specifically select amounts of less than € 1 250 (often the limit set when a credit card is issued).

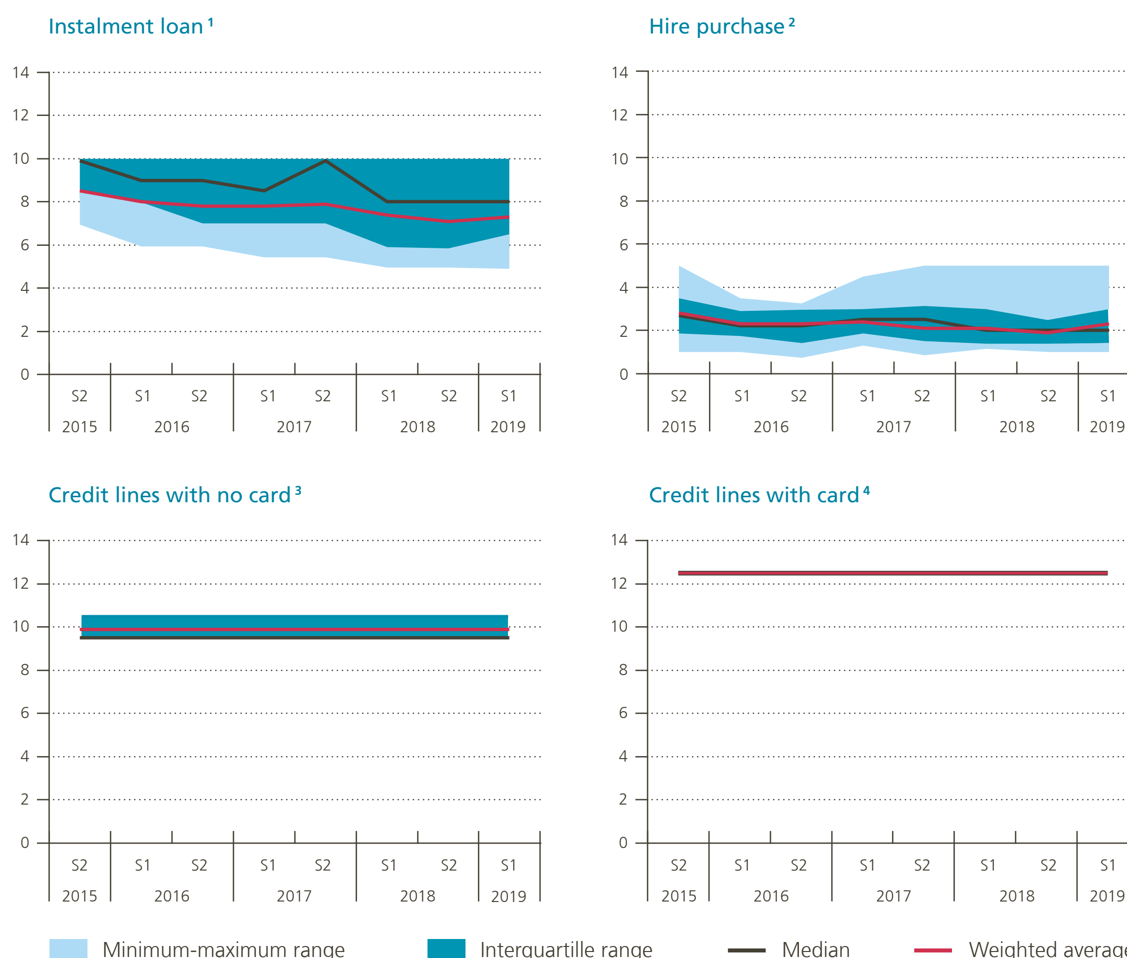
2 In this survey, four "typical" agreements representative of the various forms of consumer credit were selected: (1) car purchase finance as representative of hire purchase (€ 15 000 over a period of 48 months); (2) instalment loan (€ 10 000 over a period of 48 months); (3) credit line with card (€ 2 000 for an indefinite period); (4) credit line without card (€ 1 250 for an indefinite period).

3 No such relationship appears for the other credit types considered in the survey.

Chart 2

Trend in APR on four "typical" agreements

(in %)



Source: FPS Economy (six-monthly survey of annual percentage rates charged on consumer credit).

1 € 10 000 over a period of 48 months.

2 Car finance amounting to € 15 000 repayable over 48 months.

3 € 2 000 for an indefinite period.

4 € 1 250 for an indefinite period.

