21 February 2022
ECB-PUBLIC

ESRB
European Systemic Risk Board
European System of Financial Supervision

Assessment Team on national macroprudential measures

Background note on a measure taken in Belgium pursuant to Articles 133 and 134(5) of the Capital Requirements Directive

Introduction

On 11 January 2022 the European Systemic Risk Board (ESRB) Secretariat received a formal notification from the Nationale Bank van België/Banque Nationale de Belgique on the activation of a new systemic risk buffer (SyRB) rate, pursuant to Article 133 of the Capital Requirements Directive (CRD)[1]. The proposal is to introduce a SyRB of 9%, for banks using the internal ratings-based approach, on all retail exposures to natural persons secured by residential real estate located in Belgium. The proposed measure will be in place from 1 May 2022, and the measure currently in place, based on Article 458(2)(d)(iv) of the Capital Requirements Regulation (CRR)[2] and relating to a risk weight add-on and multiplier for mortgage loans of IRB banks, will not be extended beyond that date.

As the SyRB rate exceeds 5% for real estate exposures, the ESRB must, within six weeks of receipt of the notification, issue an opinion as to whether the SyRB is deemed appropriate, pursuant to Article 133(12) CRD. Furthermore, the SyRB applies in combination with the O-SII buffer – the buffer applicable to other systemically important institutions – in Belgium and is cumulative with the O-SII buffer rate. Pursuant to Article 131(15) CRD, as the sum of the systemic risk buffer rate and the O-SII buffer rate exceeds 5%, the ESRB must, within six weeks of receipt of the notification, issue an opinion as to whether the O-SII buffer is deemed appropriate as set out under Article 131(5a) CRD. The two aspects are dealt with in a single opinion, to which this note serves as background. The European Commission must adopt an act authorising the adoption of the proposed SyRB within three months of receipt of the notification if it is satisfied that the SyRB does not entail disproportionate adverse effects on the whole or parts of the financial system of other Member States, or of the European Union as a whole, that form or create an obstacle to the proper functioning of the internal market.

In order to avoid leakages and regulatory arbitrage following the introduction of the proposed measure, the Nationale Bank van België/Banque Nationale de Belgique notified the ESRB on 11 January 2022, in line with Article 134(5) of the CRD, of a reciprocation request concerning the measure under Article 133 CRD. The reciprocation request will be dealt with in a separate note referring to cross-border and internal market effects.

The role of the Assessment Team is to prepare a draft opinion on the appropriateness of the macroprudential policy measure of which the ESRB has been notified, with regard to relevant requirements under the CRD and

[1] Directive No 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

[2] Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013, p. 1).

the CRR, from a macroprudential and financial stability perspective. Pursuant to Article 133(8) CRD, the SyRB should not entail disproportionate adverse effects on financial stability in other Member States, or the EU as a whole, that form or create an obstacle to the proper functioning of the internal market. It should be reviewed at least every second year and it should not address risks covered by Article 130 or Article 131 CRD. The assessment draws extensively on quantitative and qualitative information provided by the Nationale Bank van België/Banque Nationale de Belgique and on discussions within the Assessment Team and with the Nationale Bank van België/Banque Nationale de Belgique.

Description of the proposed measure

The proposed measure consists of the activation of a new sectoral SyRB of 9% on IRB retail exposures to natural persons secured by residential real estate located in Belgium. It applies to nine domestically established Belgian banks, of which two are subsidiaries of entities established in another EU Member State. According to the Nationale Bank van België/Banque Nationale de Belgique, microprudential models are not able to capture potential systemic risks for these exposures, as no significant increase in defaults occurred over the period they take into account. It thus considers that a macroprudential measure is necessary for all IRB retail exposures to natural persons secured by residential real estate located in Belgium. The large majority of residential real estate loans in Belgium are granted by IRB banks (95%). The activation of the proposed measure is based on the following indicators: house prices, including indicators of price valuation; the household debt-to-income ratio; mortgage loan growth; credit standards (loan-to-value r(LTV) ratios, debt service-to-income (DSTI) ratios, mortgage loan maturities, banks' interest rate margins, etc.); and risk weights.

