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DVR: 0000078

GZ. BMF-160300/0008-III/B/2016

**Ref:** Views of the Austrian authorities on the Warning of the ESRB on medium-term vulnerabilities in the residential real estate sector of Austria

Dear Mr. Mazzaferro,

From the perspective of the Austrian authorities the warning which the ESRB has decided to issue is not justified. The ESRB assessment hinges on divergent views regarding the expected sufficiency of the Austrian policy stance regarding the collateral valuations and household indebtedness. The Austrian Authorities fully share the ESRB's view that real estate related risks in Austria should be carefully monitored.

However, we disagree with the ESRB's two main arguments in favour of a risk warning for Austria for the following reasons:

- 1<sup>st</sup> ESRB argument: Austrian real estate prices have been rising quickly and appear to be above fundamentals, especially in Vienna: Though in fact considerable price increases have occurred recently in Austria, it is important to emphasize that residential price increases in Austria started from a comparatively low level. The ESRB, overall, puts in its assessment too much emphasis on the change of variables and neglects the low levels of core variables in Austria (i.e. house prices, loan-to-value and debt-service-to-income ratios, affordability of housing). Moreover in Vienna, where house price increases had been particularly strong in recent years, only about 18% of households are owner occupiers and only 6% of households have



mortgage debt according to microdata evidence (Household Finance and Consumption Survey, HFCS). These low home ownership rates, in conjunction with a well-developed rental market with a high share of subsidized housing, limit the incentive and need for more vulnerable households to become homeowners and thus limit systemic risks caused by possible fluctuations or overvaluations of the collateral.

- 2<sup>nd</sup> ESRB argument: Mortgage lending has picked up in Austria. Additionally, an OeNB survey indicates that real estate lending standards have deteriorated recently and the share of borrowers with elevated debt to income and loan to value ratios has been increasing. The Austrian Authorities are of the view that the ESRB's assessment rests too heavily on the results of this one non-representative OeNB survey among just six banks. The OeNB has flagged to the ESRB that this survey has to be used with caution since the sample is both quite small and has changed over time. Additionally, variations between banks in the sample are high. That is also why the OeNB has decided against publishing the survey's results for the time being. Furthermore, another OeNB survey (the Bank Lending Survey) shows a somewhat different picture in this respect, indicating no major change of lending standards in recent quarters.  
The Austrian Household Finance and Consumption Survey (HFCS) data show that households that have mortgages also have wealth and income far above the median, with correspondingly good debt servicing capabilities. It also shows that the effects of strong house price declines on potential losses given default of vulnerable mortgage holders would be rather limited.  
Finally, it is important to bear in mind that the aggregate indebtedness of the Austrian household sector is comparably low and has not increased in recent years, thus further reducing systemic risk. In Q1 2016, for example, the household-debt-to-GDP ratio stood at 50.8% while it was 52.2% a year before and around 54% five years ago. Within the EU only new member states (as well as Italy) exhibit lower household debt-to-GDP ratios. Also, the share of mortgage loans in Austria is comparatively low relative to GDP and relative to banks' tier 1 capital.

In addition, the ESRB warning does not take into account recent policy actions in Austria addressing this issue. On September 23rd, 2016, the Austrian authorities introduced additional measures to prevent the emergence of residential real estate related systemic

risks in Austria. These new measures are comprehensive, broad based, and expected to be sufficient:

- They address the collateral, the household, and the banking stretch.
- They were agreed upon in the Financial Market Stability Board and are backed by the Oesterreichische Nationalbank, the Financial Market Authority, the Ministry of Finance and the Fiscal Council.
- They were communicated not only to the banks, but also to the general public.
- They encompass criteria of sustainability on three ratios (loan-to-value, debt-service-to-income, and debt-to-income) as well as on risk management practices and risk pricing.
  - The Financial Market Stability Board (FMSB) calls for conservative loan-to-value ratios to ensure that there is sufficient buffer to avoid a collateral stretch in the face of falling real estate prices.
  - Furthermore, it requires banks to consider debt-service-to-income and debt-to-income ratios in their risk management to address a potential household stretch: households must be able to service debt even under stress scenarios such as reductions of household income and unexpected payment obligations. The debt service capacity of households must also be resilient to plausible interest rate shocks leading to sharp increases of debt service obligations.
  - Finally, mortgage pricing must be risk adequate and reflect credit risk as well as the costs of liquidity and capital.
- The FMSB will continue to closely monitor the sustainability of lending standards in real estate lending. On the basis of improved reporting, it may in due course specify in more detail the criteria outlined above and issue recommendations if the need arises.

Furthermore, in the face of recent real estate market and mortgage loan developments the Financial Market Stability Board has issued the advice to the Federal Minister of Finance to take preventive action and expand the macroprudential toolbox by providing the legal instruments of imposing limits on the loan-to-value ratio, the debt-to-income ratio or the debt service-to-income ratio in new lending . The Austrian authorities are currently preparing a draft law in order to establish the legal basis for the aforementioned instruments.

Summing up, the Austrian authorities are fully convinced that the ESRB has not based its assessment on a balanced view of the empirical evidence. From the view of Austrian Authorities the continuation of the careful monitoring of real estate developments is of the utmost importance.

Für den Bundesminister:

A handwritten signature in blue ink, appearing to be a stylized 'M' or a similar character, positioned below the text "Für den Bundesminister:"