

WARNING OF THE EUROPEAN SYSTEMIC RISK BOARD
of 22 September 2016
on medium-term vulnerabilities in the residential real estate sector of Austria
(ESRB/2016/05)
(2017/C 31/02)

THE GENERAL BOARD OF THE EUROPEAN SYSTEMIC RISK BOARD,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to 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 ⁽¹⁾, and in particular Articles 3 and 16 thereof,

Whereas:

- (1) Past experience in many countries shows that the manifestation of residential real estate vulnerabilities may lead to significant risks to domestic financial stability and serious negative consequences for the real economy, as well as potentially leading to negative spill-overs to other countries.
- (2) The European Systemic Risk Board (ESRB) has recently concluded a systematic and forward-looking Union-wide assessment of vulnerabilities relating to residential real estate. In this context, the ESRB has identified in eight countries certain medium-term vulnerabilities as a source of systemic risk to financial stability, which may have the potential for serious negative consequences for the real economy.
- (3) The ESRB's vulnerability assessment highlights the following for Austria:
 - a. Residential real estate prices in Austria have been rising rapidly, particularly since 2011. Until recently, house price dynamics were much stronger in Vienna than in the rest of Austria. However, annual house price growth outside of Vienna has been significant of late, surpassing that in Vienna. These developments have led to a level of real estate prices that appear to be above fundamentals compared to the long-term development of domestic fundamentals, particularly in Vienna ⁽²⁾. However, in the rest of the country, house prices are broadly in line with fundamentals according to Oesterreichische Nationalbank (OeNB) estimates.
 - b. More recently, the strong house price dynamics have coincided with robust mortgage credit growth. Results of an OeNB survey on lending standards indicate a decline in lending standards. Moreover, they show that the share of new mortgage borrowers with elevated debt-to-income ratios and loan-to-value ratios has been increasing. However, these results from the OeNB survey data should be interpreted cautiously given the large variance of survey results between banks, the small sample size and changing sample composition. But, in general, households that become highly indebted relative to income or the value of their property could be particularly vulnerable to economic shocks such as an increase in unemployment or a fall in household incomes or residential real estate prices. Under such circumstances, households may find it more difficult to service their debts and the number of mortgage defaults may increase leading to direct credit losses to banks, especially in the event of a fall in residential real estate prices. Moreover, if an adverse scenario for the economy does materialise, the associated negative household income and wealth effects may reinforce the initial shock, further enhancing the negative direct and indirect effects on financial stability (e.g. if households need to reduce consumption in order to service their mortgage loans). More information on lending standards based on a broader sample of financial intermediaries is needed to assess the systemic impact of potentially deteriorating lending standards.
 - c. In general, rapid residential real estate price growth that surpasses household income growth, such as is recently observed in Austria, make it more difficult for households to become homeowners, and can lead to an overall increase in household indebtedness and/or an increase in the group of households with elevated debt levels. Moreover, given robust credit and house price dynamics, there is a risk of a further deterioration of lending standards.

⁽¹⁾ OJ L 331, 15.12.2010, p. 1.

⁽²⁾ Based on estimates from the Oesterreichische Nationalbank (OeNB) and the European Central Bank (ECB).

- d. Austrian banks' mortgage exposures are low in comparison to other Union countries. This is related to the low homeownership rate ⁽¹⁾ and the moderate share of mortgage holders among homeowners in Austria. However, the total exposures of Austrian banks to real estate activities, also including loans to the construction sector etc., are somewhat higher in comparison to other Union countries. The average risk weights for Austrian banks that apply internal ratings-based models are well above the Union average. This makes the Austrian banking sector relatively less vulnerable to potential direct risks from the residential real estate sector. However, it should be noted that the overall average capitalisation of Austrian banks is slightly below the Union average.
- e. When analysing the nature of the identified vulnerabilities in Austria, there are both mitigating and aggravating factors. Aggravating factors include a significant share of variable rate loans (for both new loans and in the stock of existing loans) as well as existing foreign currency loans on housing, which expose households to interest rate and exchange rate risks, respectively. However, the share of mortgage loans with a variable interest rate or issued in foreign currency has been declining. Moreover, several analyses show that particularly borrowers with foreign currency loans on housing in Austria hold considerable risk buffers that mitigate related vulnerabilities. Other important risk mitigating factors include a relatively low home ownership rate, which has been stable for decades, combined with a well-developed rental market and an overall moderate level of household indebtedness. Moreover, most mortgages are amortising and debt tends to be held by wealthier households.
- f. The ESRB notes the measures introduced by the Austrian authorities, including the expectations on sustainable lending standards that have been communicated to banks ⁽²⁾. In addition, the Austrian Financial Market Stability Board (FMSB) has advised the Ministry of Finance to extend the macroprudential toolkit for borrower-based macroprudential instruments in the field of real estate financing to ensure that the FMSB can act on systemic risks arising from unsustainable real estate market developments ⁽³⁾. Residential real estate prices and mortgage credit are growing robustly, there are groups of households with elevated debt levels and there is some evidence of weakening credit standards. While the policy measures that have been taken by the Austrian authorities are appropriate given the nature of residential real estate vulnerabilities in Austria, they may not be sufficient to fully address them,

HAS ADOPTED THIS WARNING:

The ESRB has identified medium-term vulnerabilities in the residential real estate sector of Austria as a source of systemic risk to financial stability, 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 robust growth, particularly recently, in residential real estate prices and mortgage credit and the risk of a further loosening in lending standards.

Done at Frankfurt am Main, 22 September 2016.

Francesco MAZZAFERRO

Head of the ESRB Secretariat

On behalf of the General Board of the ESRB

⁽¹⁾ Especially in Vienna homeownership is low — 82 % of households are renters.

⁽²⁾ Following the ESRB's decision to issue this warning, the Austrian FMSB discussed sustainable lending standards in residential real estate during its meeting on 23 September 2016.

⁽³⁾ The FMSB's Advice is available publicly: <https://www.fmsg.at/en/publications/warnings-and-recommendations/advice-2-2016.html>