The proposed measure is intended to replace the current measure under Article 458 CRR, which expires on 30 April 2022. The latter mitigates risks from IRB retail exposures to natural persons secured by residential real estate located in Belgium by imposing stricter risk weights,[3] thereby complementing the Nationale Bank van België/Banque Nationale de Belgique's prudential expectations on LTV limits. The measure under Article 458 CRR consists of two components: 1) a risk weight add-on of 5 percentage points for IRB banks' retail exposures secured by real estate; and 2) a risk-sensitive risk weight multiplier, calculated as 33% of the average microprudential risk weight on the residential mortgage portfolio. It was first activated on 1 May 2018 and was extended twice, with the last extension in 2021 for the period until 30 April 2022. The aim of the measure was to address the low level of risk weights used to calculate capital requirements for residential real estate exposures in microprudential models in order to increase the resilience of the banking system. The risk weights applied by Belgian IRB banks to residential real estate exposures are among the lowest for EU countries; however, the measure has ensured that higher risk weights are applied.

The scope of the proposed measure is identical to that of the current measure under Article 458 CRR and should have a very similar effect at the sectoral level. The total impact of the sectoral SyRB on IRB banks' Common Equity Tier 1 (CET1) capital is estimated by the Nationale Bank van België/Banque Nationale de Belgique to be the

[3] See the **Opinion of the ESRB of 18 February 2021** regarding Belgian notification of an extension of the period of application of a stricter national measure based on Article 458 of Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms (ESRB/2021/1).

same as that of the current measure. Given that the design of the two measures differs somewhat, the impact on individual institutions' CET1 buffer requirements will be slightly different, with the largest effect for a mid-sized bank with a solid solvency position. The reason for activating a sectoral SyRB to replace the current measure is the need, following the introduction of sectoral SyRBs via the CRD V, to continue to respect the pecking order of macroprudential measures, according to which measures under Article 458 CRR should be activated only when no other measure is available to address the risks as effectively.

The new sectoral SyRB will be activated on 1 May 2022. The new buffer is expected to remain in place until the underlying risks subside, or the identified systemic risk materialises and banks start to recognise substantial losses owing to rising defaults or significant debt restructuring. In such circumstances, the Nationale Bank van België/Banque Nationale de Belgique will consider the immediate withdrawal of the proposed measure.

Risks addressed through the proposed measure

The purpose of activating the sectoral SyRB is the same as for the current measure under Article 458 CRR. The SyRB is aimed at enhancing the resilience of Belgian IRB banks to the systemic risk present in residential real estate markets. A number of vulnerabilities have been identified in the Belgian residential real estate sector.[4]

First, there is a protracted expansion of mortgage lending to Belgian households, combined with low risk weights applied to these exposures by IRB banks. Total outstanding mortgage loans by Belgian banks to Belgian households increased from 15% of banks' total assets to about 21%between March 2020 and September 2021, according to the Nationale Bank van België/Banque Nationale de Belgique. Average growth in mortgage lending to Belgian households stood at 5.5% over the same period. Microprudential risk weights of IRB banks within the scope of the measure for these exposures were among the lowest in the EU, at 9.8% on average.

Second, house prices have continued to increase strongly, exacerbating overvaluation. House prices grew by 5.8% year on year on average in nominal terms in 2020, and by 7.9% in the first half of 2021. Measures of house price valuation, though they need to be taken with caution due to model uncertainty, show signs of an overvaluation by about 15-20% in 2021.[5]

Third, household indebtedness is elevated and increasing (64.3% of GDP in the second quarter of 2021), according to the Nationale Bank van België/Banque Nationale de Belgique. Even though lending standards have tightened since the introduction of supervisory expectations in January 2020, a large share of loans are still relatively risky. Moreover, intense competition between credit institutions on the mortgage loan market owing to low profitability in the context of low interest rates might be leading to some underpricing of risks, according to the Nationale Bank van België/Banque Nationale de Belgique.