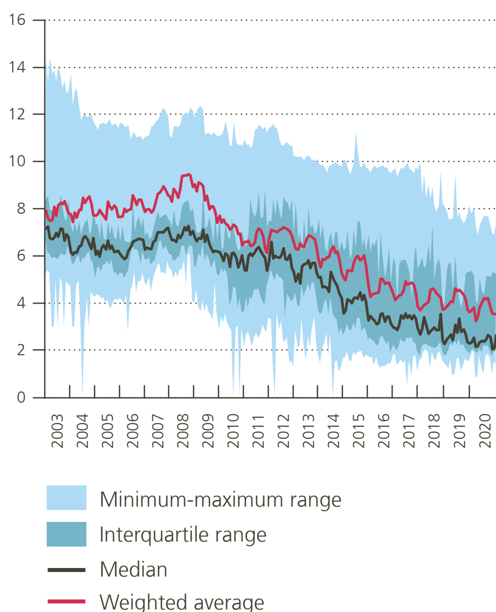
covers Belgian banks, and therefore excludes other companies active in consumer credit (including subsidiaries of traditional banks specialising in that sphere). Examination of the individual data from each institution participating in the MIR survey – not reported here for confidentiality reasons – identifies two factors which may at least partly explain the variations in average APRs. First, since lending rates are generally higher for credit facilities, the average rate on the consumer credit portfolios of banks specialising in this type of product is naturally higher. Next, as chart 3 shows, there is a positive correlation between the banks' average APR and the percentage of riskier loans in their portfolio. In particular, the two banks notable for their high APR are also the ones with a larger proportion of defaulting loans in their portfolio.

Moreover, the average APRs charged on consumer credit are essentially determined by the rates on instalment loans and, on the whole, have mirrored the general trend in lending rates charged by Belgian banks since the 2008-2009 financial crisis. Thus, they declined steadily over a period of more than ten years as a result of the successive easing of monetary policy and the reduction in the banks' funding costs.

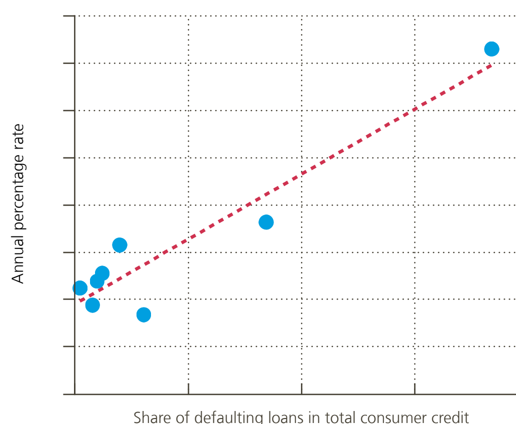
Chart 3

Annual percentage rate charged by Belgian banks and share of defaulting loans in their portfolio
(in %)

Annual percentage rate charged



Annual percentage rate charged and credit risk[1]
(situation at the end of 2020)



Minimum-maximum range
Interquartile range
Median
Weighted average

Source: NBB (MIR survey and prudential reporting).
1 For confidentiality reasons, the scales are not shown on this chart.

3. Higher interest rates on consumer loans: from the borrowers' perspective

The information obtained from the Central Individual Credit Register plus the survey data presented in the previous section are insufficient on their own to gauge the importance of high-interest-rate consumer loans among Belgian households and assess the possible effects of any change in the maximum interest rates. One reason is that they do not provide sufficiently granular information linking the amounts borrowed and the rates charged on each agreement, or information on the debtors.

However, with the data from the HFCS, it is possible to document Belgian consumers' recourse to this type of credit, as well as the characteristics of the borrower households, the purpose of the loans and the associated interest rate levels.

The HFCS is an initiative of the national central banks of the European Union, coordinated by the European Central Bank. In Belgium, the entity responsible for the survey is the NBB, with the cooperation of the National Register and Statbel. We currently have three waves of the survey available (for reference years 2010, 2014 and 2017). The HFCS provides very detailed data on the financial situation of households, including their income, assets and debts. It thus offers information on the distribution of consumer credit among Belgian households.

At present it is the only source in Belgium permitting analysis of the (financial and demographic) characteristics of indebted households.

However, in view of the constraints relating to the sample (around 2 000 households polled in each wave of the survey, less than 20 % of which report having consumer credit), the results need to be interpreted with caution as the margins of error could be relatively large.

