Decision by the Board of the Financial Supervisory Authority on the application of macroprudential instruments

At its meeting on 29 June 2020, the Board of the Financial Supervisory Authority (FIN-FSA) decided that the countercyclical capital buffer (CCyB) requirement, as referred to in chapter 10, section 4 of the Credit Institutions Act (610/2014), will remain at 0%. The FIN-FSA Board also decided that the maximum loan-to-collateral (LTC) ratio, as referred to in chapter 15, section 11 of the Credit Institutions Act, will be adjusted and brought back to the statutory standard level of 90%. With the decision of 19 March 2018, the Board lowered the maximum LTC ratio for residential mortgage loans other than first-home loans by 5 percentage points.

The FIN-FSA Board also repeals its decision of 28 March 2018, taken in accordance with section 65e of the Act on the Financial Supervisory Authority, on the reciprocation of the systemic risk buffer of 1.0% imposed by Eesti Pank on 30 June 2016.

In the current exceptional circumstances, it is important that credit institutions carefully assess the housing loan applicant’s financial margin in accordance with the FIN-FSA’s recommendations.

Justification for the decision

Countercyclical capital buffer requirement

The coronavirus pandemic, which spread rapidly around the world in the early part of the year, is having significant negative effects on global and Finnish economic developments. The economic recession is also weakening the conditions for financial stability.

The informational value of the primary risk indicator for setting the CCyB requirement – the private sector credit-to-GDP gap – is very limited in the current circumstances. GDP is expected to contract sharply in the near future, while the change in the credit stock is likely to be smaller due to growth in the private sector’s other financing needs in spite of a simultaneous decrease in investment.

At the end of 2019, the primary risk indicator was heavily negative, in line with previous figures. The effects of the coronavirus pandemic are not yet reflected in the supplementary macroprudential indicators. An exception is the financial market stress indicator, which rose sharply in March 2020. The rise of the stress indicator and the prevailing exceptional circumstances support the decision to keep the CCyB rate at 0%.

Maximum loan-to-collateral ratio

The maximum LTC ratio for residential mortgage loans restricts the amount of a residential mortgage to 90% at most (in the case of a first home purchase, to 95% at most) of the current value of collateral posted at loan approval. In order to limit any exceptional build-up of risks to financial stability, the Board of the FIN-FSA may decide to reduce these maximum amounts by no more than 10 percentage points. In addition, it may decide to restrict the taking into account of any other collateral security except real security in calculating the LTC ratio.

On 19 March 2018, the FIN-FSA Board lowered the maximum LTC ratio for residential mortgage loans other than first-home loans by 5 percentage points to curb household indebtedness. The decision entered into force on 1 July 2018.

The corona pandemic has had a significant impact on the real economy. The uncertain economic situation has led to a reduction in home sales and the volume of residential mortgage loans granted to households. The stock of households’ housing finance relative to household income is estimated to increase due to decreasing household incomes. The housing market is showing no signs of overheating. Instead, in an environment of weak macroeconomic developments, housing market activity may still slow significantly and there is also a possibility that house prices will fall throughout Finland. Nevertheless, housing market developments may continue to diverge between growth centres and the rest of Finland.

It is justified to bring the maximum LTC ratio for residential mortgage loans other than first-home loans back to the base level to support the housing market and the real economy in the current exceptional circumstances. Over the past year, about three quarters of the euro volume of new residential mortgage loans have been housing loans other than first-home loans. Relaxing the LTC ratio for these loans could increase housing demand and total demand compared with a situation where the tighter LTC ratio would continue to apply. Supporting demand can contribute to offsetting the contraction in house sales and the economy and thus alleviate the threat of an exceptional build-up of risks to financial stability. As a whole, however, the impact of the measure will be fairly limited in the current situation.

The level of household indebtedness is still record high and may rise even further in the current circumstances, as many households have made use of interest-only periods for their housing loans. The corona crisis has led to lay-offs and redundancies, which may weaken the debt servicing capacity of indebted households. The adjustment of the maximum LTC ratio will not affect the debt burden of households that have already taken out a mortgage loan, but may reduce potential disruption to indebted households and the related effects. Bringing the maximum LTC ratio back to the standard level is justified in order to support the stable functioning of the housing market.

The Board of the FIN-FSA decided to lower the maximum LTC ratio in March 2018 because household indebtedness was considered to constitute an exceptional risk to financial stability, the growth of which needed to be contained. High household indebtedness remains a key structural vulnerability that needs to be addressed in the longer term by means of the maximum LTC ratio and other macroprudential instruments. In the current situation, however, in order to ensure financial stability, the need to counter the above-mentioned cyclical risks is greater than the need to reduce the structural risks associated with household indebtedness. Therefore, bringing the maximum LTC ratio back to the base level is justified.

In the current uncertain situation, it is important that credit institutions carefully assess housing loan applicants' financial margins in accordance with the FIN-FSA's recommendations. A careful solvency assessment reduces the credit risk associated with new residential mortgage loans. Strong disruptions in the housing market may nevertheless have an adverse effect on the consumption behaviour of heavily indebted households.

Repeal of the decision concerning the Estonian systemic risk buffer

On 28 March 2018, the FIN-FSA Board decided, in accordance with section 65e of the Act on the Financial Supervisory Authority, to reciprocate the systemic risk buffer of 1% imposed by Eesti Pank on 30 June 2016. The Estonian measure was reciprocated by applying the systemic risk buffer requirement referred to in chapter 10, section 4 of the Credit Institutions Act to balance sheet items and off-balance sheet commitments located in Estonia of credit institutions authorised in Finland, in compliance with the Recommendation of the European Systemic Risk Board (ESRB) of 24 June 2016.

Due to the coronavirus pandemic, Eesti Pank decided on 6 April 2020 to lower the systemic risk buffer of 1.0% temporarily to 0.0% as of 1 May 2020. On 2 June 2020, the ESRB decided to remove the systemic risk buffer of 1% imposed by Eesti Pank from the list of measures included in the ESRB Recommendation on the assessment of cross-border effects of and voluntary reciprocity for macroprudential policy measures (ESRB/2015/2).

Following the decisions of Eesti Pank and the ESRB, the FIN-FSA Board repeals its decision of 28 March 2018 concerning the systemic risk buffer imposed by Eesti Pank.