These vulnerabilities could lead to a severe downturn in the Belgian residential real estate market, which could have a substantial impact on the solvency positions of Belgian credit institutions. The Nationale Bank

---

4 See also "**Vulnerabilities in the residential real estate sectors of the EEA countries**", ESRB, February 2022.

5 See footnote 4.

van België/Banque Nationale de Belgique assesses that the size of the exposures targeted by the SyRB could give rise to a serious risk to the financial system and the real economy in Belgium, that credit losses might be significant under an adverse macroeconomic scenario, and that it could lead to negative spillover effects to other exposures. A countervailing factor is evidence of somewhat improved lending standards owing to the prudential expectations on lending standards put into place in January 2020.

Certain measures in addition to the Article 458 CRR measure have been put in place to mitigate financial stability risks resulting from these vulnerabilities. A supervisory expectation on lending standards was introduced in January 2020, setting LTV limits for various loan segments, as well as limits on loans combining a high LTV ratio (above 90%) with high borrower indebtedness (a DSTI ratio above 50% or debt-to-income (DTI) ratio above 9%). In addition, the Nationale Bank van België/Banque Nationale de Belgique has a monitoring framework for credit standards, consisting of a semi-annual survey collecting data on lending standards and other parameters of the Belgian mortgage market portfolios of banks and insurers, as well as an informal communication channel to ensure that banks maintain sound lending standards. The countercyclical capital buffer (CCyB) currently stands at 0% (since April 2020) owing to the pandemic-related economic situation.

Effectiveness and proportionality

The Nationale Bank van België/Banque Nationale de Belgique calibrated the sectoral SyRB on the basis of credit losses under stress scenarios for the residential real estate market. It used crisis events in other European countries to estimate probabilities of default and loss given default ratios of residential mortgage portfolios under stress scenarios. The scenarios suggest that the macroprudential buffer accumulated as a result of the current measure under Article 458 CRR is sufficient to cover simulated losses at the sectoral level. While the application of the scenarios to the latest available data would suggest that a lower macroprudential buffer (by €200 million) could be sufficient to cover the risk, the Nationale Bank van België/Banque Nationale de Belgique decided to take a cautious approach and keep requirements at the current level. This implies a sectoral SyRB of 9% to replace the current Article 458 CRR measure with an equivalent effect on capital at sectoral level. The main reason for this cautious approach is that, overall, risks are assessed to be broadly stable with, on the one hand, increasing medium-term vulnerabilities from a dynamic residential real estate market and, on the other, improving lending standards for new loans. However, default rates might still be distorted by existing support measures, and it remains to be seen whether recently observed improvements in risk metrics following the prudential expectations introduced in January 2020 are sustainable.

Should banks start taking substantial losses owing to rising defaults or significant debt restructuring, the Nationale Bank van België/Banque Nationale de Belgique will consider the immediate withdrawal of the proposed measure. According to the Nationale Bank van België/Banque Nationale de Belgique, this will ensure that banks which recognise losses can provide sustainable solutions to over-indebted consumers, thereby reducing risks in the residential real estate market that would stem from a sharp rise in payment defaults. The proposed measure is complementary to the prudential expectations, as the latter mainly address risks pertaining to flows of new loans.

The total impact of the sectoral SyRB on IRB banks' CET1 capital is estimated by the Nationale Bank van België/Banque Nationale de Belgique to be €1.9 billion, the same as the impact of the current Article 458 CRR measure. While the two measures target the same risk, the impact of the shift from the Article 458 CRR measure to the sectoral SyRB may have a somewhat different impact on CET1 buffer requirements of individual institutions. According to the Nationale Bank van België/Banque Nationale de Belgique, these requirements range from 0.6 to 1.0 percentage points for the Article 458 CRR measure and from 0.3 to 1.3 percentage points for the sectoral SyRB. However, according to the Nationale Bank van België/Banque Nationale de Belgique, no credit institution would need to issue new capital to comply with them. No change in the risk-taking of individual banks is expected, as the prudential expectations provide a backstop.