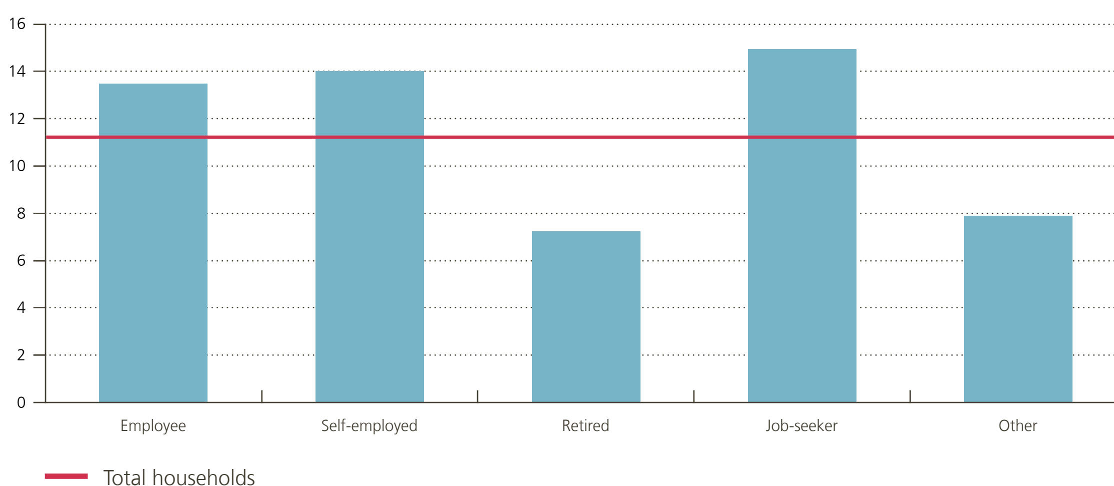
3.1 Level and distribution of consumer credit among Belgian households

According to the HFCS, 11 % of Belgian households had at least one consumer loan in 2017 ; that was lower than the percentage seen in previous waves (18 % in 2010, 12 % in 2014).

Chart 4

Households with at least one consumer loan

(in % ; by activity status of the reference person ; 2017 data)



Source : NBB (HFCS).

In addition, among households in which the reference person was not retired [1], 13 % had at least one consumer loan current in 2017 (compared to 15 % in 2014 and 23 % in 2010).

The median outstanding amount on consumer loans declined between 2010 (€ 16 289) and 2017 (€ 10 819). According to the households, the purposes of these loans were manifold [2]. In 2017, the main reasons for contracting a consumer loan were to purchase a vehicle, to renovate or convert the household's main residence, to repay other consumer credit or to cover current expenses.

1 Debt levels are very low when people retire. At the same time, these households have higher levels of net wealth and relatively lower income levels. Therefore, to avoid an excessive impact on the statistics shown, in this first part of the analysis of the HFCS data, we disregard households in which the reference person is retired.

2 This analysis only takes account of the primary purpose indicated by the household.

In 2017, among the households in which the reference person was not retired, those which had contracted consumer loans[1] had a lower equivalent gross income[2] than households which did not have this type of debt. The differences in terms of net wealth[3] were even more pronounced: the net wealth of households contracting consumer loans was 32 % lower than that of other households.

Furthermore, a higher proportion of households contracting consumer loans had also taken out a mortgage loan (56 %, compared to 52 % for households without consumer credit in 2017). If we consider indebted households on their own, the median ratio between debts and assets – still in 2017 – was more unfavourable for households resorting to consumer credit, but this observation is not constant over time. Conversely, the debt/income ratio was considerably more favourable, with the consumer credit generally concerning smaller amounts.

