ESRB
European Systemic Risk Board
European System of Financial Supervision

Assessment Team on national macroprudential measures

Assessment of a measure taken in Belgium pursuant to Article 131 in combination with a measure pursuant to Article 133 of the Capital Requirements Directive

Introduction

On 18 July 2023 the European Systemic Risk Board (ESRB) Secretariat received a formal notification from the Nationale Bank van België/Banque Nationale de Belgique (NBB/BNB) of its decision to require certain institutions to maintain a buffer applicable to other systemically important institutions (O-SIIs), in accordance with Article 131 of the Capital Requirements Directive (CRD)[1]. The O-SII buffer will be applied to eight domestically established Belgian banks, with buffer rates ranging from 0.75% to 1.50%. From 1 January 2024 the O-SII buffer rate would increase for one of the institutions, while it would remain the same for the others.

Simultaneously, the ESRB also received a formal notification from the NBB/BNB of its decision to recalibrate the sectoral systemic risk buffer (sSyRB) rate starting from 1 April 2024. The sSyRB is imposed – on a consolidated, sub-consolidated and individual basis - on all internal ratings-based (IRB) bank retail exposures to natural persons secured by residential real estate (RRE) property whose collateral is located in Belgium, and it will be recalibrated to 6% from the current rate of 9%.

As the sum of the O-SII buffer rate and the sSyRB rate exceeds 5% for a number of institutions and a group of exposures, both before and after the downward recalibration of the sSyRB rate, the ESRB must issue an opinion as to whether the combined buffer is deemed appropriate, pursuant to Articles 131(15) and (5a) of the CRD. Following the issuance of the ESRB opinion, the European Commission must adopt an act authorising the setting or resetting of the O-SII buffer and sSyRB rates if it is satisfied that the combined buffer 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, forming or creating an obstacle to the proper functioning of the Internal Market.

On 16 February 2022 the ESRB issued an opinion stating that the setting of the sSyRB rate applicable in Belgium was justified, proportionate, effective and efficient.[2] In addition, the combined sSyRB and O-SII buffer rates in place at that time were assessed as proportionate and effective for all credit institutions falling within the scope

[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] See the ESRB **Opinion** of 16 February 2022 and the **Background note** of 21 February 2022.

of these two measures. The ESRB also recommended reciprocation of the sSyRB in order to avoid leakages and regulatory arbitrage.

On 28 July 2022 the ESRB issued an opinion assessing that the setting of an O-SII buffer by the NBB/BNB applicable to the same eight credit institutions, being cumulative with the existing sSyRB to which six[3] of these credit institutions had already been subject, was appropriate and effective in addressing the identified risks.[4] In last year's assessment, the eight institutions subject to the O-SII buffers were KBC Groep NV, BNP Paribas Fortis SA/NV, ING Belgium NV, Belfius Bank SA/NV (with a 1.5% O-SII buffer rate), Euroclear Holding, The Bank of New York Mellon, Investeringsmaatschappij Argenta and Crelan SA (with a 0.75% O-SII buffer rate). These rates were cumulative to the already applicable 9% sSyRB imposed – on a consolidated, sub-consolidated and individual basis - on all IRB bank retail exposures to natural persons secured by RRE property whose collateral is located in Belgium.

The role of the Assessment Team is to prepare a draft opinion, from a macroprudential and financial stability perspective, on the appropriateness of the proposed measures, with regard to relevant requirements under the CRD and the Capital Requirements Regulation (CRR)[5]. Pursuant to Article 131(15) in conjunction with Article 131(5a) of the CRD, the O-SII buffer in combination with the SyRB rate should not entail disproportionate adverse effects on financial stability in other Member States, or in the European Union as a whole, forming or creating an obstacle to the proper functioning of the Internal Market.

Description of the proposed measures

The setting of the O-SII buffer rates in Belgium by the NBB/BNB applies to eight domestically established Belgian banks. Two of these are subsidiaries of entities established in another EU Member State. The identification of the O-SII buffers is based on the size of the institution, its importance to the Belgian economy, its complexity, its cross-border activity and its interconnectedness with the financial system. The identification of O-SIIs follows the European Banking Authority (EBA) guidelines EBA/GL/2014/10[6]. Following this methodology, seven institutions had a score automatically designating them as O-SIIs. Additionally, Crelan SA was included in the list of O-SIIs by applying supervisory judgement, as its alternative O-SII score (based on optional indicators with a domestic scope) is above the threshold. The new O-SII buffers will be published on 1 December 2023 and will be applicable from 1 January 2024.

