



ECB-CONFIDENTIAL

Mr Bjarni Benediktsson
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Arnarhvoli vid Lindargotu
101 Reykjavik
Iceland

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ESRB/2019/0174

Warning of the European Systemic Risk Board of 27 June 2019 on medium-term vulnerabilities in the residential real estate sector in Iceland (ESRB/2019/13)

Dear Mr Benediktsson,

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 Iceland (hereinafter "Recommendation ESRB/2019/13"). 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 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.

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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).

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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 Iceland 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 vulnerability to be a high household indebtedness associated with the strong medium-term increase of house prices and potential overvaluation of house prices.

The General Board of the ESRB, having assessed the results of the risk and policy analyses carried out, has concluded that the current policy measures that are in place or available in Iceland are partially appropriate and partially sufficient to mitigate the identified systemic risks related to vulnerabilities in the residential real estate sector in Iceland. For this reason, the General Board of the ESRB decided to issue a Warning to Iceland 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/2019/13 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.

The ESRB intends to monitor the risks identified in Warning ESRB/2019/13 and invites Iceland to provide information, within one year from the publication of Warning ESRB/2019/13 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 Iceland in order to address these vulnerabilities. In this regard, while the ESRB acknowledges the initiatives taken as regards monitoring of residential real estate, further measures may be needed concerning lending to households with high DTI ratios. Iceland may therefore consider a pre-emptive implementation of explicit guidelines on income-based measures, either in the form of a recommendation or of legally-binding borrower-based measures. Income-based measures may help to better prevent households from becoming overly indebted, should the strong growth in house prices persist. Such measures could be particularly relevant, as the growth in house prices may have reduced the effectiveness of the cap on LTV ratios.

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).

Furthermore, when activating any measures to address the identified vulnerabilities, their calibration and phasing-in should take into account the position of Iceland in the economic and financial cycles, and 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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