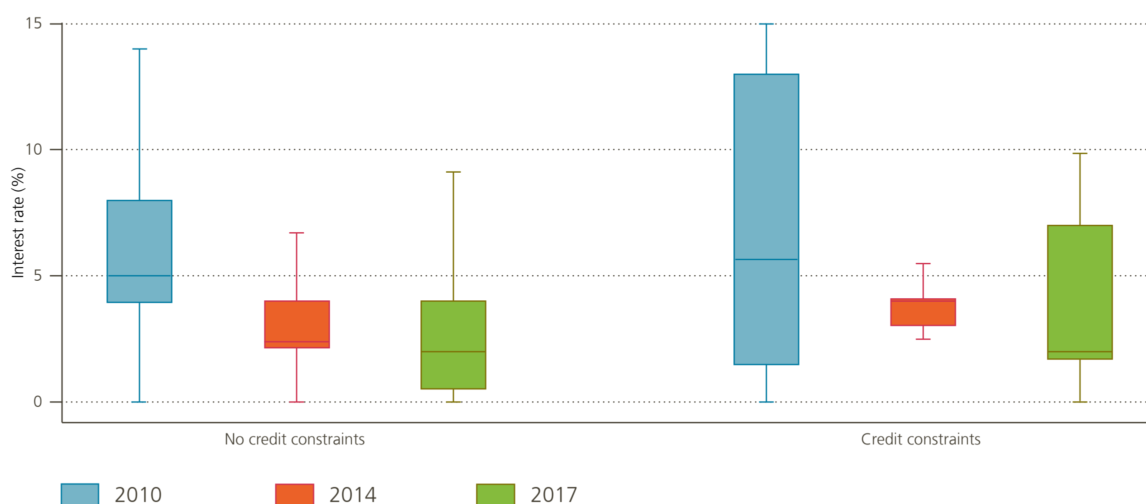
A smaller proportion of households which had contracted consumer loans stated that they could save regularly (40 %, compared to 57 % for households with no consumer credit). A slightly higher percentage of households with this type of loan reported that they faced credit constraints, in that they had not asked for an additional loan because they thought it would not be granted or had asked for at least one loan which had been refused in whole or in part. For these "constrained" households, the top of the rate distribution displayed wider dispersion.

1 Excluding unsecured loans to finance the purchase or construction of real estate.
2 The household's total gross income per member, according to the OECD equivalence scale (1/0,5/0,3): equivalence "means adjusting a household's income for its size, so that we can look at the income of all households on a comparable basis. The needs of a household grow with each additional member but – due to economies of scale in consumption – not in a proportional way". Source: OECD, "Compare your income – methodology and conceptual issues", June 2020.
3 Net wealth comprises all the assets held by the household, both real and financial, minus its debts.

Chart 5

Rates on consumer loans, by household credit constraints

(excluding loans to finance real estate)



Source: NBB (HFCS).
Note: The rectangle contains the values between the lower and upper quartiles. The horizontal line in the rectangle indicates the median. The vertical lines comprise the values between the lower quartile less 1.5 times the interquartile range and the upper quartile plus 1.5 times the interquartile range.

3.2 Distribution of interest rates

In the analysis below, we have disregarded loans mainly used to finance the purchase or construction of a dwelling, in order to stick to the definition of consumer credit in the other data sources. But the HFCS data provide no information on the specific type of loan [1], the year of granting or the lender institution (bank or other). In addition, the reported interest rates do not include charges, and they applied at the time when the household responded to the survey. Thus, in the case of a variable interest rate, the rate may have differed from the rate applied when the loan was granted.

As already mentioned in section 3, interest rates have maintained a downward trend in recent years, and that is also reflected in the rates on consumer loans reported by households in the HFCS. However, the dispersion of the rates has remained significant on loans obtained to pay off debts and cover current expenditure or other purchases. In other words, some households have continued to pay very high interest on such loans, despite the generally shorter loan maturity and lower amounts borrowed.

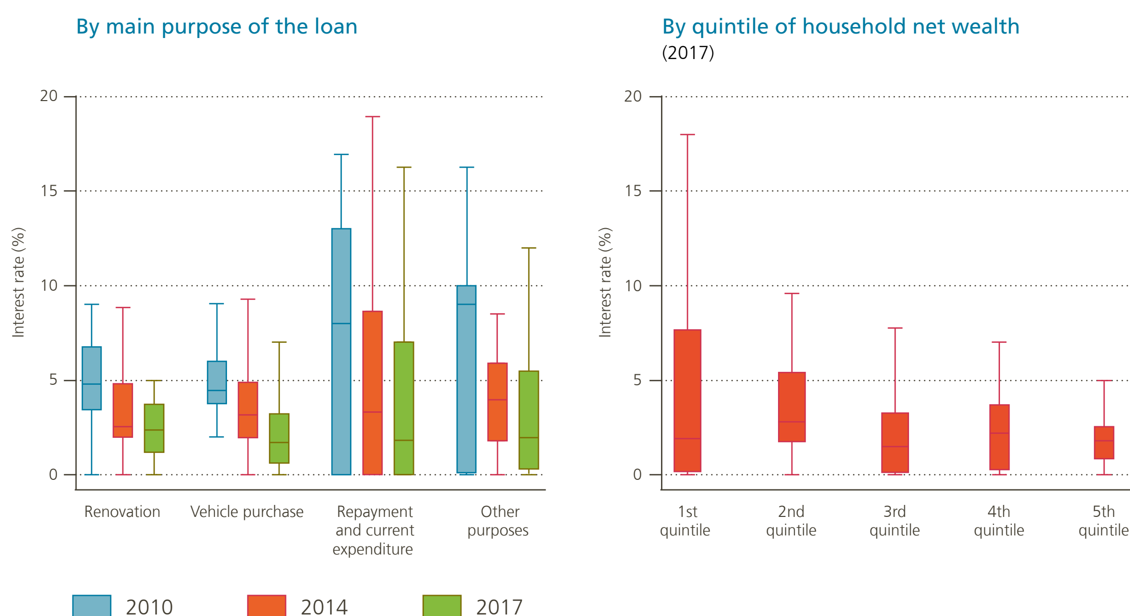
There are significant differences between households according to the purpose of their borrowings. For example, those that had taken out a loan to buy a vehicle had a considerably higher (total and equivalent) income and considerably greater net wealth than households that had borrowed in order to pay off other debts or to finance current expenditure or other purchases. Only 9 % of the latter households stated that they could save regularly, and 22 % said that they were subject to credit constraints (compared to 43 % and 2 % respectively for households taking out a vehicle loan). In general, the less well-off households were much more likely to pay considerably higher interest than the more affluent.