Compared with the previous setting of O-SII buffers applicable since 1 January 2023, the situation has only changed for one of the identified O-SIIs. The O-SII buffer rate of Euroclear Holding will increase from 0.75% to 1.5%, as this institution has seen its balance sheet increase strongly with its cross-border liabilities being inflated owing to the international sanctions against Russian entities. The other O-SII buffers remain unchanged. Of the eight banks subject

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[3] When looking at the institutions at the highest level of consolidation on which the buffers are applicable. The sSyRB also applies to AXA Bank Belgium, a subsidiary of Crelan SA on the sub-consolidated level.

[4] See ESRB **Opinion** and **Background note** of 28 July 2022.

[5] 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).

[6] Guidelines on the criteria to determine the conditions of application of Article 131(3) of Directive 2013/36/EU (CRD) in relation to the assessment of other systemically important institutions (O-SIIs) (EBA/GL/2014/10, p. 1).

to an O-SII buffer, two banks are not subject to a sectoral SyRB, as they don't use IRB models to determine capital requirements for residential mortgages.[7]

As of 1 April 2024, the NBB/BNB also intends to recalibrate the 9% sSyRB rate imposed on all IRB bank retail exposures to natural persons secured by RRE property whose collateral is located in Belgium, to 6%. The 9% sSyRB rate has been applicable since 1 May 2022. The recalibration of the rate to 6% takes into account the improvement in the loan-to-value (LTV) profile of the stock of RRE loans, which is also due to the introduction of NBB/BNB prudential expectations in 2020 and decreasing signs of overvaluation in housing prices, which lowers the magnitude of potential losses on residential mortgage portfolios. The sSyRB rate continues to apply to nine domestically established Belgian banks[8], of which two are subsidiaries of entities established in another EU Member State.

Risks addressed through the proposed measures

The aim of the O-SII buffer setting is to reduce risks posed by institutions whose failure would have a significant negative impact on the domestic financial system or the real economy. Capital buffers reduce the probability of failure of O-SIIs, which may be desirable given the high economic and social cost of their failure. In addition, capital buffers require O-SIIs to internalise externalities they impose on the financial system and the real economy, and the buffers may provide incentives for O-SIIs to reduce their systemic importance. The Belgian banking sector is large (around 235% of the national GDP) and highly concentrated, with the four largest banks representing 76% of the sector's total assets and the eight identified O-SIIs representing almost 98%. The identified O-SIIs are institutions of domestic systemic importance, given that their total assets range from 7% to 60% of Belgian GDP. They are also important in terms of credit provisioning and deposit taking for the Belgian economy or global custodian services (The Bank of New York Mellon) and activities as an international central securities depository (Euroclear Holding).

The sSyRB aims to enhance the resilience of Belgian IRB banks to the systemic risk present in RRE markets. The NBB/BNB assessed that in the event of a significant price correction for RRE or a major shock to unemployment, banks may suffer major credit losses on their mortgage portfolios. While the level of the risk is assessed to have decreased since 2022, it remains significant. The latest risk assessment shows (i) the continued expansion and significant size of banks' exposures to mortgage lending to Belgian households, along with risk weights applied by IRB banks whose levels may not be commensurate with the level of systemic risk these exposures entail; (ii) persistent but decreasing signs of overvaluation and downside risks in housing prices; (iii) persistently high household indebtedness; and (iv) improving credit quality.

The downward recalibration of the sSyRB rate is due to improving credit quality and decreasing signs of overvaluation of housing prices. After having increased to 10% in the third quarter of 2021, the year-on-year nominal growth rate of housing prices decelerated in 2022 and was 4% in the first quarter of 2023. In real terms, on a year-on-year basis, the growth rate has been negative since the second quarter of 2022. In the past, RRE price developments

[7] The six banks affected by a combined O-SII buffer and sectoral SyRB requirement are KBC Bank NV, BNP Paribas Fortis SA/NV, ING Belgium NV, Belfius Bank SA/NV, Argenta Spaarbank SA/NV and Crelan SA. The sSyRB also applies to AXA Bank Belgium, a subsidiary of Crelan SA.

[8] The nine institutions include Crelan SA on the consolidated level and AXA Bank Belgium, its subsidiary, on the sub-consolidated level.

have been more dynamic than justified by changes in fundamentals, leading to signs of persistent overvaluation in the Belgian RRE market. While remaining sizeable, the computed overvaluation decreased recently; the model used by the NBB/BNB suggested an overvaluation of RRE prices close to 20% in 2021, whereas it fell back to 12% in the first quarter of 2023. The other important factor in the recalibration of the sSyRB rate was the introduction of the NBB/BNB's prudential expectations[9] regarding new mortgage loans in 2020, which has led to a tightening in lending conditions. Given the high new production amount until mid-2022, the expectations had observable effects also on the entire mortgage stock. Hence, the share of loans in the portfolios with current LTV metrics higher than 80% decreased from 25% at the end of 2019 to 15% at the end of 2022. The share of outstanding loans combining an LTV higher than 90%, a debt service-to-income (DSTI) ratio higher than 30% and a maturity longer than 20 years declined from 16.6% at the end of 2019 to 12.7% at the end of 2022. Over the same period, the share of outstanding loans combining an LTV higher than 90% and a DSTI ratio higher than 50% declined from 6.2% to 3.9%. The positive impact of the measures on the loan stock's risk profile is expected to be even greater by the application date of the new sSyRB rate.

