

Notification template for borrower-based measures

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This notification will be made public by the ESRB once the relevant authorities have adopted and published the notified macroprudential measure¹.

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| 1. Notifying national authority and scope of the notification | | |
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| 1.1 | Name of the notifying authority | Czech National Bank |
| 1.2 | Country of the notifying authority | Czech Republic |
| 1.3 | Type of borrower-based measure | <input checked="" type="checkbox"/> Debt-service-to-income (DSTI) |
| 1.4 | Type of notification | <input checked="" type="checkbox"/> The upper limit on the DSTI ratio shall be abolished |

¹ On request by the notifying authority, it may be agreed with the Head of the ESRB Secretariat that this notification, or a part thereof, should not be published for reasons of confidentiality or financial stability.

| 2. Description of the measure | | |
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| 2.1 | Description of the measure | The upper limit on the ratio of the consumer's outgoings arising from the consumer's total debt to the consumer's net monthly income (hereinafter the " DSTI ratio ") shall be abolished with effect from 1. 7. 2023 |
| 2.2 | Definition of the measure | <p>The DSTI ratio means the ratio of the average monthly expenses arising from a consumer's total debt to net monthly income.</p> <ul style="list-style-type: none"> - The amount of a consumer loan secured by residential property means the principal of the loan agreed in the loan agreement; - a consumer's total debt means the sum of the loan provided and the consumer's other secured and unsecured loans from the relevant provider, as well as loans from another providers, including not drawn principal of these loans; - a consumer's net income means the amount of annual after-tax income prudently assessed as permanent on the basis of a provably documented income history for a sufficiently long period; - Details regarding definitions are set by Decree No. 399/2021 Coll. on credit ratios pursuant to Article 45a(6) of Act No. 6/1993 Coll., on the Czech National Bank, as amended by Act No. 219/2021 Coll., the Czech National Bank |
| 2.3 | Legal basis and process of implementation of the measure | <p>Legal basis:</p> <p><i>Act on CNB 6/1993, Article 45b:</i> the CNB shall be entitled to set an upper limit on LTV, DTI, DSTI as legally binding macroprudential measures</p> <p><i>Decree No. 399/2021 Coll., on credit ratios:</i> regulate manner of, and rules for calculating ratios and definitions of items included in the calculation</p> |

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| | | <p><i>The CNB shall be entitled to issue a provision of a general nature on setting, changing or cancelling upper limits on credit ratios:</i></p> <p>Process of implementation: The CNB regularly (at least twice a year) assesses consumer loans secured by residential property and the overall situation in the mortgage and residential property market. This is based on macroprudential analyses and information gathered in the course of the financial market supervision, the CNB issues:</p> <ul style="list-style-type: none"> - Provision of a general nature on setting upper limits on credit ratios according to Act No. 6/1993 Coll., on the Czech National Bank (since 2021), and - Recommendation on the management of risks associated with the provision of consumer loans secured by residential property (since 2015, hereinafter the “Recommendation”). Until 2021, the Recommendation contained a summary of recommended limits on selected credit ratios and a set of other rules, the observance of which constituted prudent behaviour when conditions on the financial market are taken into account. Since December 2021 the Recommendation contains selected conditions related to the provision of consumer loans secured by residential property, which are not regulated by the Act on the Czech National Bank and specified by the provision of a general nature, e.g. maximum maturity, acceptable methods of principal repayment, prudential practices regarding increasing the principal of an existing mortgage loan. |
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| 2.4 | Coverage | <p>Loan providers: The measure applies to entities authorised as an entrepreneur to provide consumer credit under Act No. 257/2016 Coll., on Consumer Credit.</p> <p>Loan applicants: The measure applies to natural persons applying for a consumer loans secured by residential property.</p> <p>Loan product: It applies to consumer loans secured by residential property provided to natural persons (individuals) and to consumer credit provided to natural persons (individuals) who have a consumer loans secured by residential property.</p> |
| 2.5 | Calibration | <p>The CNB uses three main approaches when setting upper limits on credit ratios: an indicator approach, a simulation approach and an expert approach.</p> <p>The indicator approach takes into account current and expected future developments linked to the CNB's macroeconomic forecast for the indicators defined in the Act on the CNB and other key indicators used to identify systemic risks to financial stability. The aim of the indicator approach is to recognise in good time whether conditions are being created on the mortgage and property markets for the formation or build-up of potential systemic risks. For simplicity, the individual indicators are combined into composite risk perception indicators based on the overlap of standard deviations and the deviation from the long-term average.</p> <p>The simulation approach helps to quantify whether the potential risks indicated by the above indicators can take on a systemic dimension. The approach is based on</p> |