1 Instalment loan or hire purchase. The HFCS does not include data on the interest rates charged on credit lines or credit cards.

Chart 6

Interest rates

(excluding loans for the purpose of the purchase or construction of real estate)



Source: NBB (HFCS).

Note: The rectangle contains the values between the lower and upper quartiles. The horizontal line in the rectangle indicates the median. The vertical lines comprise the values between the lower quartile less 1.5 times the interquartile range and the upper quartile plus 1.5 times the interquartile range.

Table 3

Equivalent gross income and total net wealth per interest rate quintile

(in €, unless otherwise stated; 2017 data)

	Gross income	Net wealth	Share of loans for current expenditure and other purchases [1]	Share of loans for repayment of other credit [1]
			(in %)	
1st quintile	29 055	215 331	1	18
2nd quintile	31 601	196 810	2	2
3rd quintile	32 210	139 973	3	1
4th quintile	31 973	165 120	1	4
5th quintile	31 284	83 420	14	18
Households with no consumer loan	29 182	227 568		
Non-retired households with no consumer loan	34 670	192 335		

Source: NBB (HFCS).

1 In % of loans included in each quintile for which the main purpose was to pay off other consumer loans or to finance current expenditure and other purchases except vehicles.

The main feature of households paying higher interest (i.e. those in the last quintile of the rate distribution) was that they had considerably less net wealth than the others, which confirms the existence of a negative correlation between the rates paid and household wealth. Conversely, there is no clear trend regarding total gross income (not shown) or equivalent gross income.

In median terms, the ratios between total debt and assets, total debt and income, and debt service and income are relatively high for households paying the highest interest rates.

The majority of the loans at higher interest rates (top quintile) were intended to finance the purchase of a vehicle or the renovation of the household's main residence (34 % and 21 % respectively), followed by loans granted to repay other consumer credit (18 %) and those covering current expenditure or other purchases (14 %). This last type of loan is, proportionally, more heavily represented in the top quintile of the interest rate distribution (they only represent 1 % of the loans granted at the lowest rates – first quintile).

Regardless of purpose, the loans at the highest interest rates had relatively long maturities (over-representation of loans with a maturity of between five and ten years). However, in 2017, 13 % of loans included in the quintile with the highest interest rates had a maturity of between 2 and 3.5 years, and 18 % between 3.5 and 5 years.

In 2017, 54 % of households had a credit line or overdraft, a higher share than in previous years. Among them, only 12 % had an outstanding balance (potentially incurring interest and other charges) which, on average, amounted to € 1 945 (the median conditional amount was lower, at € 600). The share of households with an open balance was higher among the unemployed (11 %) and lower for households where the reference person was retired (4 %). All in all, households that could access a credit line or overdraft were in a better financial position than those that could not (higher income and net wealth, more likely to be owner of their main residence). But among them, those with an outstanding balance were clearly worse off than those who had not incurred any actual debt through the available credit facilities. While the HFCS does not provide information about the rates charged for credit lines and overdrafts, section 2 of this article shows that the rates offered by creditors are very close to the authorised maxima, with very little variation. Households with outstanding balances are also more likely to pay higher rates on other consumer credit.