According to Article 133(8) of the CRD, the SyRB should not be used to address risks that are covered by the O-SII buffers, as detailed in Articles 130 and 131 of the CRD. The objectives of the two buffers are clearly different in Belgium and there is no meaningful overlap between them. In particular, the sSyRB only covers risks of exposures to the Belgian RRE market, whereas the O-SII buffer addresses the systemic footprint of specific banks in the domestic market.

Effectiveness and proportionality

The Assessment Team considers the O-SII buffers to be effective and proportional. The O-SII buffers applicable to Belgian institutions were calibrated accounting for the institutions' systemic importance. To this end, Belgian O-SIIs were allocated to two buckets, applying a 1.5% and a 0.75% O-SII buffer rate to these buckets. Furthermore, the calibration of the O-SII buffer levels explicitly accounted for a level playing field and internal market considerations. Given the above considerations, the imposed levels of the O-SII buffers are expected to be both effective and proportional.

The sSyRB measure has also been assessed to be effective and proportional. It directly increases CET1 capital requirements of IRB banks for RRE portfolios, for which microprudential risk weights are deemed too low compared with the systemic risks observed in the RRE markets. The measure targets the stock risks in banks' RRE exposures by building resilience in the banking sector to overcome a severe downturn scenario. No signs of any strong impact on overall credit supply and, indirectly, on the real economy have been observed during the period of application of the capital buffer. No signs of any disruption of the Single Market through cross-border spillovers have been observed either. These impacts are not expected to change when reducing the sSyRB rate. The calibration has been based on an assessment of credit losses under stress scenarios for the real estate market. These scenarios stress both probabilities of default (using crisis episodes in other European countries as a benchmark) and loss given defaults (through the application of a severe add-on). Taking into account the improvement in the LTV profile of the stock of RRE loans and lower overvaluation in housing prices, the NBB/BNB updated the sensitivity/scenario analysis with a

[9] See the **press release** of the NBB/BNB about the prudential expectations

somewhat reduced stress on loss given default. This update confirmed that microprudential capital requirements implied by microprudential risk weights remain insufficient to cover all potential losses under severe macroprudential stress scenarios but that a buffer rate of 6% rather than 9% would be sufficient to cover the simulated losses at the sector level. The total impact of the proposed measure (6% sSyRB) on IRB banks' CET1 capital is estimated at €1.3 billion, compared with €2.0 billion if the 9% buffer rate were to be maintained. The sSyRB remains significant and corresponds to a 49% increase in the capital buffer compared with the microprudential CET1 capital requirements for this portfolio.

In addition, the overall resilience of banks is not expected to decrease with the sSyRB recalibration, as the Belgian authorities also intend to activate the countercyclical capital buffer (CCyB) from 1 April 2024 at the 0.5% level and to increase it to 1.0 % from 1 October 2024. Due to the activation of the CCyB, the combined buffer requirement is expected to be higher than before the downward recalibration of the sSyRB. The overall macroprudential buffer requirement is expected to increase from €2.0 billion (only 9% sSyRB) to €2.5 billion as of April 2024 (€1.3 billion for sSyRB and €1.2 billion for CCyB) and to €3.6 billion as of October 2024 (€1.3 billion for sSyRB and €2.3 billion for CCyB). Overall, the downward recalibration of the sSyRB and the activation of the CCyB will lead to a change in the composition of capital buffers, reflecting a shift of risks from RRE and household exposures to corporate exposures. The increased systemic risk in corporate exposures comes from high inflation and rising interest rates, whereas households are shielded by wage indexation and a high share of loans with fixed interest rates (or with long fixation periods).

Overall, on the basis of the information provided by the NBB/BNB, the ESRB considers that the combined O-SII buffer and sSyRB requirements are effective and proportional.

Conclusions

The ESRB is of the view that the proposed combined buffer consisting of the sSyRB and the O-SII buffers for the institutions concerned is appropriate for addressing the identified risks. It does not entail disproportionate adverse effects on financial stability in Belgium or in the European Union, nor is it expected to form or create an obstacle to the proper functioning of the Internal Market. This applies also after the recalibration of the sSyRB applicable from 1 April 2024.