Dear Mr Mazzaferro,

In accordance with article 18(3) of Regulation (EU) No 1092/2010, I am writing to share with you my views on the Warning issued by the ESRB General Board on medium-term vulnerabilities in the residential real estate sector of Luxembourg.

In the context of its systematic and forward-looking Union-wide assessment of vulnerabilities relating to residential real estate, the ESRB has identified in eight Member states- among them Luxembourg- certain medium term vulnerabilities as a source of systemic risk to financial stability.

From a macroprudential perspective, the ESRB considers the main vulnerabilities in Luxembourg to be a combination of high residential real estate prices and increasing household indebtedness.

According to the ESRB, the direct risks to the banking system related to residential real estate vulnerabilities seem limited at present. The ESRB recognises that on average, Luxembourg banks are well-capitalised and have relatively low exposures to residential real estate. Moderate loan-to-value and debt-service-to-income ratios as well as the high levels of financial assets held by Luxembourg households are further mitigating factors. The ESRB acknowledges that the Luxembourg authorities have taken a series of measures in relation to residential real estate aimed at increasing the resilience of the banking sector.
The Banque centrale du Luxembourg (BCL) and the Commission de surveillance du secteur financier (CSSF) have indeed been closely monitoring the developments related to the Luxembourg residential real estate sector for more than a decade. The developments related to the Luxembourg residential real estate sector are regularly on the agenda of the Comité du Risque Systémique. The analysis conducted by the Luxembourg authorities has not identified an imminent threat to financial stability from the domestic residential real sector. This is also acknowledged in the ESRB warning.

The ESRB warning highlights that a risk to financial stability could potentially materialise in the medium term in the event of an adverse economic shock. This potential threat to financial stability is not unique to Luxembourg but exists also in other Member states. The Luxembourg authorities are fully aware of that risk and for that very reason, have followed closely the developments related to the Luxembourg residential real estate sector. They stand ready to take measures as deemed appropriate on the basis on factual evidence. Over the past decades, the continuous increase in residential real estate prices in Luxembourg has been driven by market fundamentals. In particular, demographic factors and a strong economic growth are the main drivers behind the strong housing demand. The Comité du Risque Systémique will duly take into account the ESRB analysis in the ongoing monitoring process, in addition to the aforementioned national specificities.

Luxembourg authorities, under the lead of the Comité du Risque Systémique, have taken so far a series of preventive measures to mitigate potential risks related to residential real estate. They will continue to assess whether further measures are warranted.

You may rest assured that the Luxembourg authorities will remain vigilant to the medium-term risk identified by the ESRB and will continue to closely monitor developments in the residential real estate sector in Luxembourg. The Luxembourg authorities will keep the ESRB informed about any further measures taken.

I would appreciate if you published this letter alongside the publication of the Warning.

Yours sincerely,

Pierre GRAMEGNA
Minister of Finance