3.3 How do changes in maximum rates affect the financial situation of households ?

In 2017, according to the HFCS data, the upward dispersion of interest rates was greater for loans intended to repay other consumer credit and to finance current expenditure or other purchases. This type of borrowing made up almost one-third of the loans associated with the highest interest rates. In general, households contracting this form of credit had significantly lower incomes and net wealth than households which borrowed for other purposes or had not contracted any consumer loans.

It is therefore likely that any change in the maximum APRs on loans would have a more direct impact on these household categories, which are more vulnerable in terms of financial security. Any reduction in these maximum rates would mean either that these households could borrow at more moderate interest rates or that they would be denied access to credit if the lenders consider that lower rates do not cover the risks. Conversely, a rise in these maximum rates, while providing incentives for lenders to loan to riskier consumers, could also overburden the borrowers. The question of a possible impact on the supply of riskier loans, especially in the event of a reduction in the maximum rates, is examined in the next section.

4. Sensitivity of lenders' profitability and credit supply to changes in maximum rates

A change in the maximum APRs on consumer credit could affect lenders in various ways. As a rule of thumb, if business remains the same, a reduction in maximum APRs could erode the generation of interest income. If consumer credit makes up a significant share of a lender's business, that could lead to a deterioration in his general profitability. A lender might equally consider that the new maximum rates no longer allow him to set his tariffs so as to cover various costs (risk of non-repayment, provision of liquidity to finance the loan, capital requirements, etc.) while still generating an adequate profit margin. That could cause lenders to cease offering certain types of loan. If consumer credit represents a significant part of a lender's activities, that could have a major impact on his business model.

If such effects – on profitability and business models – are significant for a large number of lenders, that could potentially threaten financial stability. In terms of the supply of financial services, it should be borne in mind that, even if some lenders were to withdraw from (part of) the market in the event of a significant decline in maximum rates, other credit providers ready to accept lower maximum rates might take over their market shares.

The next sections address the impact of a possible reduction in the maximum APRs on bank lenders and non-bank lenders, and on the stability of the financial system and the supply of financial services.

4.1 Bank lenders

As mentioned in section 3 above, the major part of the Belgian consumer credit market (especially the instalment loan segment) is covered by the banking sector, either directly or indirectly via specialist subsidiaries. Among the Belgian banks operating on the Belgian consumer credit market, there are evidently significant differences, notably as regards the share of consumer credit in their total assets and interest income.

For most banks, Belgian consumer credit represents only a small part of their business. The implicit interest rates (calculated by comparing the interest income on consumer credit with the stock of consumer credit) also show relatively low average levels for the majority of banks. That suggests that the share of the banks' business for which the rates charged are close to the maximum levels is small. A reduction in the maximum APRs is therefore unlikely to have a significant effect on the profitability and business model of these institutions.

Differences in the average implicit interest rate between lenders mainly reflect differences in the consumer credit portfolio mix. The rates offered in fact vary widely between, for example, a loan for the purchase of a car, a credit line or a personal loan for an unspecified purpose (see section 3). Interest rate differentials may also reflect a difference in the average quality of the portfolio.

For a small number of bank lenders, Belgian consumer credit represents a more significant part of their business (up to one-third of their total assets). Some of them operate on the private banking market. For those banks, consumer credit forms part of their general customer relationship management and the average interest rates are relatively low. The rules on the maximum APRs are therefore unlikely to have any significant impact. For a similarly limited number of players (though their cumulative share of the market is estimated at around 10 % of consumer credit in Belgium), the implicit interest rates are on the whole higher. That reflects a generally larger proportion of credit lines in their consumer credit activities. It may also indicate that the share of instalment loans for which the rates charged are close to the current maximum rates is greater than for the majority of banks. Therefore, a reduction in the maximum APRs could have an impact on those institutions. However, it should be noted that some of those banks belong to a Belgian banking group in which consumer credit represents a much smaller part of the business.

4.2 Non-bank lenders

A large percentage of non-bank lenders feature a significant proportion of hire purchase agreements (e.g. in the mass retail sector) or have links with the automotive sector. In these segments of activity, the rates offered are usually well below the maximum APRs (see section 3). A reduction in the maximum APRs is therefore unlikely to have any significant impact.

In contrast, other lenders typically have a higher percentage of credit lines and instalment loans for various purposes. The rates that these credit providers offer, particularly on credit lines and instalment loans for no specified purpose, are generally close to the maximum APRs (see section 3). It follows that a reduction in the maximum APRs could have an effect on these institutions.

