



ECB-CONFIDENTIAL

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10 July 2019
ESRB/2019/0172

Warning of the European Systemic Risk Board of 27 June 2019 on medium-term vulnerabilities in the residential real estate sector in the Czech Republic (ESRB/2019/10)

Dear JUDr. Schillerová,

This is to inform you that on 27 June 2019, the General Board of the European Systemic Risk Board (ESRB) adopted Warning of the European Systemic Risk Board of 27 June 2019 on medium-term vulnerabilities in the residential estate sector in the Czech Republic (hereinafter "Recommendation ESRB/2019/10"). The General Board of the ESRB also adopted four other country-specific ESRB Warnings, addressed to four other Member States in which vulnerabilities relating to the residential real estate sector as a source of systemic risk have also been newly identified as not being sufficiently addressed. Furthermore, on the same date, the General Board of the ESRB adopted country-specific ESRB Recommendations to six Member States that received country-specific ESRB Warnings in 2016 on medium-term vulnerabilities in their respective residential real estate sector, and in which vulnerabilities relating to the residential real estate sector as a source of systemic risk are still not being sufficiently addressed.

Vulnerabilities relating to the residential real estate can be a source of systemic risk and may affect financial stability both directly and indirectly. In 2016, the ESRB conducted a Union-wide assessment of the vulnerabilities relating to residential real estate¹. This assessment enabled the ESRB to identify a number of

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medium-term vulnerabilities in several countries as sources of systemic risk to financial stability, which led to the issuance of warnings to eight countries: Belgium², Denmark³, Luxembourg⁴, the Netherlands⁵, Austria⁶, Finland⁷, Sweden⁸ and the United Kingdom⁹.

The ESRB has recently concluded a systematic and forward-looking European Economic Area (EEA)-wide assessment of vulnerabilities relating to residential real estate. As a result of this assessment, the ESRB has identified certain medium-term vulnerabilities in the residential real estate sector in the Czech Republic as a source of systemic risk to financial stability, that have not been sufficiently addressed and which may have the potential for serious negative consequences for the real economy. From a macroprudential perspective, the ESRB considers the main vulnerabilities to be the high overvaluation of house prices coupled with the high growth in housing credit and loose lending standards, against the backdrop of the non-legally-binding nature of the borrower-based measures currently available and in place.

The General Board of the ESRB, having assessed the results of the risk and policy analyses carried out, has concluded that the current macroprudential policy that is in place in the Czech Republic is partially appropriate and partially sufficient as regards the potential development of vulnerabilities in the residential real estate sector in the Czech Republic over the medium term. For this reason, the General Board of the ESRB decided to issue a Warning to the Czech Republic on medium-term vulnerabilities in its residential real estate sector.

In line with Article 18(2) of Regulation (EU) No 1092/2010¹⁰, I would hereby like to inform you that Warning ESRB/2019/10 will be published on the ESRB's website and later in the *Official Journal of the European Union*. In addition, in line with Article 18(3) of Regulation (EU) No 1092/2010, addressees of public warnings have the right to make public their views and reasoning on the matter. Should you wish to utilise this right, you are kindly invited to submit to the ESRB Secretariat any views and reasoning that you may have on the matter by 9 September 2019.


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- ¹ See 'Vulnerabilities in the EU Residential Real Estate Sector', ESRB, November 2016, available on the ESRB's website at www.esrb.europa.eu.
- ² Warning ESRB/2016/06 of the European Systemic Risk Board of 22 September 2016 on medium-term vulnerabilities in the residential real estate sector of Belgium (OJ C 31, 31.1.2017, p. 45).
- ³ Warning ESRB/2016/07 of the European Systemic Risk Board of 22 September 2016 on medium-term vulnerabilities in the residential real estate sector of Denmark (OJ C 31, 31.1.2017, p. 47).
- ⁴ Warning ESRB/2016/09 of the European Systemic Risk Board of 22 September 2016 on medium-term vulnerabilities in the residential real estate sector of Luxembourg (OJ C 31, 31.1.2017, p. 51).
- ⁵ Warning ESRB/2016/10 of the European Systemic Risk Board of 22 September 2016 on medium-term vulnerabilities in the residential real estate sector of the Netherlands (OJ C 31, 31.1.2017, p. 53).
- ⁶ Warning ESRB/2016/05 of the European Systemic Risk Board of 22 September 2016 on medium-term vulnerabilities in the residential real estate sector of Austria (OJ C 31, 31.1.2017, p. 43).
- ⁷ Warning ESRB/2016/08 of the European Systemic Risk Board of 22 September 2016 on medium-term vulnerabilities in the residential real estate sector of Finland (OJ C 31, 31.1.2017, p. 49).
- ⁸ Warning ESRB/2016/11 of the European Systemic Risk Board of 22 September 2016 on medium-term vulnerabilities in the residential real estate sector of Sweden (OJ C 31, 31.1.2017, p. 55).
- ⁹ Warning ESRB/2016/12 of the European Systemic Risk Board of 22 September 2016 on medium-term vulnerabilities in the residential real estate sector of the United Kingdom (OJ C 31, 31.1.2017, p. 57).
- ¹⁰ Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010 on European Union macro-prudential oversight of the financial system and establishing a European Systemic Risk Board (OJ L 331, 15.12.2010, p. 1).

The ESRB intends to monitor the risks identified in Warning ESRB/2019/10 and invites the Czech Republic to provide information, within one year from the publication of Warning ESRB/2019/10 in the *Official Journal of the European Union*, on the evolution of the vulnerabilities identified and on any policy measures that may have been taken in the Czech Republic in order to address these vulnerabilities. In this regard, it is important that national authorities in the Czech Republic have legally binding borrower-based measures at their disposal to provide them with the necessary powers to address potential financial stability vulnerabilities, including, in particular, powers to set legally binding limits to loan-to value ratios – and to either debt-to-income ratios or debt-service-to-income ratios, in combination with maturity limits – where necessary in relation to new housing loans. Only legally binding borrower-based measures would ensure that all credit providers, irrespective of their type or whether they are domestic or foreign, comply fully with the measures in place. In addition, when activating any measures to address the identified vulnerabilities, their calibration and phasing-in should take into account the position of the Czech Republic in the economic and financial cycles, and any potential implications as regards the associated costs and benefits.

Please also note that the following reports, adopted by the ESRB on 27 June 2019, will be made available electronically:

- “Methodologies for the assessment of real estate vulnerabilities and macroprudential policies – residential real estate”; and
- “Vulnerabilities in the residential real estate sectors of the EEA countries”.

Yours sincerely,


Francesco Mazzaferro

Head of the ESRB Secretariat

Enclosed:

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