The ESRB is of the view that the new sectoral SyRB is effective and proportionate. It acts on the objective of enhancing the resilience of Belgian IRB banks to potential (severe) downward corrections in residential real estate markets by increasing their CET1 capital in relation to exposures to these markets. Current risk weights for lending secured by residential real estate in Belgium are deemed too low from a macroprudential perspective. A sectoral SyRB of 9% is considered commensurate with the intensity of, and potential losses stemming from, the above-mentioned risks in the Belgian financial system, and with the risk covered by the current Article 458 CRR measure, which will expire at the start of the proposed sectoral SyRB. This is also confirmed by the most recent ESRB assessment of vulnerabilities in residential real estate markets[6], which considers the current macroprudential stance appropriate and sufficient to address vulnerabilities of the residential real estate sector in Belgium. As the scope of the sectoral SyRB does not change compared with that of the Article 458 CRR measure currently in place, this assessment is still valid. Moreover, it is not expected to have a strong impact on credit supply as its capital impact is, on aggregate, similar to that of the current Article 458 CRR measure. The Nationale Bank van België/Banque Nationale de Belgique has not observed any substantial leakage to the non-bank sector under the current Article 458 CRR measure and does not expect this to occur under the proposed sectoral SyRB.

Other measures in the CRD

The proposed measure does not cover risks covered by Article 130 CRD. The CCyB has been released in the context of the COVID-19 pandemic. According to the Nationale Bank van België/Banque Nationale de Belgique, a potential activation of the CCyB could cover other cyclical risks and potential spillover and second-round effects from residential real estate developments.

Following the latest amendment to the CRD, the cumulated G-SII/O-SII buffer and SyRB rates determine the procedure to be followed. As set out under Article 133(12) CRD, since the proposed sectoral SyRB is higher than 5%, it must be authorised by the European Commission. Additionally, pursuant to Article 131(15), an authorisation will be required for the O-SII buffer, as the sum of the SyRB and O-SII buffer rates on the relevant exposures exceeds 5%.[7] Thus the ESRB must be notified of any change in the O-SII buffer rates of the affected institutions and must then provide the Commission with an opinion on whether the O-SII buffer is deemed appropriate.[8] The table below provides

---

[6] See footnote 4.

[7] See Article 131(15) CRD.

[8] See Article 131(5a) CRD.

an overview of currently applicable O-SII requirements of the Belgian credit institutions covered by the proposed measure.

Name of institution	O-SII consolidation level	O-SII buffer plus sectoral SyRB requirements on relevant exposures to residential real estate
BNP Paribas Fortis SA/NV	1.50%	10.50%
KBC Bank NV	1.50%	10.50%
Belfius Bank SA/NV	1.50%	10.50%
ING Belgium NV	1.50%	10.50%
Argenta Spaarbank SA/NV	0.75%	9.75%
AXA Bank Belgium	0.75%	9.75%
Crelan	-	9.00%
CBC Banque	-	9.00%
vdk bank	-	9.00%

On the basis of the information provided by the Nationale Bank van België/Banque Nationale de Belgique, the ESRB is of the view that the combined buffer requirements are appropriate. The sectoral SyRB covers risks of exposures to the Belgian residential real estate market only, whereas the O-SII buffer addresses the systemic footprint of specific banks in the domestic market. While banks with a large share in the domestic real estate market will be affected more heavily by the sectoral SyRB and will also receive a higher O-SII score[9] and therefore potentially a higher O-SII buffer, the objectives of the two buffers are clearly different and there is no meaningful overlap between them.

Conclusions

The ESRB is of the view that the proposed sectoral SyRB is appropriate to address the identified risks and to replace the currently active Article 458 CRR measure, which will expire at the time of activation of the proposed measure. It does not entail disproportionate adverse effects on financial stability in Belgium or the EU. The effects of the proposed measure are similar to those of the currently active Article 458 CRR measure. The sectoral SyRB is not expected to form or create an obstacle to the proper functioning of the internal market, as also not observed in the case of the currently active measure. Its focus is Belgian residential real estate exposures of IRB banks and it does not address risks which could be covered by Articles 130 or 131 CRD. The combined O-SII buffer and SyRB rates are also assessed to be appropriate. The reciprocation request in the notification will be dealt with in a separate note.

[9] In step 1 of the European Banking Authority O-SII identification methodology, an indicator of share in the market for loans to households (which include loans to households for house purchase) has 8.33% weight in the overall systemic importance scoring. See "**Annual disclosure regarding the designation of and capital surcharges on Belgian O-SIIs (1 December 2021)",** Nationale Bank van België/Banque Nationale de Belgique, 2021.