4.3 Potential impact of a reduction in the maximum APRs on financial stability and the supply of financial services

A reduction in the maximum APRs charged on consumer credit is likely to have little impact on financial stability. For most lenders, such a change is unlikely to have any significant impact. However, a change in the maximum permitted APRs on consumer credit could have an impact on a small number of lenders, but their market share in terms of total banking assets or the supply of credit and financial services in Belgium is marginal.

If we consider the supply of consumer credit in Belgium on its own, the share of these lenders potentially affected by a change in the maximum APRs is more significant, especially in the case of credit lines and instalment loans for an unspecified purpose. In these specific segments a reduction in the supply cannot be ruled out. That also applies to the specialist subsidiaries of banking groups in which the supply of certain types of consumer credit could be reduced. It should nevertheless be noted that scope for substitution could (partially) offset such a negative effect on lending.

5. Beyond the APR: some additional considerations

The price reflected by the APR is only one dimension of a consumer loan agreement. The literature addresses other issues relating to this type of credit which likewise merit attention. Some of those issues are mentioned in the following paragraphs.

According to the FSUG report, Belgium is one of the ten largest consumer credit markets in the European Union, along with Germany, France and the Netherlands, among others. An efficient consumer credit market is deemed to benefit households, businesses and sellers of goods and services, and to stimulate economic growth. But if credit creates an excessive debt burden which becomes unsustainable, that can have a significant impact on some categories of households and lenders, because although consumer credit represents only a small part of household debt, its influence on the household budget may be greater if it is granted without the necessary safeguards (BEUC, 2019).

A study by the European Commission (EC, 2017) estimated that, in 2016, the financial detriment that consumers suffered via the market in loans and credit cards could be put at € 12.8 billion. The main problems affecting the consumer credit market concerned the cost of credit obtained at very short notice (particularly via mobile applications, speedy but expensive because of the high estimated default risk), poor use of consumer credit (poor matching between the purpose of the loan and the type of credit offered), the proliferation of marketing channels encouraging borrowing, inadequate assessment of borrower solvency, and inadequate contract and pre-contract information, particularly regarding the credit terms and conditions, penalties and early repayment (EBA, 2019[1]).

More particularly in the case of very short-term credit ("payday loan" type) in France, for instance, this type of credit concerning modest sums (€ 200 to € 600) is negotiated on loan platforms on a peer-to-peer basis, circumventing the national legislation. Companies operating on this segment do not generally assess the consumers' borrowing capacity correctly and do not include any APR in their offers. In the Netherlands, this type of loan is called "flash credit" or "mini loan" (*flitskrediet* or *minilening*). *Minilening* providers must have a licence and are subject to the regulator's supervision. The maximum permitted charges on these agreements come to 10 % on an annual basis. Owing to the existence of this strict regulation, the Netherlands is no longer attractive for the payday loan market; some credit providers based in other Member States therefore circumvented the law by making offers on the internet. In response, the advertising of these loans was banned (Cherednychenko and Meindertsma, 2019).

There is also a recurring problem with the cost of insurance linked to the loan (cross selling) which is not generally taken into account in the APR (because the insurance is optional and depends on the borrower's personal situation). One way of remedying this would be to ask lenders to offer the consumer two APRs (with and without the premiums for such insurance). In addition, the sale of this type of insurance, deemed to protect consumers facing circumstances that prevent repayment of their loan (sickness, disability, unemployment, etc.), seems to have caused a lot of trouble (particularly a lack of clarity over whether or not certain clauses apply) in a number of European countries (including Germany, Belgium and France) (BEUC, 2019), causing some countries to pass legislation to enhance transparency and disclosure in this sphere.

Another aspect of the question concerns the current context of low interest rates, encouraging the granting of consumer credit. However, the risk that future interest rate rises may lead to payment defaults and a rise in excess debt levels is particularly significant the bigger the share of variable rate loans, i.e. loans indexed to benchmarks such as Euribor. The low interest rate environment may have led consumers to contract more expensive loans while ignoring the effects of a potential interest rate rise. If rates go up, that could have adverse implications for the financial system as a whole if the portfolio of consumer loans in some institutions is of poor quality (EBA, 2019).