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| | | <p>simulations in the household stress test with different upper limits on the credit ratios. This approach takes into account the current size and quality of the loan portfolio and simulates its future trends based on a combination of CNB projections consistent with the CNB macroeconomic forecast (the first two years of the simulation) and an extremely adverse scenario (the next three years). The simulations are thus conducted over a five-year horizon. The simulation outputs are the default rate, loss given default and the size of the expected absolute losses for different upper limits on the credit ratios. The simulation results depend largely on the narrative of the scenario and the riskiness of the initial mortgage portfolio.</p> <p>The expert approach takes into account all other factors, including market uncertainty or other policy setting. It is based on the analytical perspective and expert judgement of the Bank Board and the recommendations of the Monetary Department and Financial Market Supervision Department. This allows the broader macroeconomic conditions, the interaction between monetary and macroprudential policies, the specific nature of past or expected future adverse shocks, the rate of change in the risk of the existing portfolio, structural changes in the economy and so on to be incorporated into the decision.</p> |
| 3. Timing for the measure | | |
| 3.1 | Timing for the decision | 01/06/2023 |
| 3.2 | Timing for publication | 02/06/2023 |
| 3.3 | Disclosure | <p>The provision of a general nature disclosed on June 2, 2023 on the CNB website (link).</p> <p>Recommendation on the management of risks associated with the provision of consumer loans secured</p> |

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| | | by residential property disclosed on June 19, 2023 on the CNB website (link). |
| 3.4 | Timing for the application | 01/07/2023 |
| 3.5 | End date (if applicable) | The measure is not time-limited. However, under the Act on the CNB, the CNB has to review the reasons for setting upper limits on credit ratios at least once every six months, and assesses them in light of the existence and expected further evolution of the systemic risks. If there is a material change in these risks, the CNB will issue a new provision of a general nature or will amend or abolish the existing one. |
| 4. Reason for activation of the measure | | |
| 4.1 | Description of the macroprudential risk | |
| 4.2 | Indicators used for activation of the measure | |

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| 4.3 | Effects of the measure | |
| 5. Sufficiency, consistency and non-overlap of the policy response | | |
| 5.1 | Sufficiency of the policy response | <p>The potential risks associated with mortgage lending have lessened and the CNB does not expect significant growth in systemic risks stemming from the mortgage and property markets at the two-year horizon. Most of the factors defined in the Act on the CNB to identify those systemic risks are currently either at/below their long-term averages or heading towards them at the scenario horizon. In particular, there was a large decline in the volume of mortgage lending due to very low demand for these loans in response to high interest rates, and uncertainty about economic activity. Based on the CNB's macroeconomic spring forecast, domestic economic activity will be subdued in 2023 and return to higher growth in 2024 at the earliest. The risks to the forecast are considerable and tend to be in the direction of lower GDP growth. Similar developments are expected in the case of credit dynamics for both households and non-financial corporations, including mortgage loans (subdued in 2023, moderate growth in 2024). At the same time, the CNB has been communicating that monetary policy interest rates may remain at a higher level over a longer horizon than expected by the spring forecast. The potential highly risky loans should thus account for a low proportion of bank portfolios over these two years. In addition, results of stress test of households and the banking sector do not indicate the presence of significantly elevated systemic risk either.</p> |

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| | | Nevertheless, residential property prices in the Czech Republic remain significantly overvalued and the associated risk of a price correction persists. In this price environment, and with regard to the evolution of household income, there is still some risk of households becoming over-indebted, as less than 10% of households can safely debt-finance an average-price apartment. For these reasons, the CNB left the upper limit on the LTV ratio at 80% (90% for applicants under 36 years) and that on the DTI ratio at 8.5 (9.5) times net annual income. |
| 5.2 | Consistency of application of the policy response | The CNB responded to the decline in systemic risks associated with the provision of consumer loans secured by residential property and with property market, in accordance with the Act on CNB. The CNB acted in line with previous policy actions and risks development. |
| 5.3 | Non-overlap of the policy response | Still effective limit on DTI regulates the market in the same direction. |
| 6. Cross-border and cross-sector impact of the measure | | |

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| 6.1 | Assessment of cross-border effects and the likely impact on the Internal Market (Recommendation ESRB/2015/2 ²) | Cross-border effects are not expected |
| 6.2 | Assessment of leakages and regulatory arbitrage within the notifying Member State | |
| 6.3 | Request for reciprocation | |

² Recommendation of the European Systemic Risk Board of 15 December 2015 on the assessment of cross-border effects of and voluntary reciprocity for macroprudential policy measures (ESRB/2015/3) (OJ C 97, 12.3.2016, p. 9).

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| 6.4 | Justification for the request for reciprocation | |
| 7. Miscellaneous | | |
| 7.1 | Contact person(s)/mailbox at notifying authority | Zlatoše Komárková, +420 224 412 969, zlatuse.komarkova@cnb.cz Jiří Gregor, +420 224 412 647, jiri.gregor@cnb.cz |
| 7.2 | Any other relevant information | Please visit the following webpage for more information: https://www.cnb.cz/en/financial-stability/macroprudential-policy/requirements-for-ltv-dsti-and-dti-limits/ |
| 7.3 | Date of the notification | 10/07/2023 |