1 This study only considers loans by credit institutions.

Finally, excess debt often goes hand in hand with inadequate or underdeveloped (digital) financial literacy among consumers. That concerns in particular a lack of knowledge about the methods of calculating product prices or interest rates, a limited understanding of the terms and conditions associated with loans, ignorance of basic financial terminology and a lack of understanding of the risks inherent in financial products such as consumer credit (EBA, 2019). Research in the United States and Germany also shows that financial institutions offer products on far less favourable terms to persons with a lower (average) level of financial literacy (Bucher-Koenen *et al*., 2021; Ru and Schoar, 2019). In that regard, the most vulnerable groups are poorly educated consumers, young people, the unemployed, and the elderly and migrants (EBA, 2019). To remedy this problem, some countries have programmes offering financial education right from primary school or providing training for the elderly, and for consumers in vulnerable groups.

Conclusion

The consumer credit market in Belgium is diversified and comprises several categories of lenders and loans to meet the seemingly varied needs of households. Analysis of the available data shows that most of these loans are provided at rates far below the maximum APRs legally established. Nonetheless, it is possible to identify two market segments where that is less the case. First, on the supply side, this concerns instalment loans for an unspecified purpose and credit lines, on which interest rates are very uniform, both over time and for different lenders, and close to the permitted maximum. Next, on the demand side, it would mainly concern financially vulnerable borrowers, who seem to be the ones more often having to pay higher rates.

From the lenders' viewpoint, changes in the statutory maximum APRs should have little impact on financial stability, but they could nevertheless affect the commercial margins where the rates charged are close to the maximum. However, the data available do not enable us to estimate the scale of that effect on the profitability of the various types of lenders. Yet we should stress that, if the margins on riskier loans – such as unsecured loans, loans for an indefinite period or loans to households considered vulnerable – were to be reduced, that could hinder some households' access to traditional credit channels and prompt them to turn to alternative sources of finance (subject to little or no regulation).

In that connection, the experience of the Netherlands where foreign entities target customers on the fringes of the credit market is interesting, as it shows that regulations can have an impact on access to finance for certain categories of persons and, at the same time, increase the risks of excess debt, especially in groups with low financial literacy. Measures intended for households facing credit constraints could therefore be envisaged. The market entry of lenders not subject to national regulation also highlights the need for uniform legislation throughout the European Union.

That said, it is equally possible that, despite the cut in the commercial margins on the loans concerned, those loans may remain viable, even for the riskiest market segments. In that case, the debt burden of the most vulnerable households would be eased. Also, supply could shift to more efficient lenders (with more scope to reduce their margins).

Finally, it would likewise be useful to assess the competition on the various segments of the consumer credit market so as to estimate the impact of any change in the statutory maximum rates, particularly for the market segments where tariffs have not kept so closely to the general (downward) trend in interest rates and financing costs.

Bibliography

Bucher-Koenen, T., A. Hackethal, J. Koenen and C. Laudenbach (2021), *Gender differences in financial advice*, SAFE Working Paper 309
Gender Differences in Financial Advice by Tabea Bucher-Koenen, Andreas Hackethal, Johannes Koenen, Christine Laudenbach: SSRN

Bureau européen des unions de consommateurs (BEUC) (2019), *Review of the Consumer Credit Directive. BEUC position*
https://www.beuc.eu/publications/beuc-x-2019-019_review_of_the_consumer_credit_directive.pdf

Cherednychenko O. and J. Meindertsma (2019), "Irresponsible lending in the post-crisis era: is the EU consumer credit directive fit for its purpose?", *Journal of Consumer Policy*, 42, 483-519
https://link.springer.com/content/pdf/10.1007/s10603-019-09421-4.pdf

European Banking Authority (2019), *EBA Consumer Trends Report 2018/19*
https://www.eba.europa.eu/sites/default/documents/files/documents/10180/2551996/75e73a19-d313-44c9-8430-fc6eca025e8b/Consumer%20Trends%20Report%202018-19.pdf?retry=1

European Commission (2017), *Study on measuring consumer detriment in the European Union*
https://ec.europa.eu/info/sites/default/files/consumer-detriment-study-final-report_en.pdf

Faherty M., O. McCarthy and N. Byrne (2017), *Interest rate restrictions on credit for low-income borrowers*
https://cora.ucc.ie/bitstream/handle/10468/7172/IRR_Research_Report_Final_Feb_2018.pdf?sequence=1&isAllowed=y

Financial Services User Group (FSUG) (2019), *Responsible consumer credit lending. FSUG opinion and recommendations for the review of the Consumer Credit Directive*
https://ec.europa.eu/info/sites/default/files/business_economy_euro/banking_and_finance/documents/fsug-opinions-190408-responsible-consumer-credit-lending_en.pdf

Ru, H. and A. Schoar (2019), *Do Credit Card Companies Screen for Behavioral Biases*?
https://ssrn.com/abstract=2795030